

Appellant
David Philip Ereira
Third Statement
"DPE3"
21 October 2009

IN THE COURT OF APPEAL
(CIVIL DIVISION)

Court of Appeal No.
A2/2009/1994

ON APPEAL FROM THE HIGH
COURT OF JUSTICE

No. 7942 of 2008 and Claim
No. 16389 of 2009

CHANCERY DIVISION

COMPANIES COURT

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

AND IN THE MATTER OF THE INSOLVENCY ACT 1986

AND IN THE MATTER OF THE COMPANIES ACT 2006

**WITNESS STATEMENT OF
DAVID PHILIP EREIRA**

I, DAVID PHILIP EREIRA, of Linklaters LLP, One Silk Street, London EC2Y 8HQ,
state as follows.

A. INTRODUCTION

1 I am a solicitor and a partner in Linklaters LLP ("**Linklaters**"), a law firm at the above address. Linklaters acts for the joint Administrators of Lehman Brothers International (Europe) ("**LBIE**") (in administration) (the "**Administrators**"). I have been working with the Administrators since the commencement of LBIE's administration on 15 September 2008. I am duly authorised to make this witness statement on behalf of LBIE and the Administrators.

- 2 I make this witness statement in support of LBIE's and the Administrators' appeal against the Order of the Honourable Mr Justice Blackburne, dated 21 August 2009, declaring that, insofar as the scheme of arrangement proposed by them (the "**Scheme**") is concerned with the distribution by LBIE of property held or controlled by it on trust for any of its creditors, and to the extent that the Scheme varies or extinguishes the property rights of such creditors, the Court has no jurisdiction under Part 26 of the Companies Act 2006 to sanction it.
- 3 In particular, this witness statement is made in order (i) to update the Court on certain matters addressed in my witness statement of 14 July 2009 ("**Ereira 2**"), which was made in support of the "jurisdiction" application which was heard on 29 and 30 July 2009, most notably the issue of what progress has been made to identify alternatives to the Scheme that might be available to expedite the return of trust assets, and (ii) to clarify certain aspects of the proposed Scheme which have been highlighted in the skeleton argument filed by the London Investment Banking Association ("**LIBA**") in this appeal.
- 4 Where I give no 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. Nothing in this witness statement is intended to waive privilege in respect of any matter referred to and privilege is not being waived.
- 5 There is now shown to me a paginated bundle of copy documents, marked "**DPE3**", to which I refer in this witness statement.
- 6 The remainder of this witness statement is divided into the following sections:
- Section A: Alternatives to the Scheme
- Section B: Clarification of the proposed Scheme.
- A: ALTERNATIVES TO THE SCHEME**
- 7 In Ereira 2, I explained the significant difficulties that would be faced by the Administrators in the event that the Scheme could not be pursued. I

explained that the continuing uncertainty over competing claims and entitlements would mean that the Administrators would have no option but to continue negotiating the return of assets on a bi-lateral basis, requiring indemnities and credit support as a pre-condition to the return of assets. Unless alternative protection can be obtained for LBIE and the Administrators, only once sufficient time has passed and sufficient information has been obtained as to afford the Administrators a high degree of assurance that further claims will not emerge will it be feasible for assets to be returned on a bi-lateral basis without indemnities and credit support. I also suggested that it might be possible to promulgate an alternative scheme of arrangement or to make a series of applications to Court in order to resolve some of the issues that would have been dealt with by the Scheme, but that these alternatives would involve significant further delay.

- 8 The expeditious return of trust assets remains a key priority of the Administrators and they are anxious to ensure that, whatever the ultimate outcome of the appeal in relation to the Scheme, they are able to implement a process for returning assets in a timely manner. Accordingly, in light of Mr Justice Blackburne's Order, the Administrators have been giving active consideration to alternative solutions for the return of trust assets.
- 9 The Administrators remain of the view that the Scheme represents the most fully encompassing solution for dealing with the return of trust assets and, if it can be achieved, it remains their preferred solution. However, in the course of their considerations, they have identified a number of different routes that could be pursued, either in isolation or in combination with one another, which would achieve certain of the objectives which the Scheme would achieve. These options were outlined in an update on the PricewaterhouseCoopers LLP ("PwC") website posted on 5 October 2009, a copy of which is at **pages 1 to 7 of DPE3**. The options described have been the subject of discussion with members of the Managed Funds Association (the "MFA") and the Alternative Investment Management Association ("AIMA") in meetings in New York and London on 8 and 9 October 2009, as well as with members of the Scheme working group. Following the meetings with the MFA and AIMA, an updated website

posting, including a link to the presentation given to the MFA and AIMA, was placed on the PwC website. A copy of this posting (including the presentation) is contained at pages 8 to 43 of DPE3.

- 10** On the basis of the analysis and discussions that have taken place to date, the Administrators currently believe that the most viable alternative solution to the Scheme is a multi-lateral contractual compromise (referred to in the 5 October website update as the “contractual solution”), most likely combined with a court application (referred to in the 5 October website update as a “bar date application”). As explained in the website update, creditors would be invited to bind themselves voluntarily to a contractual settlement, the provisions of which would be substantially the same as those contained in the proposed Scheme. In broad terms, it is anticipated that 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 would be very similar to those contained in the Scheme.
- 11** However, although based upon the terms of the proposed Scheme, it is envisaged that the contractual settlement will necessarily differ from the Scheme in certain respects. In addition to the obvious consequential amendments that will need to be made as a result of the change in structure (e.g. regarding an offer period for the contract and termination provisions), based upon the work undertaken to date, the Administrators anticipate that the key difference will relate to the provisions regarding allocations.
- 12** It is anticipated that the contractual provisions in relation to allocations will need to differ from those contained in the Scheme, to take account of the fact that non-signatories (who will not be bound by the contract) may raise challenges or bring claims in relation to distributions of assets by LBIE under the contract. In order to commence the return of assets as soon as practicable, it is currently envisaged that the contractual solution will provide for a phased distribution, with the ability (i) to distribute stock-lines where there is no shortfall (or stock-lines where there is a shortfall but all

holders of that line of stock are signatories) before stock-lines where there is a shortfall and those stock-lines are held by non-signatories; and (ii) to put assets aside in reserve, where a non-signatory has asserted a claim in respect of a stock-line in respect of which there is a shortfall, pending resolution (whether by agreement, order of the court or otherwise) of the non-signatories' entitlements. In addition, in order to assist with the administration of trust property and protect LBIE and the Administrators from claims (by unknown claimants) for breach of trust, it is anticipated that a bar date application will be made to Court (as to which, see further below).

- 13** The key drawback with the contractual solution is that it cannot bind non-signatories. Accordingly, in order to be viable as an alternative to the Scheme that is acceptable to trust property claimants (e.g. as regards the level of risk of claims from non-signatories), it is critical that a large proportion of trust property claimants sign the contract. Self-evidently, the greater the number of claimants who agree to be bound by the contractual compromise, the lower the risk that LBIE, the Administrators and the recipients of the trust property could find themselves exposed to claims from non-signatories as a result of the actions taken in accordance with the contract. One of the purposes in holding meetings with industry bodies and the Scheme working group and in publishing regular updates on the website is to gauge opinion on the level of support that the contractual solution (and other possible options) might garner. On the basis of the feedback obtained to date, the Administrators believe that, subject to the contract containing satisfactory terms on a number of open issues, it may be possible to obtain the support of a sufficient proportion of trust property claimants.
- 14** It has only been possible for the Administrators to give serious consideration to the proposal of a multi-lateral compromise as a result of newly acquired factual information regarding the level of likely shortfalls in trust property within the Administrators' control. As indicated in the website update of 5 October 2009, the Administrators estimate that, of the US\$8.9 billion of securities (as valued at 30 June 2009) currently under their control

(i.e. excluding assets currently held by Lehman Brothers, Inc. ("LBI") and certain other affiliates and third party sub-custodians), a shortfall of less than \$300 million is expected. On the basis of this information, the Administrators anticipate that, once the bar date has passed, LBIE will be able to distribute a significant proportion of trust assets without needing to resolve issues regarding the sharing of shortfalls. Issues regarding the sharing of shortfalls as between signatories and non-signatories can be postponed until a second phase of distribution, thus allowing the contractual solution to provide a potentially workable option, particularly for creditors whose stock lines are unaffected by shortfalls. As noted above, the Administrators do not yet have control of assets held by LBI or certain other sub-custodians. I explain at paragraph 23 below why the insolvency process relating to LBI results in the need for a separate asset pool and why the Administrators believe that, should there be a shortfall in assets held by LBI (which is currently unknown), this should not create an issue as between signatories and non-signatories, given that any entitlements are to a pro rata distribution of an omnibus pool of customer property.

- 15 Although the contractual solution may provide a workable alternative to the Scheme, it has significant disadvantages as compared to the Scheme. As indicated above, both LBIE/the Administrators and the signatories to the contract will be exposed to risks of claims from the non-signatories. For this reason, the contractual solution will not be able to achieve the same degree of finality as that provided for by the Scheme. In addition, it is likely that one or more Court applications will need to be made in due course, to resolve any outstanding issues regarding entitlements raised by non-signatories (i.e. as part of the second phase of distribution).
- 16 As noted above, the Administrators are also considering making an application to Court (referred to in the 5 October update and above as the "bar date application"), in order to obtain directions to assist them in the administration of trust property. It is currently proposed that the bar date application be progressed in parallel to, and irrespective of the outcome of, either the appeal or the contractual solution (although it is unlikely that the contractual solution would proceed without the bar date application).

- 17 The aim of such an application would be to achieve a greater level of certainty with respect to LBIE's obligations as trustee in respect of claims to trust property faced by LBIE. In particular, the application would seek to protect LBIE and the Administrators should LBIE distribute assets on the basis of information known to LBIE at a date reasonably proximate to the date of distribution. It is important to appreciate, however, that although an application of this type will provide some assistance to the Administrators, it cannot provide finality or certainty in the way that the bar date within the Scheme would do. Although an order pursuant to a Court application of this type will provide protection to LBIE and the Administrators in respect of breach of trust claims brought by trust property claimants in respect of whom they had no knowledge as at the date of distribution, such an order will not afford protection to trust property claimants to whom assets have been distributed.
- 18 It has been suggested by both LIBA (in its skeleton argument filed in respect of this appeal) and Mr Justice Blackburne (at paragraph 77 of his judgment) that it would be possible to achieve the same outcome as that provided for in the Scheme by means of a series of applications to Court by LBIE as trustee. Having given serious consideration to this issue, the Administrators do not believe that this route provides a comparable, or reasonably workable, solution. In particular, bearing in mind the very large number of potentially interested parties and the need for any determination to be binding on those parties, the size and complexity of any application (or, more likely, series of applications) of the type suggested by LIBA cannot be overestimated. By way of example, resolving the many issues relating to the calculations of financial positions under the relevant contracts would likely involve the determination of a number of generic issues, as well as whatever fact specific issues counterparties saw fit to raise. The facts in relation to each counterparty may differ, relevant information could be hard to obtain and the identification of appropriate representative respondents would be problematic.
- 19 In addition, the Administrators do not believe that there is a single, free-standing application that would provide a comprehensive solution to the

various issues that would have to be resolved in relation to trust property, in order to be able to distribute assets. The above factors, combined with the desire to return assets as expeditiously as possible, has led the Administrators to conclude that, as matters currently stand, a series of applications to the court does not represent a practical alternative to the Scheme.

B: CLARIFICATION OF THE PROPOSED SCHEME

- 20** The skeleton argument filed by LIBA in relation to this appeal contains a number of observations and, in certain cases, criticisms in relation to the proposed Scheme. Although I do not propose to deal with each of the points made by LIBA I attempt in the following paragraphs to clear up certain areas of apparent uncertainty in an attempt to ensure that the Court has a clear picture as to what is intended to be done through the Scheme.
- 21** In paragraph 55 of LIBA's skeleton argument, it is asserted that the fact that clients of LBIE could waive their monetary claims against LBIE (with the result that they would not be creditors of LBIE) means that the Scheme is unworkable. This assertion is simply not correct. Putting to one side the inherent improbability of clients adopting that course, the Scheme can if necessary provide that, where there has been such a waiver by a client, the amount of stock claimed by that client will be set aside by way of reserve pending the resolution of that client's entitlement. There would be no distributions of such reserved stock until any disputes over entitlements to that stock had been resolved.
- 22** Contrary to the suggestion in paragraph 68 of LIBA's skeleton argument, the Scheme does not extinguish a creditor's right (to the extent it can establish one) to trace into property held in LBIE's proprietary (or "house") accounts. The preservation of the right to trace is described at page 30 of the Scheme Summary.
- 23** Paragraphs 76 to 84 of LIBA's skeleton argument contain a description of, and commentary on, the three asset pools that the Scheme (at least as it is currently drafted) envisages there will be for the purposes of calculating entitlements and distributions. The "Custody Securities" pool and "Non-

Custody Securities" pool are intended to reflect the manner in which LBIE recorded the holding of client assets prior to its administration. As regards the "Affected Asset" pool, it is important to appreciate that the decision to create a separate pool was done out of necessity, to reflect the fact that LBI (and possibly other affiliated entities that are in insolvency processes of their own) is under no strict obligation to deliver particular securities to LBIE in satisfaction of what might, before the onset of insolvency, have been claims to particular securities. The Administrators have been liaising and continue to liaise with the trustee appointed in respect of LBI as regards distributions of securities. However, as I understand it (based on information provided by my New York colleagues and third parties), upon entry into its insolvency process under the Securities Investor Protection Act of 1970, as amended ("SIPA"), claims by clients of LBI (other than claims for the return of securities held in the name of such clients (i.e. "customer named securities") rather than in the "street" name of LBI) have, as a general rule, been converted into "net equity" claims, which entitle clients to recover a pro rata distribution of an omnibus pool of customer property based on the cash and securities owed to such clients as of the commencement of LBI's SIPA liquidation. I understand that LBI does not hold any customer named securities for LBIE's clients. The net equity claims can be satisfied (at the discretion of the SIPA trustee) by the delivery of securities (although not necessarily of the same stock-line as that deposited with LBI), by the payment of cash in lieu of securities, or by a combination of the two. Accordingly, the position in relation to the "Affected Asset" pool is intended to do no more than reflect the position under SIPA.

- 24** In paragraph 80 of LIBA's skeleton argument, there is a suggestion that the Scheme grants LBIE an element of discretion in respect of the identification of what comprises a "stock-line" for the purposes of allocation and distribution. This is not correct. It is intended that the identification of a stock-line should be by reference to ISIN or CUSIP numbers and thus no element of discretion should arise in this regard.

CONCLUSION

25 In all the circumstances, 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: 

DAVID PHILIP EREIRA

26th October 2009

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2006

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