

Lehman Brothers International (Europe) (In Administration)

Update to MFA members

Update to AIMA members

New York – 16 November 2010

London – 19 November 2010

Agenda

1. Executive summary
2. Trust Assets and CRA returns
3. Client Money update
4. Unsecured creditor claims agreement – the Consensual Approach
5. Currency matters
6. Next steps in 2011
7. Q&A

1. Executive summary



Executive summary

Overview

Trust Assets

- As at 14 September 2010:
 - £1.7bn of assets returned under the CRA since the bar date of 19 March 2010
 - Returns to non-CRA clients of £8.4bn since administration
 - £3.6bn of securities remained under LBIE's control with £2bn+ pipeline of returns planned for Q4 2010
- LBI Determination of the client omnibus claim for securities received on 16 Sept 2010 – LBIE undertaking review
- Trust asset over-claims of c.£7bn under investigation
- CRA small claims project initiated – targeting the return of 1,145 stocklines each valued in aggregate at less than \$50k shared between 69 counterparties

Executive summary

Overview

Client Money

- Court of Appeal overturned Dec 2009 High Court judgment:
 - LBIE's House asset pool and unsecured creditors materially affected
 - Onus on LBIE to identify liabilities which should have had Client Money protection and traceable assets to increase the Client Money pool – extremely time consuming and costly
 - Permission sought to appeal to the Supreme Court
 - Substantial delay in Client Money and unsecured claims distribution
- Started analysis in parallel to determine potential additional Client Money claimants
- Claim against Bankhaus for return of \$1bn of Client Money – rejected by German court

Executive summary

Overview

Consensual Approach

- Accelerated approach to claims agreement process
- Optional framework for financial trading counterparties to agree their claims against LBIE now developed and ready to commence
- Modified original approach given Client Money uncertainty – focus on agreeing overall claim amount with any Client Money adjustments later

Currency matters

- CRA assets and claims are denominated in US Dollars
- Under UK insolvency law, all unsecured claims must be converted to Sterling using the exchange rate prevailing on 15 September 2008
- Sterling conversion of House cash halted following Court of Appeal Judgment
- Client Money funds are largely denominated in US Dollars

2. Trust Assets and CRA returns



Trust Assets and CRA returns

Claim Resolution Agreement (“CRA”)

- CRA launched in November 2009 – approved by over 90% (by value) of qualifying counterparties – became effective in December 2009
- Provides a common framework to return Trust Assets and determine the unsecured claims of Signatories
 - Standard methodology to expedite the return of trust assets
 - Full and final settlement of asset claims, without need for collateral
 - Termination and valuation of financial contracts
 - Discharge of counterparty net financial liabilities
 - Collateralisation options
 - Mechanisms to deal with affiliate liens
 - Dispute resolution mechanism
 - Crystallises unsecured claim to be paid by the estate of LBIE in due course

Trust Assets and CRA returns

Claim Resolution Agreement (“CRA”)

- CRA assets under LBIE’s control were £3bn at 19 March 2010 (bar date)
- Returns impacted by over-claims, affiliate liens and LBI exposures which reduce the “addressable population”

As at 10 September 2010	Returns made	Claim Agreement Notices (“CANs”)
Value returned / issued	£1.7bn	£2.3bn
% of addressable population	84%	89%
No. of counterparties	51	212
% of addressable population	53%	96%

- Built infrastructure to improve volume throughput – IT and Legal
- Small assets initiative launched – remaining CRA population skewed towards high volume of lower value assets
- Strong pipeline of future asset returns currently in negotiation

Trust Assets

Non – CRA signatories

- Different approach required to the CRA process
 - Asset returns handled via bespoke bilateral agreements
 - Separate team in place – distinct skill sets and processes are required
 - Returns process necessarily more time consuming and convoluted
- At 14 September 2010, £8.4bn returned to counterparties – YTD returns are £0.6bn
- We are at an advanced stage of negotiations for the return of a further £2bn of securities – lien issues required resolution
- Remaining assets within control of £0.6bn will be more difficult to release
 - Affiliate liens asserted
 - Account ownership disputes
 - Securities tainted by over-claims
 - As with the CRA population there is a long tail of low value asset lines to be returned

Trust Assets and CRA returns

Over-claims

Over-claims	£'bn	%	No.	%
Within LBIE control	2.9	40%	209	57%
Outside LBIE control	4.4	60%	157	43%
Total	7.3	100%	366	100%

- Following the bar date, £7.3bn of claims were received in excess of entitlement shown in LBIE's records
- Obligation to scrutinise all claims to establish their validity. Pending resolution, assets subject to claim are fully reserved
- Over-claims largely relate to rehypothecated assets where LBIE considers the claim to be unsecured and would rank *pari-passu* with other unsecured claims
- By 14 September 2010, £0.4bn of over-claims on assets within LBIE's control had been addressed. LBIE records proved correct
- Resolution path for some over-claims will likely require legal process
- Ongoing LBI reconciliation will reduce over-claims on assets outside of LBIE's control

Trust Assets and CRA returns

LBI Customer Property omnibus claim

- LBI determination for the omnibus claim was issued on 16 September 2010 in respect of 5,059 securities. The LBI Trustee's latest report valued this at \$6.2bn, subject to conditions
- In support of the determination LBI has provided over 5,000 detailed security reconciliations. At the date of LBIE's report we expected templates for a further 1,000 securities
- From the information received to date LBIE has identified differences on over 1,200 securities which have been referred back to LBI. Both parties continue to work together to resolve these issues
- In addition to working with LBI, LBIE has also provided data to its underlying clients so as to expedite the overall reconciliation process
- LBI has set a 90-day objection period (to 14 January 2011) for the omnibus claim
- No determination for cash has been issued to date. LBIE and LBI continue to exchange information to progress this element

Trust Assets and CRA returns

Next steps

- Drive resolution on a number of external blockers impacting CRA asset returns
- Complete CAN issuance programme
- Progress asset returns – CRA and bilateral negotiations
- Joint programme with LBI to address
 - Securities reconciliations
 - Cash determination
 - Objection deadline for 14 January 2011

3. Client Money update



Client Money

Topics for discussion

- Pre-administration Client Money
 - Court of Appeal judgment
 - Bankhaus claim

UK Court of Appeal – Client Money Judgment

Pre-Administration

Initial judgment – December 2009

- Only clients for whom money was segregated may claim against the Client Money pool:
 - Client Money entitlements calculated at date of Administration
 - LBIE is not required to “top up” Client Money pool
- Clients may seek to trace into other LBIE assets to increase their own Client Money recovery

Court of Appeal – August 2010

- Court of Appeal overturned certain key findings in High Court’s judgment:
 - ① Identifiable Client Money (including through tracing exercise) outside of segregated accounts must be added to Client Money pool
 - ② All counterparties (including affiliates) who should have had Client Money protection – irrespective of whether they actually had it – are all entitled to claim against the Client Money pool
- Burden on LBIE to identify traceable assets and additional Client Money entitlements rather than wait for client claims
- All clients benefit from tracing, not just individual clients

Impact

- Much additional work – (i) extremely time consuming and costly; and (ii) uncertainty of assets and extent of Client Money claims
- Permission sought to appeal to the Supreme Court
- Substantial delay in Client Money and unsecured distributions

Client Money

Cash held by Bankhaus

Bankhaus

- LBIE filed a claim against Bankhaus for the return of \$1bn of client monies deposited immediately prior to Administration
- Hearing was held in Germany on 7 October 2010 resulting in LBIE's petition for "Trust" status being dismissed
- Further, the German court ruled that LBIE's claim be subordinated
- LBIE plans to appeal - without a successful appeal there is a low likelihood of any financial recovery
- Counterclaim from Bankhaus – hearing in December 2010

Client Money

Next steps

Areas of focus

- Response to Court of Appeal
 - applied for leave to appeal to Supreme Court – due to hear during next few weeks whether appeal can be made – but hearing likely to be in late 2011
 - scope and implement Client Money tracing and claims identification exercise
 - quantify the potential level of “Client Money taint” and impacting the House cash pool
- Bankhaus
 - pursue appeal against Bankhaus, defend counter-claim

4. Unsecured creditors claims agreement – the Consensual Approach



Unsecured creditors claims agreement – the Consensual Approach

Consensual Approach – overview

Type	No. of cpties		LBIE current book value, £'bn
Unsecured creditors	3,490		(4.8)
Trust unsecured	326	CRA	(3.9)
	479	Non-CRA	(1.7)
Total	4,295		10.4

Note: the above table excludes affiliates and other third party unsecured creditors

- Accelerated approach to claims agreement
 - intended to save time and cost
 - optional
 - designed for non-CRA, non-affiliate creditors
- Original intention was to commence unsecured claim admission in 2010 and pay a dividend in 2011
 - focus shifted following Client Money appeal judgment
 - formal “admission” of unsecured claims is not possible at this stage due to the recent Appeal Court judgment in respect of Client Money
 - unsecured dividend payments could be substantially delayed

Unsecured creditors claims agreement – the Consensual Approach

Consensual Approach – key principles

- Key issue is uncertainty as to what constitutes a Client Money liability
 - likely to be a significant period of time before this is fully clear unless Court of Appeal judgment reversed
- In the meantime, priority is to **agree** claims, but not (yet) **admitting** them
 - filed proof of debt required
 - agreement of a counterparty's total claims against LBIE
 - converts claims under a number of master agreements to one net number
 - preserves all Client Money rights
 - claims are not admitted for unsecured dividend purposes until any potential Client Money claim is resolved
- Claim is freely tradeable upon notice to LBIE – only acknowledgement is required – consent is automatic

Unsecured creditors claims agreement – the Consensual Approach

Consensual Approach – progress

- Extensive engagement with counterparties
 - Unsecured financial trading counterparties (non-trust) total £4.8bn (3,490 counterparties)
 - Extensive dialogue with counterparties with largest and most complex claims - £3.6bn of value
 - By 14 September 2010, 477 proofs of debt submitted (totalling £2.9bn)
- Significant progress in reconciling creditor positions
 - £3.4bn reconciled at a portfolio level (748 counterparties); £2.0bn fully valued for purposes of Consensual Approach
- Now commenced making offers to counterparties

Unsecured creditors claims agreement – the Consensual Approach

Dealing with other creditors

Summary

1. **Creditors with Trust Assets:**

- CRA – follow process already agreed – no intention to vary CRA valuation principles
- Process ongoing and in parallel to Consensual Approach
- If possible, non-CRA trust creditors can be included in Consensual Approach – but depends largely on LBI asset claims

2. **Affiliates:**

- Generally too complex for Consensual Approach – bilateral negotiations underway with key affiliates

3. **Other creditors:**

- Conventional UK insolvency debt proving process and bilateral claim agreement

Unsecured creditors claims agreement – the Consensual Approach

Next steps

- Creditors are encouraged to submit proofs of debt to be eligible for Consensual Approach
- Given Client Money uncertainty, plan to seek to extend proposed first distribution by two years
- Claims agreement to proceed under the Consensual Approach and for other creditors in parallel

5. Currency matters



Currency matters

Summary

- CRA assets and claims are denominated in US Dollars
- Given LBIE is a “Distributing Administration”, the application of UK Insolvency law is such that all unsecured claims (including CRA Net Ascertained Claims) must be converted into Sterling at the exchange rate as at 15 September 2008
- Funds in hand are realised in multiple currencies
- Commenced conversion of House cash into Sterling consistent with the approach of admitting and paying dividends to unsecured claims in Sterling – mitigating foreign exchange currency risk
- Conversion of House estate halted following the Appeal Court Judgment – to avoid risk of converting Client Monies
- Currency holding as at 14 September 2010:
 - Sterling: £4.8bn
 - Euro: €2.5bn
 - US Dollar: US\$1.7bn
 - Other currencies: £0.1bn

6. Next steps in 2011



Next steps in 2011

Areas of focus

- **Trust Assets:**
 - Progress resolution of over-claims and other taints on securities, recover assets from LBI and return to claimants
- **Client Money:**
 - Appeal to Supreme Court
 - Scope and implement Client Money tracing and claims identification exercise
 - Quantify the potential level of “Client Money taint” and impacting the House cash pool
- **Formally agree unsecured claims** against LBIE through:
 - CRA;
 - Consensual Approach; and
 - Bilaterally (including non-CRA), where appropriate

Questions