

Applicants
S A Pearson
Sixth Statement
"SAP6"
26 November 2009

IN THE HIGH COURT OF JUSTICE

Claim No. 7942 of 2008

CHANCERY DIVISION

COMPANIES COURT

**IN THE MATTER OF LEHMAN BROTHERS INTERNATIONAL
(EUROPE) (in administration)**

AND IN THE MATTER OF THE INSOLVENCY ACT 1986

**SIXTH WITNESS STATEMENT
OF
STEVEN ANTHONY PEARSON**

I, STEVEN ANTHONY PEARSON, of PricewaterhouseCoopers LLP, Plumtree Court, London EC4A 4HT, state as follows.

A. INTRODUCTION

- 1 I am a licensed insolvency practitioner and a partner in PricewaterhouseCoopers LLP ("**PwC**"), a firm of accountants at the above address. My partners, Anthony Victor Lomas, Michael John Andrew Jervis, Dan Yoram Schwarzmann and I are the joint administrators of Lehman Brothers International (Europe) ("**LBIE**") (in administration) (together the "**Administrators**" and each an "**Administrator**"). We were appointed as such by order of Mr Justice Henderson on 15 September 2008. I am duly authorised to make this witness statement on behalf of LBIE and the other Administrators.
- 2 One or more of the Administrators, together with other partners in PwC, are also the joint administrators appointed in respect of a further eighteen

Lehman companies in the UK (together with LBIE, the "**Lehman Administration Companies**"). Partners in PwC have also been appointed as liquidators of various other Lehman companies in the UK.

- 3 There is now shown to me a paginated bundle of copy documents, marked "**SAP6**", to which I refer in this witness statement. Where no cross reference to the paginated bundle is provided and where there is no other indication of the source of my information or belief, the contents of this witness statement are derived from facts and matters which are within my own knowledge and belief. These facts and matters have been learned either as a result of the work undertaken by me as one of the Administrators of the Lehman Administration Companies, or they have been provided to me either by my partners and colleagues at PwC involved with the administration of the Lehman Administration Companies, or by the employees of the Lehman Administration Companies who are still available to the Administrators, or by the Administrators' legal advisers, Linklaters LLP ("**Linklaters**").

- 4 I make this witness statement in support of the Administrators' application (the "**Application**") for an order in connection with the distribution or appropriation of assets held on trust by LBIE. In particular, the Administrators seek an Order, pursuant to paragraph 63 of Schedule B1 to the Insolvency Act 1986 and/or under the Court's inherent jurisdiction, that, having given not less than six weeks' notice of the bar date referred to below in various specified ways, after 26 February 2010 (the "**Bar Date**") has passed, to the extent that there exist no valid and enforceable "Security Interests" (as defined in the Ordinary Application by which this Application is made) in respect of the relevant "Trust Assets" (as defined in the Ordinary Application), the Administrators be at liberty to procure that LBIE do, and LBIE be at liberty to:
 - 4.1 "Distribute" (as defined in the Ordinary Application) Trust Assets to those persons who, on the basis of the information available to LBIE and the Administrators at the time of such distribution, are entitled to them; and

4.2 “Appropriate” (as defined in the Ordinary Application) such Trust Assets as LBIE is, on the basis of the information available to LBIE and the Administrators at the time of such appropriation, entitled to Appropriate.

5 The remainder of this witness statement is set out under the following headings:

- B. Trust Property
- C. Court applications made to date in relation to the Administrators’ dealings with and the return of Trust Property
- D. Efforts made thus far to establish the entire population of Trust Property claimants and the extent of their claims
 - (i) *Interrogating and reconciling LBIE’s books and records*
 - (ii) *Soliciting information from potential Trust Asset claimants*
 - (a) *Direct communications*
 - (b) *Advertisement on the Administration Website*
 - (c) *Liaison with Industry Bodies*
 - (d) *Client Information Portal*
 - (e) *Press briefings and featured articles in the financial press*
- E. Imposition of a Bar Date
- F. Proposed advertisement of the Bar Date
- G. Effect of the Bar Date
- H. Bar dates imposed in respect of Lehman entities in other jurisdictions
- I. Conclusion

6 This application is being made in order to assist the Administrators in identifying those persons to whom certain assets held on trust by LBIE are to be distributed and to enable a distribution to a person entitled to assets where appropriate. Significant efforts have been made in order to establish with as much certainty as possible the total population of persons entitled to such assets and details of those efforts are set out in Section D, below. In order to put those efforts in context, I briefly explain in the following section

some of the issues faced by the Administrators in respect of assets held on trust by LBIE.

B. Trust Property

7 Prior to its insolvency, LBIE's business as a global investment bank routinely involved it in holding large quantities of assets on trust for its clients. At that time, its operations were divided among various divisions, including:

7.1 **Prime Brokerage:** Prime brokerage services (described below at paragraph 8) were provided across the whole of Europe and in the US and Asia. The majority of clients were hedge funds.

7.2 **Equities:** this was primarily an agency (including trading as a matched principal) business but included some proprietary trading. It involved dealing in cash-settled equities, convertibles and equity derivatives, and an equity strategies (event-driven) trading business.

7.3 **Fixed Income:** this conducted LBIE's activities on behalf of clients in various fixed income instruments, including asset-backed securities, credit derivatives, real estate and securitised products.

7.4 **Principal Investing:** this conducted cross-asset proprietary trading in equities, fixed income and derivatives. All transactions were to the account of LBIE, that is, not undertaken on behalf of clients.

8 Trust claims arise primarily from LBIE's prime brokerage business. Prime brokerage was a bundled package of services offered by LBIE to institutional investors seeking the ability to borrow and invest on a leveraged basis. The services provided under prime brokerage included securities lending, trade executions, and cash management, among other things. As prime broker, LBIE provided a centralised securities clearing facility for fund clients. Under such arrangements, LBIE benefited by earning fees on financing the client's long and short cash and security positions, and by charging fees for clearing and/or other services. It also rehypothecated certain securities of the clients it serviced in order to provide collateral for the funds' own borrowing of cash and securities, in accordance with the terms of the relevant prime brokerage agreements. In

the course of carrying out these activities, LBIE routinely came to hold securities on trust for its clients, either by holding custody positions, or by holding positions on a charge (as opposed to title transfer) basis as collateral.

- 9** In his recent judgment in relation to the Administrators' application regarding the scope and effect of Clause 5.2 of LBIE's standard International Prime Brokerage Agreement (charge version) (the "**IPBA (Charge)**"), as to which see further below, Mr Justice Briggs made a finding (at paragraph 79 of his judgment dated 21 October 2010) that securities held by LBIE for clients pursuant to that agreement were held on trust. In fact, I am advised that the terms of a number of the contracts into which LBIE habitually entered with its clients were consistent with those clients retaining a proprietary interest in assets transferred to LBIE. The principal such contracts were:
- 9.1** The IPBA (Charge) (a copy of which can be found at **pages 1 to 50 of "SAP6"**);
 - 9.2** The Master Custody Agreement ("**MCA**") (pre-Markets in Financial Instruments Directive ("**MiFID**") and post-MiFID versions) (copies of which can be found at **pages 51 to 87 of "SAP6"**);
 - 9.3** The Margin Lending Agreement ("**MLA**") (a copy of which can be found at **pages 88 to 95 of "SAP6"**); and
 - 9.4** The Credit Support Annex (New York law version) to the ISDA Master Agreement ("**CSA**") (a copy of which can be found at **pages 96 to 109 of "SAP6"**).
- 10** In addition to holding property on trust for its clients, LBIE also held various property on trust for its affiliates. As noted below at paragraph 17.1, various Lehman Brothers entities within the group acted as sub-custodians or intermediaries for one another, both in respect of securities and money. Pursuant to such arrangements, LBIE acted as custodian or sub-custodian for various of its affiliates.
- 11** As set out in my first and second witness statements, dated 6 October 2008 and 25 February 2009 respectively, the Administrators have from an early

stage in the administration sought to adopt a system for dealing with property held in the name of, or otherwise to the order of, LBIE which is subject to trust or proprietary claims, whether comprising monies held under the rules set out in the FSA's Client Assets sourcebook ("**Client Money**"), or securities and assets (including monies) derived from such securities since LBIE's entry into administration ("**Trust Assets**") (together "**Trust Property**") in an orderly and efficient manner. Further, the Administrators have sought to adopt a system which balanced the importance of dealing with the potential proprietary claims and the achievement of the statutory purpose for which the Administrators have been appointed.

- 12 The Administrators have always been anxious to return Trust Property to LBIE's clients and affiliates as expeditiously as possible, but have faced numerous challenges in doing so. This Application is specifically concerned with the return of Trust Assets, of which the Administrators estimate that LBIE is currently holding, via its various accounts, depositories and sub-custodians, up to approximately US\$18.9 billion (of which approximately US\$11.4 billion is currently within the Administrators' direct control).
- 13 I set out in Section D of my second witness statement the Administrators' current approach to the return to the of Trust Property (at least in so far as that Trust Property is held for LBIE's clients). That approach, which is based on the bilateral agreement of returns to clients who can make out a special case for prioritisation and that are able and willing to accept Trust Property returns on necessarily stringent conditions (including provision by the recipient clients of indemnities and credit support), remains largely the same today. Details of that approach are set out in Appendix A to this statement (with the minor differences as compared with the approach outlined in my second witness statement identified). As at the date of this statement, the claims of approximately 100 clients have been considered by the Hardship and Prioritisation Committee referred to in Appendix A. Trust Property has been returned to the holders of 81 accounts. The total value of Trust Property returned to clients to date is US\$13.3 billion.

- 14** With regard to the distribution of Client Money held by LBIE (and received by LBIE prior to its entry into administration), the Administrators applied to Court for directions in order to resolve various issues of principle. A hearing of the application took place from 9 November 2009 to 24 November 2009 and judgment on the issues is currently awaited. Directions were sought in that application regarding a number of issues, which can be broadly grouped as follows:
- 14.1** What monies constitute the Client Money pool?
- 14.2** Who is entitled to claim against the Client Money pool and what is the extent of their entitlement?
- 14.3** How should distributions from the Client Money pool be effected?
- 15** Further, the Administrators recently sought directions clarifying the scope and effect of Clause 5.2 of the IPBA (Charge) and the application of the FSA's Rule 7.2.3 collateral transfer exemption in respect of certain cash received by LBIE post-administration.
- 16** As regards Trust Assets, the Administrators need to ascertain (i) the assets that are available to be returned to clients or affiliates i.e. those assets that do not form part of LBIE's general estate; (ii) entitlements to those assets; and (iii) the amounts (if any) which can be retained from those assets in order to satisfy liabilities owed to LBIE (and possibly also to other Lehman Group entities).
- 17** The issues described in paragraph 16 above give rise to certain difficulties which are more fully described in my first and second witness statements. In summary, although very significant progress has been made, the Administrators are not in a position to ascertain with absolute certainty the claims to any given stock or the amount of such stock that will ultimately be available for distribution or appropriation. In particular:
- 17.1** LBIE held very few Trust Assets itself. Rather, it held them through various third-party banks, custodians, agents, counterparties, exchanges and clearing houses. The Administrators do not yet have control of all of the assets that ought to be held for LBIE through such depositories. The position of LBIE's affiliates is relevant in this

regard because, when the Lehman Group was operating on a solvent basis, various entities within the group acted as sub-custodians or intermediaries for one another, both in respect of securities and money. Many of those entities are now under the control of insolvency office holders in the United States, Japan, Hong Kong, Switzerland, Luxembourg and elsewhere and, consequently, may fail to return all of the assets they held for LBIE, creating shortfalls in the Trust Assets available for distribution or appropriation.

- 17.2** During the few days immediately prior to the entry into insolvency of Lehman Brothers Inc (“LBI”), the U.S. broker-dealer in the Lehman group, the Administrators understand that it transferred a significant volume of LBIE Trust Assets (which it was holding as sub-custodian for LBIE) directly to the LBIE clients or affiliates for whom they were ultimately held. LBIE’s books and records do not reflect these transfers as LBI has not yet provided the Administrators with the information they require in order to update LBIE’s books and records in this regard. It follows that certain of LBIE’s clients or affiliates who are identified in LBIE’s books and records as Trust Asset claimants may have already received some or all of their Trust Assets and, accordingly, they are either Trust Asset claimants to a much lesser extent than indicated in LBIE’s books and records or, if they received back all of their Trust Assets, they are not Trust Asset claimants at all.
- 17.3** The Administrators face considerable uncertainty over whether a particular holding of Trust Assets may be the subject of competing claims and whether, as a result, the totality of claims to a particular stock line will exceed the number of securities held by LBIE in that stock line. Again, the consequence would be that shortfalls exist and the stock available must be allocated between the relevant Trust Asset claimants;

- 17.4** The Administrators also face uncertainty as to whether particular holdings of Trust Property are subject to security or set-off rights in respect of liabilities owed to LBIE and/or to any of its affiliates;
- 17.5** There are a number of legal and operational difficulties involved in valuing the Trust Assets and the other obligations that might exist between LBIE and any given client or affiliate. Given that the Trust Assets are often subject to security granted to LBIE (or possibly to affiliates), it can accordingly be difficult to ascertain with certainty the extent to which a client or affiliate is entitled to the return of Trust Assets.
- 18** I am informed that each of the agreements referred to at paragraph 9, above (and LBIE's standard Terms of Business, a copy of which can be found at **pages 110 to 131 of "SAP6"**) contain security or lien provisions that entitle LBIE to exercise rights of recourse to Trust Assets. As a consequence, before they can distribute Trust Assets to a particular claimant, the Administrators need to ascertain that claimant's overall financial position vis-à-vis LBIE, in order to determine whether or not they ought to appropriate (and then in their discretion dispose of) any of the relevant assets on behalf of LBIE, in exercise of the security right or lien. Given that the relationships between LBIE and the majority of its relevant clients were complex, involving various types of business (e.g. equity derivatives, foreign exchange futures and options, stock lending etc.) and governed by multiple master agreements, the determination of such overall financial positions is a complex process.
- 19** As detailed further below, the Administrators had proposed to address various of these issues and others through the promulgation of a scheme of arrangement (under Part 26 of the Companies Act 2006) in respect of certain Trust Assets. However, Mr Justice Blackburne held on 21 August 2009 that there is no jurisdiction afforded by the Companies Act 2006 for the courts to sanction such a scheme of arrangement (i.e. one that interferes with the property rights of creditors for whom assets are held on trust). That decision was appealed by LBIE and the Administrators, but the

Court of Appeal upheld Mr Justice Blackburne's decision on 6 November 2009.

- 20** The Administrators make this Application in an effort to establish a basis upon which they can proceed to distribute or appropriate Trust Assets. Having taken all reasonable steps to identify Trust Asset claimants, the Administrators seek to obtain as much certainty as possible as to the identity of claimants to whom Trust Assets are to be distributed. Without reducing the uncertainty as regards the identity and quantum of claimants to whom Trust Assets are to be returned, it is extremely difficult for the Administrators to allocate to claimants the Trust Assets held by LBIE, and on that basis establish the net position of any given claimant and make distributions and appropriations of Trust Assets, without exposing LBIE (and possibly themselves) to the risk of liability for breach of trust.
- 21** As discussed in further detail below at paragraphs 83 to 87, certain issues arise (or potentially arise) between LBIE and its affiliates out of security interests or liens purportedly contained in various agreements pursuant to which LBIE holds assets. As stated below, it is not intended that such issues be dealt with by this Application and it is not proposed that the Bar Date apply to claims in respect of such security interests or liens.

C. COURT APPLICATIONS MADE TO DATE IN RELATION TO THE ADMINISTRATORS' DEALINGS WITH AND THE RETURN OF TRUST PROPERTY

- 22** During the course of the administration so far, the Administrators have made various applications to Court in order to seek guidance as to the appropriateness of their general strategy for returning Trust Property to beneficiaries. The first such application was heard on 7 October 2008 and resulted in the making of an order (the "**Trust Property Order**") authorising the Administrators to continue their management of the affairs, business and property of LBIE, as such management relates to proprietary claims by third parties, by implementing and/or giving effect to the processes set out in the Schedule to that Order. A copy of the Trust Property Order (including the Schedule) can be found at **pages 132 to 138 of "SAP6"**.

- 23 During the months that followed the making of the Trust Property Order, whilst the Administrators endeavoured to return assets in accordance with the prioritisation process described at Appendix A to this witness statement, they were naturally mindful of the importance of dealing with all claims for Trust Property efficiently and swiftly. At the same time, the Administrators were also conscious of their obligations to the unsecured creditors of LBIE and did not wish to effect distributions of Trust Property in a manner which could potentially expose those creditors to further loss.
- 24 Having considered with their advisers the options available to them in this regard, the Administrators decided to explore a framework to deal with the resolution of the various uncertainties surrounding the extent and validity of claims to Trust Assets through a scheme of arrangement under Section 895 of the Companies Act 2006. They therefore made an application to Court, with the purpose of advising it of their intention to assess the feasibility of a scheme of arrangement and seeking liberty to propose such a scheme to Trust Asset claimants. It was envisaged that any proposed scheme of arrangement would entirely resolve the positions of Trust Asset claimants vis-à-vis LBIE (i.e. not only their Trust Asset claims, but also any net claims against or liabilities to LBIE, would be dealt with). It was never intended that the proposed scheme of arrangement would deal with the claims of those with only general unsecured claims. At a hearing of the Administrators' application on 16 March 2009, Mr Justice Blackburne granted the liberty sought (a copy of his Order can be found at **pages 139 to 141 of "SAP6"**).
- 25 Whilst it did not take an active position in relation to that application, the London Investment Banking Association ("**LIBA**") appeared at the 16 March 2009 hearing by Leading Counsel, in order to note that it considered there to be a fundamental question as to whether the Court had jurisdiction to subject trust property to a scheme of arrangement. Consequently, the Administrators made a further application (dated 14 July 2009) in order to seek clarification as to whether the Court does have jurisdiction to sanction such a scheme.
- 26 A hearing of the Administrators' application took place on 29 and 30 July 2009 and Mr Justice Blackburne handed down judgment on 21 August

2009 (a copy of his judgment is exhibited to this statement at **pages 142 to 163 of "SAP6"**). He concluded that there is no jurisdiction afforded by the Companies Act 2006 for the courts to sanction a scheme of arrangement that is concerned with the distribution of property held on trust and seeks to vary or extinguish proprietary rights. He expressed some regret at the decision he felt compelled to reach in relation to jurisdiction, noting that:

"Given the exceptional problems that the administrators face in dealing with client assets and the very great effort that they have devoted to devising a means... to bring about speedy return of those assets, this is not a conclusion which I am happy to reach. But I must set out the law as I see it, not as I might wish it to be" (see paragraph 74 of the judgment at **page 162 of "SAP6"**).

27 Mr Justice Blackburne granted permission to appeal against his decision and the Administrators' filed such an appeal on 10 September 2009, simultaneously requesting that the appeal be heard on an expedited basis. The request for expedition was granted and a hearing of the appeal took place on 26 October 2009.

28 In a judgment handed down on 6 November 2009 (a copy of which is exhibited to this statement at **pages 164 to 189 of "SAP6"**), the Court of Appeal upheld Mr Justice Blackburne's decision. In common with the court below, the Court of Appeal expressed some sympathy with the position in which the Administrators find themselves. Lord Justice Patten stated:

"I accept (as the Judge did) that the proposed Scheme represents a considered attempt to overcome the difficulties faced by the administrators in reconciling the entries in the company's books and records with the claims made against the assets held" (paragraph 56 of the Court's judgment at **page 182 of "SAP6"**)

29 Lord Neuberger M.R. referred to *"the undoubted attraction of implementing the proposed scheme of arrangement in this case"* (paragraph 71 of the Court's judgment at **page 186 of "SAP6"**) and went on to state:

"Like Patten LJ and Blackburne J, I have some sympathy with the administrators' desire to have a scheme under section 895 which

extends to trust property, in the light of the difficulties which would otherwise almost certainly arise in connection with seeking to satisfy the rights of beneficiaries in relation to trust property held in the name of LBIE. ... I hope, indeed I would expect, that if the administrators decide to make an application under the Trustee Act or pursuant to the court's inherent equitable jurisdiction, in relation to dealing with beneficiaries' rights, the court will provide effective assistance, by arriving at a practical and fair outcome, while ensuring that delay and cost are kept to a minimum."
(paragraph 86 of the Court's judgment at **page 189 of "SAP6"**)

- 30** In planning for the possibility that the appeal would not succeed, the Administrators had given consideration to how they might approach the return of Trust Assets absent a scheme of arrangement in the form previously proposed. At paragraphs 75 to 78 of his judgment, Mr Justice Blackburne suggested a "way forward" in relation to asset returns, being a "structured approach" using the court's jurisdiction to administer trusts, potentially combined with one or more new schemes of arrangement. It is in that context, and in the context of the multilateral contract referred to below, that the Administrators make the present application.
- 31** As a result of the difficulties associated with pursuing a scheme of arrangement, the Administrators have developed (in consultation with the creditors' committee and industry bodies) an alternative approach to the return of Trust Assets, whereby (if the approach is successful) LBIE will enter into a multilateral contract with consenting Trust Asset claimants (hopefully comprising the vast majority of all Trust Asset claimants) for the return of Trust Assets.
- 32** On 5 October 2009, the Administrators placed on the Lehman-dedicated section of the PwC website (the "**Administration Website**") an update whereby they explained their current thinking in relation to the proposed multilateral contract (referred to in the Administration Website update as the "contractual solution"). A copy of that update can be found at **pages 190 to 196 of "SAP6"**). As explained in the update (and in the third witness statement of David Philip Ereira dated 21 October 2009, filed in support of

the scheme of arrangement jurisdiction appeal hearing), trust claimants will be invited to bind themselves voluntarily to the proposed contractual settlement, the provisions of which are substantially the same as those that were contained in the proposed scheme of arrangement. In particular, the provisions in relation to the management of assets, the asset valuation methodology, the calculation of net contractual positions, the establishment of pools of assets and pro rata sharing of shortfalls between signatories, the resolution of disputes and the concepts of appropriation and retention amounts are substantially the same as those contained in the scheme of arrangement that was formerly proposed. The coming into operation of the multilateral contract is expressed to be conditional upon a threshold condition relating to the proportion of known Trust Asset claimants who sign up to its terms. The coming into effect of the operative provisions of the multilateral contract is also conditional upon an Order satisfactory to LBIE being made as a result of this Application. Further detail in relation to the proposed multilateral contract is contained in the third witness statement of David Philip Ereira. Please also see paragraph 56 below in this regard.

D. EFFORTS MADE THUS FAR TO ESTABLISH THE ENTIRE POPULATION OF TRUST ASSET CLAIMANTS AND THE EXTENT OF THEIR CLAIMS

- 33** As described in more detail in my second witness statement, the books and records that the Administrators took control of at the commencement of LBIE's administration did not readily identify all potential Trust Asset claimants. Further, at that time, the Administrators had no established channels through which to communicate with such potential claimants. Despite the considerable difficulties associated with the task, however, the Administrators consider that significant progress has been made in establishing with a reasonable degree of certainty the identity of potential Trust Asset claimants. In that regard, their efforts thus far have centred around (i) interrogating and reconciling LBIE's books and records; and (ii) soliciting information from potential Trust Asset claimants. Notwithstanding the progress made as a result of the actions described below, it is

impossible for the Administrators to be entirely certain that they have identified every Trust Asset claimant.

(i) Interrogating and reconciling LBIE's books and records

- 34** The IT-based systems that recorded and stored LBIE's books and records were highly complex, consisting of numerous discrete systems. Some of these systems require manual input and were initially suspended on 15 September 2008. Others continued to operate automatically, making various postings on the assumption that positions were maturing and being closed in line with their contractual settlement dates - i.e. on the (incorrect) basis that all of LBIE's business was continuing to operate as normal. Furthermore, some systems, while forming an integral part of the overall data-control framework that housed LBIE's books and records, were controlled not by LBIE, but by its affiliates, such as LBI. Following the sale of certain former Lehman Brothers business units to Barclays Capital Inc, the control and access that LBIE was able to exercise over various systems was materially impaired and data regarding transactions which LBI conducted for LBIE was withheld from LBIE.
- 35** In order to understand how these systems operated under normal conditions and how they have been impacted by LBIE's administration, the Administrators have been working with Lehman staff. They have also taken steps manually to bring the data contained in those systems up to date, where possible. This was necessary for a number of reasons. For instance, the IT systems that recorded the data comprising LBIE's books and records operated on a "contractual settlement" basis, meaning that they recorded trades as having settled on the contractual settlement date whether or not they had in fact settled. In reality, typically three days can elapse between the date on which a trade is concluded and the date on which it settles (i.e. the date on which the relevant securities are actually "delivered"). The result was that trades for which instructions were received in the days leading up to 15 September 2008 and were executed but which failed to settle as a result of LBIE entering administration were nonetheless, in some circumstances, recorded in LBIE's books and records as if they had actually

settled. There were some 840,000 pending and failed trades as at the date of LBIE's entry into administration.

- 36** In order for the books and records to reflect the actual position for European securities as at 15 September 2008, it was necessary for the Administrators to identify (by reference to various sources, including exchanges and custodians) those trades that failed and then adjust for them in LBIE's books and records. This exercise was made more complex by the fact that not all trades booked during the last three business days prior to 15 September 2008 failed to settle. Whether or not any particular trade failed depended upon factors such as the jurisdiction and/or market in which the relevant trade was due to settle. The adjustment process is substantially complete for those positions within the Administrators' control.
- 37** As noted above, it has not been possible for the Administrators to update LBIE's books and records to reflect the distributions of Trust Assets from LBI to LBIE clients during the days leading up to LBI's entry into insolvency (referred to above at paragraph 17.2), since LBI has not yet provided the Administrators with the requisite data that would enable them to do so.
- 38** In updating LBIE's systems to reflect the position at any given time since 15 September 2008, it has been necessary manually to input into those systems transactions to reflect the corporate events (such as dividend receipts) that have occurred in respect of the positions.
- 39** In addition to updating LBIE's books and records to include corporate actions in order accurately to reflect the current position, those books and records have also needed to be updated to reflect actions taken by LBIE's trading counterparties. LBIE's entry into administration prompted many depositories and sub-custodians to liquidate certain of LBIE's house positions with them and to exercise purported rights of set-off in relation to the proceeds of such liquidation. Similarly, a large number of counterparties to "over the counter" derivative transactions (which are, by their nature, highly complex to value) have exercised rights to terminate those transactions, necessitating the valuation by the Administrators of the close-out positions in respect of those transactions and, in some instances, of the collateral held by the counterparty. Such a high volume of counterparty

activity would not have been expected in the ordinary course of LBIE's business and compounded the difficulties associated with bringing up to date of LBIE's books and records. Whilst the valuation of derivatives does not impact the control of securities, it does impact the determination of a client's or affiliate's net indebtedness and, therefore, the extent to which assets charged to LBIE are to be retained by LBIE (or, alternatively, returned to the client or affiliate). Until these valuations were complete for affected clients or affiliates, the Administrators were not in a position to establish the extent to which assets should be returned to the relevant entities.

- 40 The process of updating the data contained in LBIE's systems has involved liaising with LBI, in order to obtain up to date information in relation to the numerous LBIE systems within LBI's control, to the extent that LBI has been able and prepared to provide such information. Discussions with LBI regarding such issues are ongoing.
- 41 In addition to updating the data comprising LBIE's books and records, the Administrators have been working to reconcile those books and records with the books and records of the various depositories and sub-custodians (including affiliates), and those of each of the relevant clients and affiliates (in either case, where available). As regards the depositories and sub-custodians, the reconciliation process is reliant upon the ability of the Administrators to obtain accurate and up to date information from the depositories and sub-custodians themselves. This has been a protracted and difficult process in many cases.
- 42 In addition to reconciling LBIE's records with data received from the depositories and sub-custodians, the records need to be reconciled with information received from LBIE's clients and affiliates. As described in further detail below, the Administrators have contacted LBIE's clients a number of times in order to obtain from them full details of their claims to Trust Property. Further, they have issued notices on the Administration Website inviting those to whom letters have not been sent, but who nonetheless believed that they might have claims to Trust Property, to supply them with details of such claims. The Administrators have also been

engaged in extensive dialogue with various of LBIE's affiliates in this regard.

- 43** Once in receipt of this information from a Trust Property claimant, the Administrators are engaging in the process of reconciling such information and valuations with those of LBIE, as manually updated. The end result ought to be that the position can be examined by reference to three independent sets of records, being those of LBIE, those of the relevant depository or sub-custodian and those of the Trust Property claimant. It is only by engaging in this process that the Administrators can be confident that they are acting on complete information when they return Trust Property.
- 44** In as far as it relates to Trust Property claimants who have already submitted claims, the above process is now largely complete although, as detailed further below at paragraph 47.8, the Administrators recently made available to clients Updated Position and Balance Statements (i.e. updates to the Interim Position and Balance Statements referred to below at paragraph 47.7), which will inevitably prompt some clients to submit new information that can be incorporated into the reconciliation process. Having said that, in order for the reconciliation process to be entirely effective, it is necessary to identify and understand the entire population of claims to Trust Property.

(ii) Soliciting information from potential Trust Asset claimants

- 45** The Administrators' efforts to engage with potential Trust Asset claimants and to solicit from them information regarding their entitlements to such Trust Assets have included the following:
- 45.1** The sending of various direct communications to clients that LBIE's books and records indicate to be potential Trust Asset claimants;
 - 45.2** Advertisement on the Administration Website (through the posting of 27 separate updates in relation to Trust Assets);
 - 45.3** Regular liaison with and presentation to the members of industry bodies, namely the Managed Funds Association ("MFA") in New York

and the Alternative Investment Management Association (“AIMA”) in London;

45.4 The establishment and maintenance of a customised web-based portal known as the “**Client Information Portal**”, to which only registered LBIE claimants have access and which provides a further secure channel of communication between potential Trust Asset claimants and the Administrators;

45.5 Press briefings and featured articles, mostly widely in the financial press (for example the Financial Times and the Wall Street Journal) and specialist industry journals.

46 In the paragraphs that follow, I set out further details of efforts that the Administrators have made to communicate with potential Trust Asset claimants through each of the channels referred to.

(a) Direct communications

47 With regard to direct communications, the various circular letters and e-mails relating to Trust Assets that the Administrators have sent out *en masse* to clients indicated in LBIE’s books and records to be potential Trust Asset claimants (or otherwise creditors of LBIE) are as follows:

47.1 As I noted in my second witness statement, the Administrators initially wrote to 1,707 account holders thought potentially to have claims, rights or other interests in Trust Property, asking them to provide full details of such claims, rights or other interests which they purport to have in relation to Trust Property, including: (i) confirmation of positions and balances held with LBIE as at 7:56am on 15 September 2008 (the time the administration order was made by the Court); (ii) copies of any contractual agreements and other relevant documentation; and (iii) details of all positions terminated or closed since 7:56am on 15 September 2008 together with the basis of any valuations assumed in the client’s calculations. These letters (a sample copy of which can be found at **pages 197 to 198 of “SAP6”**) were sent on 8 October 2008. They were followed up by a further letter in December 2008 to those recipients from whom

responses had not yet been received (a template of such a further letter is exhibited to this statement at **pages 199 to 200 of “SAP6”**) and a further letter in April 2009 to those recipients who had still not responded by that stage (a template of such a further letter is exhibited to this statement at **pages 201 to 202 of “SAP6”**). The Administrators have to date received some 1,222 responses to these letters.

47.2 On 26 June 2009, the Administrators wrote to all clients identified in LBIE’s books and records as potentially having claims to Trust Assets, in order to explain our proposal to implement a scheme of arrangement. The referenced letter (a sample copy of which can be found at **pages 203 to 206 of “SAP6”**) explained, among other things, the purposes of the proposed scheme of arrangement, the manner in which it was intended that it be implemented and the valuation methodology to be adopted for voting purposes. In a section headed *“Communications”*, it stated as follows: *“So that we can continue to communicate with you efficiently and ensure that you receive all necessary documentation regarding the proposed Scheme, it is important that we have an up to date and accurate record of your contact details. We therefore request that you email any amendments to your legal client name and contact details, including preferred postal address (if different from this letter) and e-mail address to: schemeofarrangement@lbia-eu.com” (emphasis in original).*

47.3 On 14 July 2009, the Administrators wrote to all clients identified in LBIE’s books and records as potentially having claims to Trust Assets, stating that we were in the process of updating our contact details for all known creditors. The referenced letter (a sample copy of which can be found at **page 207 of “SAP6”**) went on to state as follows: *“We are interested in reaching as many creditors as possible via email communications when appropriate. Therefore, please provide us with your **current email address** ... by sending an email*

to schemeofarrangement@lbia-eu.com as soon as possible.” (emphasis in original).

- 47.4** On 19 August 2009, the Administrators wrote to certain of those clients previously written to on 26 June 2006 (see paragraph 47.2 above) in order to inform them that, having further reviewed LBIE’s books and records, we did not believe that they in fact had any claims to Trust Assets and that they would therefore not, subject to the following, be included in the proposed scheme of arrangement. The referenced letter (a sample copy of which can be found at **pages 208 to 209 of “SAP6”**) went on to state that: *“In the event you believe that your trust assets position is different from that which we have outlined above, and you wish to assert that you will be a creditor within the terms of the proposed Scheme please advise us directly at schemeofarrangement@lbia-eu.com ... by 4 September 2009”* (emphasis in original).
- 47.5** As a result of the analysis referred to, the Administrators concluded that there were in fact 553 clients that appeared to have Trust Asset claims.
- 47.6** On 2 September 2009, the Administrators wrote to each of the 553 clients identified in LBIE’s books and records identified as appearing to have claims to Trust Assets in order to advertise the launch of the Client Information Portal (described further below). The referenced letter (a sample copy of which can be found at **pages 210 to 211 of “SAP6”**) included a unique user identification and password, so as to enable potential claimants to log-on to the portal on a secure basis.
- 47.7** On 4 September 2009, the Administrators wrote to each of the 553 clients identified in LBIE’s books and records identified as appearing to have claims to Trust Assets, enclosing hard copies of their Interim Position and Balance Statements, as posted on the Client Information Portal. An **“Interim Position and Balance Statement”** is a statement showing an interim valuation of what LBIE’s books and records identify as (i) Trust Assets which ought to have been held

by LBIE in custody or charge accounts for the benefit of the relevant client; (ii) rehypothecated positions and short positions; (iii) assets which LBIE was contractually required to deliver to the relevant client but which were not held on the client's behalf (i.e. title assets); and (iv) valuations of any financing and derivatives positions held by the relevant client and well as any cash balances. The referenced letter (a sample copy of which can be found at **pages 212 to 217 of "SAP6"**) noted that the Administrators' purpose in providing clients at this stage with their Interim Position and Balance Statements was, in part, to assist with the ongoing reconciliation process being undertaken in relation to LBIE's books and records. It stated that *"[t]he reconciliation activity within the administration is a key priority. We encourage all clients to identify all differences they have vs. the closed Statement to LBIE."*

47.8 The Administrators recently made available to each of the 553 clients referred to above an update to their Interim Position and Balance Statement. This update reflects, where possible, valuations positions valued on a settled basis, whereas the Interim Position and Balance Statement referred to above valued positions on a trade date basis. A primary purposes of this update (termed an Updated Position and Balance Statement) is to allow clients to identify and agree all of their claims to Trust Assets held by LBIE (and any monies derived from those assets during the course of LBIE's administration). This affords clients a further opportunity to inform the Administrators of any manner in which they believe that LBIE's updated and reconciled books and records do not accurately reflect their actual entitlements to Trust Assets. It is hoped that it will aid the timely resolution of any remaining discrepancies between LBIE's books and records and those of its clients, ahead of the planned coming into effect of the multilateral contract referred to above.

48 As regards Trust Asset claims that LBIE's affiliates may wish to assert, the Administrators have, from the outset of LBIE's administration, been engaged in active dialogue with LBIE's key affiliates (and, where relevant

the insolvency practitioners appointed in respect of them). Discussions and negotiations with such entities and practitioners have been wide ranging and extensive and, in some cases, have led to reciprocal access to books and records being granted for the purposes of determining the claims arising each way as between LBIE and the relevant affiliate. In any event, it is to be expected that LBIE's affiliates (and, where relevant, the insolvency practitioners appointed in respect of them) will have been closely following the advertisements referred to in the following section of this statement. In the circumstances, any affiliate having a claim to Trust Assets should be aware of the imperative now to assert it and some affiliates have already asserted such claims.

(b) Advertisement on the Administration Website

49 As noted above, the Administrators have also endeavoured to engage with potential Trust Asset claimants via the Administration Website, which is dedicated to advertising developments in the LBIE administration and is updated on a regular basis. A copy of its "Home page" as at the date of this witness statement can be found at **page 218 of "SAP6"**. Its contents are set out in various sub-sections, being:

- 49.1** Client money;
- 49.2** Client Assets;
- 49.3** Failed Trades;
- 49.4** Creditors
- 49.5** Exchange Updates;
- 49.6** Companies in Administration; and
- 49.7** Master Agreement Terminations.

50 The first page of the "Client Assets" sub-section of the Administration Website (a current copy of which can be found at **page 219 of "SAP6"**) invites clients of LBIE who believe they may have Trust Assets claims to read the links on that page for further information. The links themselves

contain various updates (27 to date) regarding the manner in which the Administrators are dealing with Trust Assets held by LBIE.

- 51 A copy of the update posted on 15 October 2008 (and subsequently updated on 23 March 2009) can be found at **page 220 of “SAP6”**). It states as follows:

“... As part of the Court approved process for the identification and return of Client Money and Assets, the Administrators have now written to counterparties, who they currently consider may have Trust Claims, to obtain from them full details of the rights and claims they believe they have in relation to all forms of Trust Property.

The confirmation will be used by the Administrators as part of the process of individually reviewing all accounts and positions with clients of LBIE. ...

...

If you believe you have assets or money held by LBIE, please submit your positions and balances by email only on a standardised MS Excel form (see below for link). ... In addition to the standardised form for positions and balances, please also provide electronic copies of any written contracts you have with LBIE as well as any other relevant documentation. ...”

- 52 That invitation was repeated in a list of Frequently Asked Questions (and relevant answers) dated 19 March 2009 and posted on the “Client Assets” sub-section of the Administration Website (a copy of which is at **page 221 of “SAP6”**). That posting also included details of how to contact a bespoke client management team set up by the Administrators in order to respond to client queries relating to Trust Property issues.
- 53 I referred above to the letter that the Administrators wrote on 26 June 2009 to clients who LBIE’s books and records identified as potentially having claims to Trust Assets. This letter was written in the context of the proposed scheme of arrangement and provided certain information regarding, for example, the purpose of the proposed scheme. In an update posted on the “Client Assets” sub-section of the Administration Website on the same day (see **page 222 of “SAP6”**), the Administrators publicly advertised the fact

that this letter had been sent out to clients that they were aware had potential claims to Trust Property. The update went on to state as follows:

“... if you believe you have a claim to client assets and do not receive this letter by the 6th of July, please contact us through the newly designated Scheme mailbox schemeofarrangement@lbia-eu.com, re-confirming your postal address at the same time.”

- 54** In September 2009, the Administrators created the Client Information Portal via a secured website, referred to below. As set out above, on 2 September 2009, the Administrators sent hard copy letters regarding the Client Information Portal to all creditors that, according to LBIE’s books and records, appeared to have claims to Trust Assets. In an update posted on the “Client Assets” sub-section of the Administration Website on 8 September 2009 (see **page 223 of “SAP6”**), the Administrators publicly advertised the fact that this letter had been sent out. The update went on to state as follows:

“If you have not received a letter with your LOG ON information and believe you have client assets or pre-administration client money held by LBIE, please contact the clientpositionresponses@lbia-eu.com mailbox ...”

- 55** As stated above (at paragraph 47.8), the Administrators recently made available to each of the 553 clients indentified in LBIE’s books and records as appearing to have a claim to Trust Assets an update to their Interim Position and Balance Statement, known as an Updated Position and Balance Statement). On 24 November 2009, they posted an update to the “Client Assets” sub-section of the Administration Website notifying potential Trust Assets claimant that they had done so (see **page 224 of “SAP6”**). The update stated:

“If you did not receive a letter from the Joint Administrators in early September containing your log on information for the Portal and believe you have an ownership claim to trust assets, please contact the claimresolutionagreement@lbia-eu.com mailbox...”

56 Also on 24 November 2009, the Administrators announced through a further update to the “Client Assets” sub-section of the Administration Website the opportunity for certain Trust Assets claimants to sign up to the multilateral contract referred to above at paragraphs 31 and 32. A copy of the relevant update can be found at **pages 225 to 227 of “SAP6”**. The update included the following statement:

“LBIE has today sent a letter by email to each person that LBIE has determined, based on its books and records, may have an ownership claim to trust assets. These persons are referred to as “TA Offerees” in the Agreement. The letter also contains access links to the Circular and the Form of Acceptance. If you have not received a letter via email and believe you may have an ownership claim to trust assets, please contact the claimresolutionagreement@lbia-eu.com mailbox...”

57 All of the communications referred to above at paragraphs 51 to 56 are freely accessible by the public. The Administrators take the view that most of those with claims to Trust Assets held by LBIE would have been likely, during the period that has elapsed since LBIE’s highly publicised entry into administration, to have familiarised themselves with the Administration Website and its contents. Up until October 2009, the “Client Assets” sub-section of the Administration Website was combined with the section dealing with Client Money issues. Between 1 January 2009 and 1 November 2009, that combined section of the Administration Website was visited 20,654 times. Further, the “Client Assets” sub-section has been visited a further 1,622 times since it was launched as an independent section of the Administration Website in October 2009. It is therefore to be expected that most (if not all) potential Trust Asset claimants are aware of the Administrators’ requests (as set out above) that they contact them and assert their claims.

(c) Liaison with Industry Bodies

58 As noted above at paragraph 45.3, at various times during the administration, the Administrators and their advisers have liaised with industry bodies, representing significant proportions of the likely population of Trust Asset claimants, with regard to the manner in which it is proposed

that Trust Assets be dealt with. As set out in the first witness statement of David Philip Ereira (dated 12 March 2009), filed in relation to the Administrators' application referred to above at paragraph 24, presentations regarding the possibility of the Administrators promulgating a scheme of arrangement in relation to Trust Assets were made by the Administrators to MFA in New York and AIMA in London, in the week commencing 2 March 2009.

- 59** On 5 and 7 August 2009, the Administrators and their advisers made further presentations to the MFA and AIMA, in order to provide members of those bodies with possible interests in Trust Assets held by LBIE with an overview of the scheme of arrangement at the stage of development which it had reached by that time. During the week commencing 5 October 2009, the Administrators and their advisers again met with both MFA in New York and AIMA in London, in order to discuss, among other things, this Application.
- 60** In total, the Administrators have made four such presentations during the course of the Administration, each of which has been made to both the MFA (in New York) and to AIMA (in London). On each occasion, the cumulative attendance in New York and London has been between approximately 200 and 300 people.

(d) Client Information Portal

- 61** In a further effort to establish and maintain contact with potential Trust Asset claimants, the Administrators recently created the Client Information Portal (referred to above at paragraph 45.4), via a secure website. The Client Information Portal, which is accessed by LBIE clients using a unique user identification and password provided to them by the Administrators, shows clients who may have held custody or charge positions at the time when LBIE entered administration their Interim Position and Balance Statements and their Updated Position and Balance Statements (both referred to above). It also includes a function whereby clients may submit queries to the Administrators in relation to their positions. As at 22 October 2009, 64% of the 553 clients referred to above as apparently having Trust Asset claims (all of whom were sent unique user identifications and

passwords) had logged into the Client Information Portal since its establishment in September 2009.

(e) Press briefings and featured articles in the financial press

62 From the outset, the Administrators have adopted a pro-active press communications strategy, in order to ensure that the financial community as a whole, and LBIE's creditors and clients in particular, were kept abreast of developments in the administration. This strategy has entailed the holding of press conferences and the publication of press releases in relation to major milestones in the course of the administration. Both the previously proposed scheme of arrangement in relation to Trust Assets and the currently proposed multilateral contract (referred to above at paragraph 31) have received extensive coverage in the financial press and specialist journals.

63 In addition to all of the above communications specifically targeted at potential Trust Asset claimants, there have also been several milestones in the administration in general that have involved the Administrators sending to all known potential creditors (approximately 6,500 recipients having relationships of one form or another with LBIE) various communications that, in the ordinary course, can be expected to have come to the attention of potential Trust Asset claimants. Such communications include:

63.1 The notice of the appointment of the Administrators, dated 16 September 2008;

63.2 The notice of the first creditors' meeting, dated 28 October 2008;

63.3 The notice of the results of the first creditors' meeting, dated 27 November 2008;

63.4 The first progress report to creditors, dated 14 April 2009; and

63.5 The second progress report to creditors, dated 14 October 2009.

E. IMPOSITION OF A BAR DATE

64 As at the date of this statement, only 13 of the 553 LBIE clients identified in LBIE's books and records as apparently being Trust Asset claimants have

yet to engage in a dialogue with the Administrators with regard to their claims. Unfortunately, however, the Administrators cannot be certain that all persons who are in fact entitled to Trust Assets have made claims to them or are capable of identification from LBIE's books and records. This is causing difficulty for the Administrators because, for the reasons outlined above, they are not able to rule out (or determine the extent of) shortfalls in any particular stock line (and therefore distribute and appropriate assets without the risk of incurring liabilities for the general estate) until all claims into that stock line have been ascertained and the validity of such claims determined.

- 65** As long as the potential exists for further claims to Trust Assets to be asserted, the Administrators cannot release such assets (without exposing LBIE to the risk of claims for breach of trust) unless they impose conditions on such returns, such as indemnities supported by significant collateral or guarantees (see Appendix A to this witness statement for further details). This means that, even where all information currently available to the Administrators suggests that particular Trust Assets belong to a particular LBIE client, and even where the relevant client may be suffering hardship as a result of its assets continuing to be held by LBIE, the Administrators are often unable to release the assets because the client is either unwilling or unable to provide the requisite indemnity and credit support.
- 66** In light of the significant challenges associated with identifying with certainty all claims that may be asserted to Trust Assets held by LBIE, the Administrators now wish to set a date (i.e. the Bar Date) by which all persons who wish to assert certain proprietary claims to Trust Asset claimants would be requested to submit their quantified claims. After that date, the Administrators (and LBIE as trustee) wish to be entitled to distribute and appropriate Trust Assets on the basis of the claims submitted to them (or apparent from LBIE's books and records) by the time of such distribution or appropriation. I am advised that such distribution could be made without the need for indemnities and credit support, since the Court's Order would mean that LBIE would be protected from breach of trust claims arising out of the distribution.

- 67** If the Court grants the Order sought by this Application, once the Bar Date has passed, the Administrators will be able to complete the tasks of determining entitlements and ultimately distributing or appropriating Trust Assets. It is recognised that, if new claims to Trust Assets were to be asserted after the Bar Date, but prior to distributions or appropriations being made in respect of such Trust Assets, then such claims would need to be taken into account.
- 68** Most of the assets held by or on behalf of LBIE are dematerialised. For present purposes, therefore, the Administrators propose to treat an asset as “distributed” once a settlement instruction has been given to the relevant depository or sub-custodian. Such assets are generally delivered electronically through a centralised securities settlement system. Alternatively, where LBIE is not a direct participant in such a system, its agent will generally deliver the securities for it through the system, or by book entry transfer in its own accounts, by transfer of the security from an account in the name of LBIE (or its nominee) to an account in the name of a third party.
- 69** There are typically one or more such systems in each jurisdiction in which securities are held by LBIE and they do not all operate in the same way. As I understand it, they generally require participants to input settlement instructions into the system, specifying the relevant security and settlement date, and if the proposed transferor's and transferee's settlement instructions match, at that point they become irrevocable. In certain jurisdictions (such as those within the EU), it is at that point unlawful for an administrator to seek to interfere in the settlement process and in other circumstances it is not possible unilaterally to “unmatch” or revoke the settlement instructions.
- 70** Even if there are jurisdictions in which it is possible lawfully to revoke or interfere with an instruction, doing so would result in the failure of the transaction in circumstances which may nonetheless give rise to disputes and potential liabilities for LBIE. In practical terms, it is also likely to be difficult for the administrators to take the necessary legal advice in the relevant jurisdiction and act on it prior to the matched instructions taking

effect. It is for these reasons that once instructions have been put into the relevant system, the asset is proposed to be treated as having been transferred. To do otherwise is likely to be unworkable and lead to potential liabilities.

- 71** As regards the information that the Administrators will take into account when determining entitlements (and ultimately making distributions or appropriations) after the Bar Date, the intention is that this will include all information received from Trust Asset claimants prior to distribution or appropriation of Trust Assets, as well as all information that is apparent to the Administrators from LBIE's books and records. For these purposes, LBIE's books and records include all data systems (whether they record data in hard copy, electronically or otherwise) which LBIE controls and/or is entitled to access.
- 72** It is not intended that the Bar Date apply to every kind of right that might ultimately be asserted in respect of a particular Trust Asset. Rather, it is envisaged that it will only apply in relation to claims for delivery of Trust Assets by the legal or beneficial owner of the such Trust Assets. As such, the Ordinary Application by which this Application is made is drafted such that the liberty (to distribute or appropriate) that it seeks will apply in relation to a particular Trust Assets only to the extent that there exists no valid and enforceable security interest or lien in respect of it. It follows, for the avoidance of doubt, that the Bar Date will not apply to claims that LBIE's affiliates may wish to assert under the security or lien provisions referred to below at paragraph 83.
- 73** The Administrators' proposal is that the Bar Date be set for 26 February 2010. In setting the Bar Date, the Administrators recognise that there is a tension between, on the one hand, promptly commencing work on determining entitlements and making distributions and appropriations and, on the other hand, ensuring that potential beneficiaries are afforded a sufficient opportunity to submit all claims to Trust Assets before being exposed to the risk that their assets will be distributed to third parties without them having any recourse to LBIE. The proposal of a 26 February 2010 Bar Date is an attempt to strike a balance between those competing

objectives. In proposing that date, the Administrators have also taken into account the significant efforts that have already been made to contact potential Trust Asset claimants (described above at paragraphs 45 to 61) and the very public nature of LBIE's administration.

- 74** The Administrators have already taken various steps, specifically in relation to a proposed early 2010 Bar Date, to ensure that all potential Trust Asset claimants are aware of the proposed Bar Date. The Administrators originally planned to request the Court's approval of a 31 January 2010 Bar Date and, on 5 October 2009, they posted on the "Client Assets" sub-section of the Administration Website an update stating, among other things, that:

"It is the Joint Administrator's intention to seek a Bar Date of 31 January 2010 on proprietary claims to segregated property.

The order would be that from the Bar Date LBIE would be at liberty to effect distributions of trust property on the basis of the information known to it as at a date reasonably proximate to the date of distribution. This means that if a claimant has failed to notify LBIE of its proprietary claim prior to the date of distribution it will be at risk that LBIE may effect the distribution without regard to its claim.

The basis of the application would be that at the moment LBIE can only make distributions if it receives an indemnity against unknown claims and that indemnity is supported by adequate security. This is delaying the return of assets to customers who cannot provide such an indemnity or security. By finalising the universe of potential claimants the risk to LBIE which the indemnity covers can be eliminated. LBIE will advertise the Bar Date" (see pages 190 to 196 of "SAP6").

- 75** During the week commencing 5 October 2009, I met (along with the Administrators' advisers) with both MFA and AIMA in order to explain, among other things, the Administrators' intention to apply for a Bar Date in early 2010. The Administrators have also consulted with the creditors' committee in this regard.

F. PROPOSED ADVERTISEMENT OF THE BAR DATE

- 76** The Administrators propose widely to advertise the fact of this Application having been made and the date set for the hearing (as well as giving specific notice of the Application to the FSA). The Administrators propose to invite, via the Administration Website, interested parties to make representations at the hearing, should they wish to do so.
- 77** If the Court grants the Order sought by this Application, the Administrators propose, in the time between now and the Bar Date, to make extensive efforts to publicise the fact and effect of the Bar Date. In particular, they intend to:
- 77.1** Post on the Administration Website, not less than six weeks before the Bar Date, a copy of the Court's Order and of the notice (the "Notice") that appears at Schedule 1 to the Ordinary Application by which this Application is made. The Court will note that the Notice:
- 77.1.1** Advertises the fact that the Application has been successful;
- 77.1.2** Notes the date upon which the Bar Date will fall;
- 77.1.3** Invites those with claims to Trust Assets to assert those claims in full prior to the Bar Date; and
- 77.1.4** Explains the effect that the Bar Date will have (noting that Trust Asset claimants may lose their ability to share in distributions of relevant Trust Assets if they fail to assert their claims in full prior to the Bar Date)
- 77.2** Send a copy of the Notice by post or e-mail to all LBIE clients that the Administrators believe have a claim to Trust Assets; and
- 77.3** Publish the Notice in the Financial Times and the Wall Street Journal.
- 78** In addition to taking the above steps, the Administrators propose to invite all known Trust Asset claimants to meetings in New York and London during the week commencing 7 December 2009, at which the Administrators intend to explain the terms of the proposed multilateral contract referred to above at paragraph 31 and further elucidate the effect of the Bar Date. The Administrators also propose to continue to liaise with the LBIE creditors'

committee, in order to advertise and explain the fact and effect of the Bar Date.

G. EFFECT OF THE BAR DATE

- 79** As outlined above (paragraph 31), the Administrators now propose an approach to Trust Assets returns whereby LBIE would enter into a multilateral contractual arrangement with consenting Trust Asset claimants as regards the return of Trust Assets. However, whilst the proposed Bar Date is a central element to the potential contractual approach to Trust Assets returns, the value of the Bar Date is independent of that approach.
- 80** For instance, if the multilateral contract does not proceed (e.g. because it does not receive sufficient support from known Trust Asset claimants to satisfy the threshold conditions referred to above at paragraph 32), the advantage to the Administrators in seeking to return Trust Assets will be that bilateral agreements to return assets (for instance pursuant to the procedure employed by the Hardship and Prioritisation Committee) will be easier to progress once the proposed Bar Date has passed. At that time, if LBIE's books and records indicate that a client's claim to Trust Assets is well founded, there is no shortfall in respect of the stock line from which the relevant assets are claimed and there is no other reason for not returning the assets, then the Administrators may be in a position to return such assets to the relevant client, without requiring an indemnity or guarantee. That follows from the fact that the Bar Date protects LBIE from breach of trust claims arising out of claims to Trust Assets asserted after (post-Bar Date) distributions or appropriations.
- 81** However, the imposition of a Bar Date will not, of itself, resolve all of the issues faced by the Administrators in attempting to make distributions and appropriations of Trust Assets. For example, difficulties associated with valuing assets and liabilities will remain. That is particularly the case in so far as these issues are not (largely) overcome in respect of any given Trust Asset claimant by the application of the proposed multilateral contract.
- 82** Further, some Trust Assets that LBIE held through depositories and sub-custodians (including affiliates) are not yet within the Administrators control.

Whilst the Administrators continue actively to engage with depositories and sub-custodians to resolve the outstanding issues, it is unclear whether or not the Administrators will ultimately be able to secure control of such assets, either because there is an ongoing reconciliation exercise with the relevant affiliate or other sub-custodian in respect of the relevant Trust Assets, because LBIE's entitlement to them is disputed, or because, for example, the relevant affiliate is in an insolvency process and may not be holding sufficient assets to meet all of its obligations to deliver up assets held on trust for LBIE. It follows that such Trust Assets will not become capable of being distributed or appropriated merely because of the imposition of the Bar Date.

- 83** In addition, as regards those Trust Assets that are under the Administrators' control, many of the contracts entered into by LBIE with its clients contained security or lien provisions which purported, in addition to securing the relevant client's liabilities to LBIE, to secure the relevant client's liabilities to LBIE's affiliates. Further, I am advised that some of the custody arrangements that LBIE entered into with its affiliates (where LBIE acted as custodian) contained similar provisions which conferred a lien and power of sale over the Trust Assets not only in respect of the relevant affiliate's liabilities to LBIE, but purportedly also in respect of the relevant affiliate's liabilities to other Lehman Brothers entities.
- 84** Whilst the effect of such provisions is yet to be determined, I am advised that certain Lehman Brothers entities have suggested that the effect is that LBIE owes duties to its affiliates to retain, when making distributions to clients, sufficient Trust Assets to satisfy liabilities owed by the recipients of such distributions to LBIE's affiliates (and to retain, when making distributions to affiliates, sufficient Trust Assets to satisfy liabilities owed by the recipient to LBIE's other affiliates).
- 85** It follows that, if the Administrators make distributions or appropriations in circumstances where they cannot be certain that LBIE's affiliates do not have claims in respect of such provisions, LBIE's affiliates might subsequently bring claims against LBIE on the basis that the lien or security provisions ought to have been exercised in their favour.

- 86 This gives rise to a difficulty, since LBIE's affiliates have not yet confirmed their positions in respect of such provisions and, to the extent that they purport to have the rights described, which of LBIE's clients (or affiliates) they may have claims against. The possibility of affiliate claims under these provisions places a restriction on the ability of the Administrators to make distributions or appropriations without fear of exposing LBIE to claims, even if this Application is successful and such distributions or appropriations are made after the Bar Date. For this reason, the Administrators wrote in June to those affiliates that they believe contracted directly with clients, referring them to a list of LBIE's clients on the Administration Website and requesting that they inform the Administrators, by 31 December 2009, if they wish to assert any rights under the above provisions in respect of any particular client (and if so, to what extent). A sample copy of the relevant letter can be found at **pages 228 to 231 of "SAP6"**). Similarly, as regards the lien and power of sale provisions contained in the custody arrangements referred to above at paragraph 83, the Administrators are approaching key affiliates with a view to engaging in active dialogue as regards the extent of their claims (if any) arising under such provisions.
- 87 As noted above, due to their potential complexity and uncertainty regarding their validity, it is not intended that the Bar Date should apply to claims made by affiliates under these provisions and the relief sought has been drafted accordingly. The Administrators are giving consideration to the most appropriate method of determining the extent to which such claims impact on their ability to distribute Trust Assets to LBIE's clients and affiliates and appropriate Trust Assets to LBIE, absent responses to their letter referred to immediately above. In that regard, they have approached key affiliates with a view to engaging in active dialogue and it may be that a commercial solution (by way of compromise or information sharing arrangement) can be reached. On the other hand, it may ultimately be necessary for these issues to be resolved by way of one or more applications to the Court for directions.
- 88 It is also intended that the scope of the Bar Date be limited so as to cover only claims to segregated Trust Assets (i.e. assets that were recorded in

LBIE's books and records as at 7:56 a.m. on 15 September 2008 as being held in a segregated manner for clients of LBIE, separately from other assets held by LBIE). The Ordinary Application by which this Application is made has been drafted accordingly. It follows that, if the Court grants the Order sought, the Bar Date will not apply to claims to assets held in LBIE's house accounts.

H. BAR DATES IMPOSED IN RESPECT OF LEHMAN ENTITIES IN OTHER JURISDICTIONS

- 89** The Administrators do not consider that a Bar Date falling more than seventeen months after LBIE entered administration can reasonably be thought premature. By way of international context, if the Court grants the Order sought, it will not be the first bar date to be imposed in respect of a member of the Lehman group. In fact, bar dates have already been imposed in respect of other Lehman group entities in other jurisdictions (and several such bar dates have already passed), including those referred to below.
- 90** In the U.S., an initial customer claims bar date of 30 January 2009 was imposed in relation to LBI on 7 November 2008. I am advised that the effect of this initial bar date was that only those creditors submitting their claims by the relevant date were entitled to maximum customer protection under the relevant U.S legislation (being the Securities Investor Protection Act). An absolute bar date of 1 June 2009 was imposed, after which I am advised that creditors could only submit new claims against LBI with the agreement of LBI's trustee in bankruptcy. LBIE submitted its customer claims, including intercompany claims, against LBI in advance of the 30 January 2009 bar date and its general claims in advance of the 1 June 2009 bar date.
- 91** Also in the U.S., a general bar date of 22 September 2009 was imposed by the U.S. Bankruptcy Court for the Southern District of New York in relation to Lehman Brothers Holdings Inc. ("LBHI") and certain of its affiliates on 2 July 2009. I am advised that this bar date applies to all claims arising otherwise than from certain securities issued or guaranteed by LBHI and/or certain affiliates. I understand that a second bar date applicable to claims

arising from such securities fell on 2 November 2009. LBIE submitted its general intercompany claims against LBHI in advance of the 22 September 2009 bar date and submitted further claims arising from securities issued by LBHI on 2 November 2009. Although not a bar date, the U.S. Bankruptcy Court imposed a deadline of 22 October 2009 by which creditors were required to submit supplemental information regarding certain derivatives and guarantee claims. LBIE submitted the required information in compliance with this deadline.

- 92 In Japan, a bar date of 21 October 2008 was imposed in relation to claims against Lehman Brothers Japan Inc ("**LBJ**"), whereby I am advised that creditors were required to file their claims by that date, failing which such claims would not (subject to the following) be taken into account in the insolvency proceedings to which LBJ is subject. I am advised, however, that in the context of Japanese insolvency proceedings: (i) the relevant creditor may complete (or amend) his/her claim after the bar date only when he/she was unable to file its claim (or do so accurately) by the bar date due to grounds not attributable to himself/herself; and (ii) such completion (or amendment) should be done within one month after those grounds cease to exist. Accordingly, LBIE submitted an initial claim in LBJ's insolvency proceedings on 21 October 2008, and submitted an amended claim on 26 December 2008.
- 93 Further, in Switzerland, a bar date of 27 February 2009 was imposed in relation to claims against Lehman Brothers Finance S.A. ("**LBF**"). I am advised that the effect under Swiss law of such a bar date is that, after the bar date, the amendment of a submitted claim, leading to an increase of amount being claimed, is only possible if the amendment is based on new circumstances, which the creditor was not able to bring forward in the first submission and the submission of new claims, which are based on different factual or legal grounds is possible, but the additional costs have to be assumed by creditor. Throughout the bankruptcy proceedings certain preferential rights of creditors may be lost in circumstances where the creditor's failure to notify counterclaims of LBF in a timely manner

constitutes a malicious violation of the notification obligations. LBIE submitted its claims against LBF prior to the 27 February 2009 bar date.

I. CONCLUSION

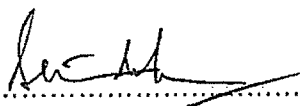
94 In conclusion, in light of (i) the difficulties associated with determining with certainty the full population of Trust Asset claimants; (ii) the risks to the Administrators and to LBIE associated with making distributions and appropriations of Trust Assets in the absence of such determination; and (iii) the potential resultant delays to the return of Trust Assets to their beneficial owners, the Administrators respectfully suggest that, in the circumstances, the step of imposing the Bar Date described above is appropriate.

95 The Administrators respectfully invite the Court to make the Order sought.

STATEMENT OF TRUTH

I believe that the facts stated in this witness statement are true.

Signed:



STEVEN ANTHONY PEARSON

26 November 2009

Appendix A

Current approach to the return of Trust Property

- 1 Whilst the complexity of the administration of LBIE has meant that the Administrators have not been able to accede to many of the requests for prioritised return of Trust Assets, the Administrators are keen to return Trust Assets as expeditiously as possible and are sympathetic to the difficulties faced by clients as a result of uncertainty regarding whether and, if so when, they will receive their property.
- 2 Enshrined in the Schedule to the Trust Property Order (the "**Schedule**") was the concept of the prioritised return of Trust Property to certain claimants. Paragraph 2.2 of the Schedule envisages the setting up of a sub-committee with the remit of reviewing the principles applicable to the prioritisation of the determination of the claims of particular counterparties (by identifying, where appropriate, high profile problems or hardship issues, to ensure that the overriding objective of treating all counterparties fairly is not prejudicial to the interests of a minority or that there is not otherwise a problem that requires specific and accelerated attention). Such a sub-committee (referred to as the "**Hardship and Prioritisation Committee**") has been set up in accordance with the Schedule and has been meeting regularly ever since the making of the Trust Property Order.
- 3 The Hardship and Prioritisation Committee considers each case in accordance with the principles set out in the Trust Property Order, but in many cases it is not possible for assets to be returned as requested.
- 4 In light of the difficulties and complexities described above, and in order to ensure consistency with the Trust Property Order, an asset will only be returned where the following conditions have been satisfied:
 - 4.1 the case must be one which is appropriate for prioritisation (whether on the basis of hardship or otherwise) in accordance with the principles set out in the Trust Property Order;
 - 4.2 the client must have provided adequate information and documentation in order for its claim to be analysed and substantiated;

- 4.3** a reconciliation of the information received from the client must be undertaken with the data held on LBIE's systems and the data received from the relevant depository or sub-custodian. It must be sufficiently clear from this exercise that the assets to which the client is claiming to be entitled are, in fact, held on trust by LBIE for that client. There must be no evidence of a relevant shortfall;
- 4.4** as part of the process of reconciling the data received from the client with that held by LBIE and received from the relevant depository or sub-custodian or affiliate, it is necessary to check that the depository or sub-custodian in fact holds the Trust Asset in question and is willing and able to transfer it to LBIE's client. The Administrators do not yet have access to assets which are held by certain depositories or sub-custodians;
- 4.5** the entirety of the particular client's relationship with LBIE must be analysed and understood. As set out above, most of the documents pursuant to which LBIE holds Trust Assets provide for security rights in favour of LBIE. Whether or not it will be appropriate for LBIE to release all or some of the relevant Trust Assets will therefore depend upon the client's overall position with LBIE. For some clients, this will involve a detailed review of a range of complex documentation and relationships with LBIE. If there is any uncertainty as regards whether, or the extent to which, the client is indebted to LBIE, and therefore as regards whether, or the extent to which, LBIE has a security interest that it may wish to exercise, it will not be possible for that client's assets to be returned. In the event that the legal review of the contracts governing the client's position gives rise to uncertainty as regards whether or not the client is entitled to the return of the assets in question, it will not be possible for that client's assets to be returned; and
- 4.6** the net liabilities of the relevant client must accordingly be capable of being ascertained and have been agreed as between LBIE and the client. Where the client has unterminated positions, this will include an agreed close-out and valuation of such positions.

- 5 The Administrators have devoted significant resources to requesting relevant information from clients and locating relevant documents and data so that the Administrators may conduct a line-by-line reconciliation of the client's position. From the total number of Trust Assets claims, 281 are under review for the potential expedited return of assets (the remainder cannot currently be progressed due to the nature of the relevant claims; for example, because they are claims in respect of pre-administration client money). However, as explained in my second witness statement (dated 25 February 2009), there are inherent short-comings in the approach to expedited asset returns currently available to the Administrators and many creditors have been unable to meet the requirements for such returns.
- 6 The need to seek indemnities and credit support from clients was explained in detail in my second witness statement (see paragraphs 76 to 86). I repeat below the terms of the deeds of undertaking pursuant to which assets are currently returned and the inherent difficulties caused by having to insist upon such terms.
- 7 The Administrators, together with their staff and advisers, have put in place a framework requiring clients to enter into deeds of undertaking in order that assets can be returned without exposing the LBIE estate and/or the Administrators to additional risk. Appropriate return and indemnification arrangements and, if necessary and subject to *de minimis* threshold, credit support for those arrangements are an essential part of this framework and, subject to exceptional circumstances, all clients whose claims are processed on this basis are required to enter into such arrangements. Note that, as at the date of my second witness statement (i.e. 25 February 2009), the *de minimis* threshold also applied in relation to the applicability of the return and indemnification arrangements.
- 8 The Administrators' objectives in seeking such protection are to ensure that:
 - 8.1 in the event that it is determined that returned assets should not have been returned, for example where it emerges that the returned assets were, in fact, the subject of competing claims, the client asset position and the LBIE estate are able to be restored (as far as

practicable) to their respective positions had those assets not been returned on an expedited basis;

8.2 the client whose claim is prioritised contributes to the cost of prioritisation (and that neither the LBIE estate nor the LBIE clients as a whole should be burdened with costs associated with a prioritised return); and

8.3 the pool of clients (and their assets) to which the costs of administering and dealing with Trust Property generally might be allocated is not diminished.

9 The arrangements approved by the Administrators in furtherance of these objectives have varied on a case by case basis and will continue to do so and the terms of such arrangements have developed as the process of returning assets to clients has progressed. However, in summary, the current arrangements are as follows:

9.1 if the Administrators, acting in good faith, subsequently determine that any assets transferred on an expedited basis (the "**Transfer Assets**") should not have been so transferred, the transferee will be obliged:

9.1.1 to return such proportion of the Transfer Assets or equivalent securities as the Administrators determine should not have been transferred;

9.1.2 to pay an amount to LBIE equal to any proceeds earned on those assets since the date of the transfer; and

9.1.3 to pay the amount, if any, notified by LBIE as the amount of interest it would have earned on those proceeds.

(These sums, together, are referred to as the "**Return Amount**".)

9.2 in the event that the transferee fails to pay any or all of the Return Amount, the transferee will be liable to pay an amount in respect of such failure calculated as the sum of:

- 9.2.1 the actual or estimated cost to LBIE of acquiring replacement assets in the market;
- 9.2.2 the proceeds that should have been returned to LBIE and any interest LBIE would have earned on those proceeds; and
- 9.2.3 the costs incurred by the LBIE estate and/or the Administrators as a result of the transferee's failure to pay the Return Amount;
- 9.3 if deemed appropriate by the Administrators, credit support in an agreed form is required. The guaranteed obligations in these circumstances include any indebtedness owed to any Lehman Brothers entity that would otherwise have been covered by a lien over the Transfer Assets;
- 9.4 save as provided in the sub-paragraph immediately above, the transferee must warrant to LBIE that it has no liabilities to LBIE affiliates;
- 9.5 the transferee pays a fixed sum contribution towards the cost of prioritising its claim (for a straightforward claim this is set at U.S.\$50,000);
- 9.6 a retention of between 0.75% and 1% of the Transfer Assets will be held by LBIE pending determination of the amount (if any) of costs incurred in returning assets which are to be charged to the Transfer Assets, following which determination such amount will be applied towards satisfying such charge, and any excess together with any interest earned on that retention will be returned to the transferee. Note that, as at the date of my second witness statement (i.e. 25 February 2009), the retention being applied was of between 0.75% and 1.25% of the Transfer Assets;
- 9.7 the transferee will agree to pay any amount by which the retention held by LBIE (together with any interest earned on that retention) is insufficient to satisfy the obligation of the transferee to pay the amount of such costs determined to be charged to the Transfer Assets.

- 10** If the client agrees that it is willing to proceed on the above basis, a draft deed of undertaking is forwarded to and discussed with the client. For commercial reasons this cannot be an indefinite undertaking, but needs to run for sufficiently long to accommodate possibly unknown claims. The Administrators take the view that this should be for a number of years. Once agreed and upon any conditions having been fulfilled, the asset is returned to the client.
- 11** In the event that the client decides that the above requirements are unacceptable, the client's claim for the return of Trust Property is likely to be dealt with in due course with other non-prioritised LBIE clients i.e. in the ordinary course of the administration.
- 12** The Administrators recognise that the current approach to expedited Trust Assets returns is unsatisfactory in certain respects and will not meet the principal needs of clients. For instance, it does not provide any finality to clients, since they remain liable under the undertaking for a number of years. Further, the requirement for external credit support may be hard to meet, particularly for clients who are themselves experiencing financial difficulties. The Administrators understand that clients may be unable to provide such credit support without pledging the returned asset, which largely defeats the purpose of having the asset returned, at least for the duration of the undertaking.
- 13** The Administrators have tried to accommodate this by not always asking for credit support in respect of 100% of the value of the undertaking, but this creates some limited risk for the estate and is only appropriate where the Administrators have a very high degree of confidence that (at least from the books and records of LBIE) there are unlikely to be competing claims and so the risk is low. However, the risk of competing claims cannot be entirely eliminated in the present circumstances.
- 14** As a result of the large number of issues affecting any given asset and the amount of work that needs to be done by the Administrators, their advisers and Lehman staff in respect of any given potential return, the current approach is inevitably time consuming and costly. Further, it is likely that going forward much more difficult cases will emerge which are not

amenable to this current approach (either as a result of their complexity, or the issues identified above). Some of the above issues may only be capable of resolution through obtaining further directions from the Court or contested litigation.

- 15** In the absence of a viable alternative the Administrators continue to apply the approach described above and in my second witness statement. However as a result of the inherent difficulties described, as at 20 November 2009 there are 165 accounts (held by 116 LBIE clients) where the Administrators are in a position to return assets that are under the Administrators' control. In many instances, however, discussions with these account holders have been ongoing for many weeks, if not months. In these situations, many of the clients are either unable or unwilling to comply with the terms for distribution which the Administrators consider themselves obliged to apply.
- 16** Even where clients are able and willing to comply with the terms set out above, it remains a time consuming and costly process to investigate positions on a client-by-client basis and to then agree and document the appropriate terms for the return of particular Trust Property.

Applicants
S A Pearson
Sixth Statement
"SAP6"
26 November 2009

No. 7942 of 2008

IN THE HIGH COURT OF JUSTICE

CHANCERY DIVISION

COMPANIES COURT

IN THE MATTER OF LEHMAN BROTHERS
INTERNATIONAL (EUROPE) (in administration)

AND IN THE MATTER OF THE INSOLVENCY ACT
1986

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