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

(1) ANTHONY VICTOR LOMAS

(2) STEVEN ANTHONY PEARSON

(3) PAUL DAVID COPLEY

(4) RUSSELL DOWNS

(5) JULIAN GUY PARR

(as the joint administrators of the above named company)

Applicants

- AND -

(1) BURLINGTON LOAN MANAGEMENT LIMITED

(2) CVI GVF (LUX) MASTER S.À R.L

(3) HUTCHINSON INVESTORS LLC

(4) WENTWORTH SONS SUB-DEBT S.À R.L

(5) YORK GLOBAL FINANCE BDH, LLC

(6) GOLDMAN SACHS INTERNATIONAL

Respondents

EXPERT OPINION OF ROBERT S. SMITH AS TO MATTERS OF NEW YORK LAW

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1. I, Robert S. Smith, am a member of the bar of the State of New York and a former Associate Judge of the New York Court of Appeals.

2. I have been instructed by Kirkland & Ellis International LLP on behalf of Wentworth Sons Sub-Debt S.A.R.L. to prepare an opinion addressed to the High Court of Justice (the "High Court") on certain questions of New York law relevant to proceedings in the High Court commenced by the administrators of Lehman Brothers International (Europe). My instructions (the "Instructions") are at Appendix A to this report.

3. I have reviewed and relied upon the documents listed in Paragraph 2 of the Instructions, as well as the 1992 and 2002 forms of the ISDA Master Agreement.

4. The only matters in this report that are within my personal knowledge are those relating to my qualifications and to the contents of documents I have reviewed.

I. <u>My Qualifications</u>

5. I graduated from Stanford University ("with great distinction") in 1965 and from Columbia Law School (*magna cum laude*) in 1968. At law school, I was first in my class academically, was editor-in-chief of the Columbia Law Review and received a number of prizes for academic achievement.

6. Following my graduation from law school, I was for 34 years a litigation lawyer, an associate until 1976 and thereafter a partner, at the firm of Paul, Weiss, Rifkind, Wharton & Garrison LLP in New York. My practice focused primarily on commercial litigation, and included a number of complex financial cases. In 2003, I left Paul Weiss and worked briefly as an individual practitioner and as Special Counsel to the firm of Kornstein Veisz Wexler & Pollard, LLP before being appointed to the bench.

7. Until I became a judge, I was an active courtroom litigator. By my count, I tried 50 cases in federal and state courts, several of which were lengthy and complex. I also had an active appellate practice. I argued 51 appeals, including two in the United States Supreme Court and six in the New York Court of Appeals.[1] I also argued in all four departments of the New York Appellate Division, in seven federal Courts of Appeals, and in the appellate courts of four states other than New York.

8. In 1980-81, I took a leave from Paul Weiss to serve as a full-time Visiting Professor from Practice at Columbia Law School, where I taught courses in contracts and civil procedure. After returning to Paul Weiss, I continued to teach a procedure course at Columbia on a part-time basis until 1990.

9. I was appointed in November 2003 and confirmed in January 2004 as an Associate Judge of the New York Court of Appeals, where I served until reaching the mandatory retirement age in 2014. While on the Court of Appeals, I was the author of, by my estimate, more than 200 opinions for the court, as well as numerous dissenting and concurring opinions. Among my opinions were many involving the interpretation of contractual provisions, including *RJC Realty Holding Corp. v. Republic Franklin Insurance Co.*, 2 N.Y.3d 158 (2004), *Cox v. NAP Construction Co.*, 10 N.Y.3d 592 (2008), and *United States Fidelity & Guaranty Co. v. American Re-Insurance Co.*, 20 N.Y.3d 407 (2013) (discussed in paragraph 35 below). I also wrote opinions in cases involving disputed claims for interest, including *Bello v. Roswell Park Cancer Institute*, 5 N.Y.3d 170 (2005) and *Manufacturer's & Traders Trust Co. v. Reliance Insurance Co.*, 8 N.Y.3d 583 (2007).

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[1] The nomenclature of the New York courts is unusual. "Supreme Court," as commonly used, refers to a trial-level court. The "Appellate Division" (properly speaking, the Appellate Division of the Supreme Court) is an intermediate appellate court. The Court of Appeals is the highest appellate court – the counterpart of the court called "Supreme Court" in most other states.

10. While serving as a judge, I also taught a course in state constitutional law at the Benjamin N. Cardozo School of Law from 2006 to 2009. From 2010 to the present, I have been the co-teacher of a course entitled "Authority and Liberty" at Cardozo Law School.

11. Since January 1, 2015, I have been a partner in the New York City law firm of Friedman Kaplan Seiler & Adelman LLP.

II. Questions Addressed and Summary of Opinions

12. My instructions relate to the 1992 and 2002 forms of Master Agreement of the International Swaps and Derivatives Association, Inc. (ISDA). I have been asked what principles of New York law are relevant to the construction of:

(a) two terms in the Master Agreement's definition of "Default Rate." That definition reads in full: "a rate per annum equal to the cost (without proof or evidence of any actual cost) to the relevant payee (as certified by it) if it were to fund or of funding the relevant amount plus 1% per annum." I have been asked about the terms "relevant payee" and "cost without proof or evidence of accrual cost to the relevant payee (as certified by it) if it were to fund or of funding the relevant amount."

(b) Section 6(d)(ii) ("Payment Date") of the 1992 ISDA Master Agreement; and

(c) Section 7(b) of the 1992 ISDA Master Agreement, which says: "A party may make a transfer [without the prior written consent of the other party] of all or any part of its interest in any amount payable

to it from a Defaulting Party under Section 6(e)." (Section 6(e) governs "Payments on Early Termination".)

13. As to the definition of "Default Rate," I have also been asked what principles of New York law are relevant when considering the following more specific questions:

(a) Whether a relevant payee's certification of its cost of funding for the purpose of applying the "Default Rate" is conclusive;

(b) If not, under what circumstances and on what bases can the Defaulting Party challenge the relevant payee's certification of its cost of funding;

(c) How the cost of funding should be established in the event that the certifying party's certification is successfully challenged; and

(d) In the event the relevant payee is not capable of providing or does not provide certification, who is entitled to provide certification of the cost of funding?

14. My opinions on these questions may be summarized as follows:

(a) Some general principles of New York law are relevant to the interpretation of all of the contractual provisions mentioned in my instructions. These include the rules that the words of a written contract, read according to their ordinary meaning, are considered the best evidence of the parties' intent; that evidence outside the contract is generally not admissible to supplement or change the written words, but that extrinsic evidence may be considered to resolve ambiguity; that all clauses in an agreement should be

considered in its interpretation; that courts will avoid an interpretation that produces an absurd or unreasonable result; and that an interpretation that places one party at the mercy of another or permits one party to take unfair advantage of the other is not favored.

(b) New York law principles governing assignment are also relevant to the interpretation that should be given to the term "relevant payee" in the definition of "Default Rate". Among them are that claims are generally freely assignable, and an assignment carries with it the right to collect interest that would otherwise be due to the assignor; and that an assignee stands in the shoes of its assignor and can acquire no greater rights than the assignor had at the time of the assignment.

(c) As to the effect that a New York court would give to the relevant payee's certification of its cost of funding, the principle disfavoring interpretations that put one party at the mercy of the other or permit one to take unfair advantage of the other is especially significant. Also very significant is the rule that each contract contains an implied covenant of good faith and fair dealing; in cases where one party is permitted by contract to make a discretionary determination, the implied covenant has been held to require that the determination not only be made in subjective good faith, but also meet an objective standard. Several cases hold

that the exercise of discretion may not be irrational or arbitrary, and have found that whether a particular decision met that standard must be decided as an issue of fact.

III. General Principles of Contract Interpretation

15. Among the most basic principles of New York contract law is the rule that a court will interpret a contract as written, since its words are considered the best evidence of the parties' intent. *See Slamow v. Del Col*, 79 N.Y.2d 1016, 1018, 594 N.E.2d 918, 919 (1992). Evidence outside a contract itself ("extrinsic evidence") generally is not admissible to supplement or change the written words of the contract. *See W.W.W. Assocs., Inc. v. Giancontieri*, 77 N.Y.2d 157, 162, 566 N.E.2d 639, 642 (1990). However, a court will consider extrinsic evidence – e.g., evidence of what the parties said during negotiations, their conduct in performing under the agreement or industry or market custom and usage – to the extent that the words of the contract are found to be "ambiguous." *See, e.g., S. Rd. Assocs., LLC v. Int'l Bus. Machines Corp.*, 4 N.Y.3d 272, 278, 826 N.E.2d 806, 810 (2005) ("Since the meaning of 'premises' is clear and unambiguous in the lease, extrinsic evidence such as the conduct of the parties may not be considered.").

16. A contract is unambiguous where "the words [...] have a definite and precise meaning, unattended by danger of misconception in the purport of the [contract] itself, and concerning which there is no reasonable basis for a difference of opinion." *Breed v. Ins. Co. of N. Am.*, 46 N.Y.2d 351, 355, 385 N.E.2d 1280, 1282 (1978). Evidence outside a contract itself cannot be used to create an ambiguity that is not otherwise present. *W.W.W. Associates,* 77 N.Y.2d at 163, 566 N.E.2d at 642.

17. I have observed a distinct tendency in New York decisions to hold contractual language to be unambiguous, even where that characterization may be debatable. *See, e.g., S. Rd. Associates,* 4 N.Y.3d at 278, 826 N.E.2d at 810 ("premises" held, in context, unambiguously to refer only to interior of building, not land); *Vt. Teddy Bear Co., v. 538 Madison Realty Co.,* 1 N.Y.3d 470, 475-76, 807 N.E.2d 876, 879-80 (2004) (contract held unambiguous although an intermediate appellate court had divided 3-2 over its meaning). Decisions holding contracts to be ambiguous are surprisingly few, although they do exist. *See, e.g., Graev v. Graev,* 11 N.Y.3d 262, 272, 898 N.E.2d 909, 914 (2008); *Red-Kap Sales, Inc. v. Northern Lights Energy Products, Inc.*, 94 A.D.3d 1281, 1282-83, 942 N.Y.S.2d 283, 284-85 (3d Dep't 2012); *Lipari v. Maines Paper & Food Serv., Inc.*, 245 A.D.2d 1085, 1085-86, 667 N.Y.S.2d 548, 548-49 (4th Dep't 1997).

18. The fact that the parties to a contract advance differing interpretations does not, standing alone, make it ambiguous. *See Greenfield v. Philles Records, Inc.*, 98 N.Y.2d 562, 572-73, 780 N.E.2d 166, 172 (2002); *Bethlehem Steel Co. v. Turner Constr. Co.*, 2 N.Y.2d 456, 460, 141 N.E.2d 590, 593 (1957) ("Mere assertion by one that contract language means something to him, where it is otherwise clear, unequivocal and understandable when read in connection with the whole contract, is not in and of itself enough to raise a triable issue of fact.").

19. No New York state or federal court has held in any reported decision that any of the standard provisions of the 1992 ISDA Master Agreement or its successor, the 2002 ISDA Master Agreement, is ambiguous. *See Banco Espirito Santo, S.A. v. Concessionaria Do Rodoanel Oeste S.A.*, 100 A.D.3d 100, 109, 951 N.Y.S.2d 19, 26 (1st Dep't 2012) (hyphenation of term when used in Master Agreement but not in Schedule did not make term ambiguous); *U.S.*

Bank Nat'l Ass'n v. Ables & Hall Builders, 696 F. Supp. 2d 428, 440 (S.D.N.Y. 2010) (use of term "termination" in Master Agreement not ambiguous).

20. As the language quoted in paragraph 18 above from the *Bethlehem* decision makes clear, whether a contract is ambiguous is to be determined from a reading of the contract as a whole. Thus provisions of the contract other than the one immediately in dispute are not considered "extrinsic" evidence.

IV. The Interpretation of "Relevant Payee"

A. Applicable Principles of Contract Interpretation.

21. While the words "relevant payee", read in isolation, do not have a single, obvious meaning, a New York court would examine them in context, and could hold the term to be "unambiguous" if it found a clear answer to the particular interpretative issue presented. The immediate context of "relevant payee" in the Master Agreement is the definition of "Default Rate", which says that the cost of funds of the "relevant payee" determines the interest rate to be paid to a Non-defaulting Party. The issue is essentially whether the "relevant payee" is the Defaulting Party's original counterparty or a person who has acquired the counterparty's claim by assignment.

22. In deciding this issue, a New York court would consider the principle that an interpretation that renders the parties' agreement unreasonable or absurd is to be avoided. *See Lipper Holdings, LLC v. Trident Holdings, LLC,* 1 A.D.3d 170, 171, 766 N.Y.S.2d 561, 562 (1st Dep't 2003). In considering what was reasonable, a court would look at the commercial consequences of the interpretations proffered by the parties. *Elsky v. Hearst Corp.,* 232 A.D. 2d 310, 310-11, 648 N.Y.S.2d 592, 593 (1st Dep't 1996). In this case, a court would consider

whether an interpretation that effectively allowed one party, by assigning its rights, to alter the interest rate the other party must pay is unreasonable or absurd.

23. In my opinion, a New York court would also apply the rule that an interpretation placing one party at the mercy of another, or permitting one to take unfair advantage of the other, should be disfavored. As the Court of Appeals said in *Metro. Life Ins. Co. v. Noble Lowndes Int'l, Inc.*:

> A court will endeavor to give the [contract] construction most equitable to both parties instead of the construction which will give one of them an unfair and unreasonable advantage over the other. It is highly unlikely that two sophisticated business entities, each represented by counsel, would have agreed to such a harshly uneven allocation of economic power under the Agreement. Language in contracts placing one party at the mercy of the other is not favored by the courts.

See 84 N.Y.2d 430, 437-38, 643 N.E.2d 504, 508 (1994) (internal quotations omitted).

24. If a court found the term "relevant payee" to be ambiguous, it would examine any extrinsic evidence relevant to the term's meaning. In this situation, a court would be permitted to consider, as an aid to construction, a predecessor version of the ISDA Master Agreement in which assignments of claims by Non-defaulting Parties were not permitted. That predecessor agreement used the term "relevant payee" in its definition of "Default Rate", as the 1992 Master Agreement does, thus suggesting that the term was not originally used to refer to an assignee.

B. Applicable Principles of the Law of Assignment

25. New York law generally permits the assignment of a claim for an amount due under a contract. *See, e.g., Melino v. Nat'l Grange Mut. Ins. Co.*, 213 A.D.2d 86, 88, 630 N.Y.S.2d 123, 125 (3d Dep't 1995) ("Here, plaintiff did nothing more than assign, during the course of what is presumed to have been an arms' length transaction, her rights under defendant's insurance policy to the Bank and, as the Bank correctly notes, both settlement proceeds and the right to recover moneys due under a contract may be assigned."). An

assignment of a claim conveys with it any right to collect interest. *See O'Brien v. Argo Partners, Inc.*, 736 F. Supp. 2d 528, 535-36 (E.D.N.Y. 2010).

26. When an assignment has occurred, an assignee is said to "stand in the shoes" of the assignor, such that the assignee acquires no greater rights than the assignor had at the time of the assignment. *See N.Y. & Presbyterian Hosp. v. Country-Wide Ins. Co.*, 17 N.Y.3d 586, 593, 958 N.E.2d 88, 93 (2011) (assignee of insurance benefits could not bring claim to collect because deadline for notice of claim had expired before assignment); *Condren, Walker & Co. v. Portnoy*, 48 A.D.3d 331, 331-32, 856 N.Y.S.2d 42, 42 (1st Dep't 2008) (assignee of notes required to pay brokerage fee that was due on notes but unpaid by assignor prior to assignment); *Carla Realty Co. v. Cty. of Rockland*, 222 A.D.2d 480, 480, 635 N.Y.S.2d 67, 68 (2d Dep't 1995) (deed to assigned property reformed to reflect easement to which assignor had been subject prior to assignment); *Countrywide Home Loans, Inc. v. LaFonte*, Index No. 14265/01, 2003 N.Y. Slip Op. 50571(U), 2003 WL 1389089, at *3 (Sup. Ct. (Nassau Cty.) Feb. 13, 2003) (assignee of mortgage lender who had misappropriated loan proceeds could not recover under title insurance policy, because lender could not); *Robischon v. Genesee Valley Med. Care, Inc.*, 401 N.Y.S.2d 379, 381, 92 Misc. 2d 854, 856-57 (Sup. Ct. (Monroe Cty.) 1977) (assignee subject to statute of limitations defense that would have barred claim by assignor).

27. A Court of Appeals case that is often cited on this point says:

> It is elementary ancient law that an assignee never stands in any better position than his assignor. He is subject to all the equities and burdens which attach to the property assigned because he receives no more and can do no more than his assignor.

Int'l Ribbon Mills, Ltd. v. Arjan Ribbons, Inc., 36 N.Y.2d 121, 126, 325 N.E.2d 137, 139 (1975) (judgment creditor who served restraining notices creating liens against assignor's property prior to assignment had superior right to such property to that of assignee) (citations omitted).

28. In my opinion, a New York court would be likely to find that these authorities weigh against a construction of "relevant payee" that would enable an assignee to obtain a higher interest rate than could have been obtained by its assignor.

V. The Effect to be Given to a Relevant Payee's Certification of its Cost of Funds

29. My instructions ask me to consider what principles a New York court would find applicable in interpreting the words "cost (without proof or evidence of actual cost) to the relevant payee (as certified by it) if it were to fund or of funding the relevant amount". The instructions also refer to several more specific questions relating to how a New York court would deal with a challenge by a Defaulting Party to a proffered certification.

30. On this issue, a New York court might well reject as untenable certain extreme constructions. A court would be unlikely to hold that literally any certification by a relevant payee as to its cost of funding – even a knowingly and demonstrably false one – must be given binding effect. Nor would a court be likely to hold that a certification could be reviewed de novo by the court, for that would effectively give the certification no weight. So far as I know, neither of these extreme interpretations has been advanced by any party to these proceedings.

31. Thus, a central question is what standard a court would use in evaluating a challenge to a certification – a purely subjective "good faith" standard, a purely objective "reasonableness" standard, some variation on one of these or a combination of both. On this question, in my opinion, the rule discussed in paragraph 23 above that an interpretation allowing one party to take unfair advantage of another should be avoided is especially significant.

32. Also relevant is the approach New York courts have taken in cases where, as here, a contract gives a party discretion to make a decision that may be detrimental to the other party. Under New York law, such discretionary decisions are subject to the implied covenant of good

faith and fair dealing deemed to be part of every contract. *511 W. 232nd Owners Corp. v. Jennifer Realty Co.,* 98 N.Y. 2d 144, 152-53, 773 N.E.2d 496, 499-500 (2002). Where a contract contemplates the exercise of discretion, the implied covenant "includes a promise not to act arbitrarily or irrationally in exercising that discretion." *Dalton v. Educ. Testing Serv.*, 87 N.Y.2d 384, 389, 663 N.E.2d 289, 291 (1995) (upholding factual finding that a testing service failed to comply with the covenant of good faith in refusing without adequate consideration to release a student's test score, despite a contract committing that decision to the testing service's discretion).

33. The test of good faith and fair dealing, as applied to discretionary decisions, is not a purely subjective one. The dissenting opinion in *Dalton*, which agreed with the majority as to the applicable rule, stated this clearly: it said the test is whether a party "performed its discretionary functions arbitrarily or irrationally, *or* with bad faith in fact" (emphasis added). 87 N.Y.2d at 397 (dissenting opinion of Levine, J.).

34. *Dalton* and a number of other cases have held that, where no justification for a party's exercise of discretion was apparent, whether the party acted irrationally or arbitrarily presented an issue of fact. *See, e.g., Sorenson v. Bridge Capital Corp.*, 52 A.D.3d 265, 266-67, 861 N.Y.S.2d 280, 282-83 (1st Dep't 2008) (denying summary judgment where a party exercised its discretion not to purchase certain apartments); *Security Plans, Inc. v. CUNA Mut. Ins. Soc.*, 769 F.3d 807, 817-821 (2d Cir. 2014) (denying summary judgment where a company exercised its discretion in making a calculation governing a prior owner's earn-out rights).

35. Another situation in which New York law limits a contracting party's discretion to act to the detriment of another party was presented to the New York Court of Appeals in *United States Fidelity & Guaranty Co. v. American Re-Insurance Co.,* 20 N.Y.3d 407, 985

N.E.2d 876 (2013). That case involved a claim under reinsurance contracts. The reinsurer alleged that the reinsured had allocated the payments it made on certain claims so as to maximize the amount covered by reinsurance. The Court's opinion (of which I was the author) held that the reinsured had discretion in allocating its settlement payments, but that the allocation must nevertheless be "reasonable" in the sense that it "must be one that the parties to the settlement of the underlying insurance claims might reasonably have arrived at in arm's length negotiations if the reinsurance did not exist." 20 N.Y. 3d at 419-420.

36. In sum, New York courts will not always defer to a party's exercise of discretion, even where the discretion is implicitly or explicitly conferred by the agreement and even where the party may have acted in subjective good faith. The standard employed, or the words used in articulating it, may vary depending on the factual context. It is not clear that this is purely a matter of contract interpretation: some limitation on a contracting party's discretion may be required by public policy, whatever the contract says. In the *Security Plans* case cited above (¶ 34), the court mentioned, but did not decide, the question of whether a contractual provision "may constrict or obviate the protections of the implied covenant." 769 F.2d at 819 n.11.

37. In *Finance One Public Co. Ltd. v. Lehman Brothers Special Financing, Inc.*, No. 00 Civ. 6739 (CBM), 2003 WL 21638214 (S.D.N.Y. July 11, 2003), the United States District Court for the Southern District of New York, a trial-level federal court, interpreted the 1992 form of the ISDA Master Agreement. In that case, Finance One contended that it was entitled to recover the Default Rate of interest and certified its cost of funding. The defendant, a Lehman Brothers affiliate, argued, among other things, that the rates certified by Finance One were "exaggerated," but the court declined to consider evidence on that issue. The court said:

> This argument... ignores the fact that the ISDA explicitly precludes an issue of fact contest with regard to the proper default rate with the phrases

> "without proof or evidence of any actual cost" and "as certified by it." ISDA, § 14(d), at 14. Under New York law, the only possible route to avoid enforcement of this clause in the contract would be to suggest bad faith, fraud, gross negligence or contravention of public policy, which LBSF does not do.

On appeal, a federal Court of Appeals reversed on other grounds the judgment ultimately entered by the District Court in *Finance One. See Fin. One Public Co. v. Lehman Bros. Special Fin.,* 414 F.3d 325, 345 (2d Cir. 2005). The appellate court did not need to consider the issue of the Default Rate in light of its ruling.

38. In the United States federal system, federal courts may interpret state law, but their decisions are not binding on state courts. *See, e.g., People v. Perez,* 61 A.D.2d 817, 817, 402 N.Y.S.2d 51, 52 (2d Dep't 1978) (rejecting argument based on federal District Court decision where New York Court of Appeals had rejected the same argument). Thus, no New York court would be bound to follow the District Court's *Finance One* holding. The decision would receive respectful attention, but in my opinion the test it states would not be adopted.

39. The *Finance One* opinion makes no mention of the covenant of good faith and fair dealing or of the rule, stated by the New York Court of Appeals in the *Dalton* case, that that covenant includes an obligation not to act irrationally or arbitrarily. Nor did the *Finance One* court explain why it thought that "bad faith, fraud, gross negligence or contravention of public policy" were the only bases for challenging a Non-defaulting Party's certification. The only authority the court cited for this proposition, *Kalisch-Jarcho, Inc. v. City of New York,* 58 N.Y. 2d 377, 448 N.E.2d 413 (1983), involved a waiver of delay damages in a construction agreement, and is, in my opinion, irrelevant to the issue presented here. The *Finance One* court did not discuss the danger that the certification power would be abused, or consider the principle, discussed above, that an interpretation allowing one party to take unfair advantage of another should be avoided.

40. The *Finance One* decision is, in my opinion, incorrect in saying "that the ISDA explicitly precludes an issue of fact contest with regard to the proper default rate" – at least, it is incorrect if the court meant its comment generally, and not merely as applicable to the facts before it. As the cases I have cited demonstrate, New York law does not preclude an issue of fact where a party has exercised discretion granted under a contract.

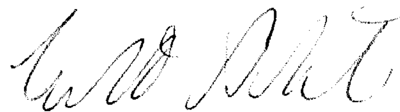
VI. My Duty to the High Court and Statement of Truth

41. I understand that my duty is to help the High Court on matters within my expertise. This duty is paramount and overrides any obligation to the parties from whom I have received instructions and by whom I am being paid. I have complied and will continue to comply with that duty.

42. I am aware of the applicable requirements of Civil Procedure Rules Part 35, Practice Direction 35, the Civil Justice Council Guidance for the instruction of experts in civil claims 2014, and the Practice Direction – Pre-Action Conduct.

43. I confirm that I have made clear which facts and matters referred to in this report are within my own knowledge and which are not. Those that are within my own knowledge I confirm to be true. The opinions I have expressed represent my true and complete professional opinions on the matters to which they refer.

Dated: June 25, 2015



Robert S. Smith

Appendix A

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16 June 2015

Robert S. Smith

Friedman Kaplan Seiler & Adelman LLP
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Dear Robert S. Smith,

Re: Instruction Letter

Thank you for agreeing to act as a party appointed expert in relation to the application of the Joint Administrators of Lehman Brothers International (Europe) (In Administration) ("**LBIE**") to the High Court of Justice (the "Court"), London, dated June 25, 2014 (No. 7942 of 2008) (the "**Waterfall II Application**").

This may involve, as directed by the court, producing an expert report and reply report to assist the court in its consideration of the matter, participating in discussions with the other parties' expert/s and producing a related statement, producing a supplemental report, giving oral evidence at the trial, and carrying out any other duties appropriate to the role of an expert, as directed by the court or instructed by us.

In this respect, please see the enclosed order of Mr Justice David Richards in relation to the 9 March 2015 case management conference (the "**Experts Order**") dated 7 May 2015, which sets out, among other things:

(a) The relevant steps and timings regarding your expert evidence (the "**Experts Steps**").

(b) The questions you are expected to address as an expert in New York law (the "**Experts Questions**").

KIRKLAND & ELLIS INTERNATIONAL LLP

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ASSOCIATED OFFICES

Beijing Chicago Hong Kong Houston Los Angeles Munich New York Palo Alto San Francisco Shanghai Washington, D.C.

For convenience, we also attach a timetable reflecting the Experts Steps (the "**Timetable**").

With regard to oral evidence at trial, please note that, from 1 April 2013, the court has the power at any stage in the proceedings to order experts to give their evidence concurrently at trial. Do let us know if it would be helpful to discuss this further.

We set out below, among other things, the background facts of the case, certain enclosures, as well as indicating the questions for you to address.

1 Background Facts

1.1 LBIE was the principal trading company within the European Lehman Brothers group of companies and is an English unlimited company. LBIE entered into administration on 15 September 2008 (the "**Administration Date**"). The current Joint Administrators are Anthony Victor Lomas, Steven Anthony Pearson, Paul David Copley, Russell Downs and Julian Guy Parr (the "**Joint Administrators**").

1.2 The Joint Administrators have for some time anticipated the possibility of there being sufficient assets in the LBIE estate for them to be able to pay 100 pence in the pound in respect of claims admitted for dividend and of there being a surplus of assets remaining after they have done so (the "**Surplus**").

1.3 The Joint Administrators made the Waterfall II Application to determine certain questions which affect distribution of the Surplus.

1.4 Broadly, the questions concern how statutory interest is to be calculated (it is in this context that the questions you are being asked to consider arise), how currency conversion claims are to be quantified, and the impact on claims to statutory interest and/or currency conversion claims and/or possibly other non-provable claims of certain contracts entered into, post-administration, between LBIE and certain of its creditors.

1.5 Specifically, the Expert Questions will help inform the court in relation to the following question in the application: 19.

1.6 There are the following respondents to the Waterfall II Application: (1) Burlington Loan Management Limited; (2) CVI GVF (Lux) Master S.à.r.l; (3) Hutchinson Investors, LLC; (4) Wentworth Sons Sub-Debt S.à.r.l; and (5) York Global Finance BDH, LLC.

1.7 By way of further background information only, please see the enclosed Application Notice (as amended) and the accompanying ninth witness statement of Anthony Victor Lomas.

2 Enclosures

We enclose the following documents:

(1) Notes for experts (the "**Guidance Notes**").

(2) Part 35 of the Civil Procedure Rules, (b) the Practice Direction to Part 35, (c) the Guidance for the instruction of experts in civil claims 2014 (the "**Guidance**"), and (d) the Practice Direction on Pre-Action Conduct including Annex C (together the "**CPR Enclosures**").

(3) The Experts Order.

(4) The Timetable.

(5) (a) The Application Notice, and (b) accompanying ninth witness statement of Anthony Victor Lomas.

3 Questions

3.1 You will need to address the specific New York law Experts Questions which are set out in the Experts Order at Schedule B.

3.2 If, having read this letter and its enclosures, you feel that you may not, after all, have the appropriate experience or expertise to deal with these matters, please let us know immediately.

4 Duties of an Expert

4.1 You have a duty to exercise reasonable skill and care in carrying out your instructions and should comply with any relevant professional code of practice, but your overriding duty as an expert is to the court. Your primary function is to assist the court and, in this capacity, you must provide your unbiased opinion as an independent witness in relation to those matters which are within your expertise.

4.2 An expert's duties are set out more fully in the CPR Enclosures, and you should ensure that you understand and comply with these duties.

4.3 As you may be aware, in March 2011 the Supreme Court abolished the immunity from suit for breach of duty (whether in contract or negligence) that expert witnesses previously enjoyed in relation to their participation in legal proceedings (*Jones v Kaney [2011] UKSC 13*).

5 Your Report

5.1 To be used in evidence before the court, your report must comply with the requirements of the Civil Procedure Rules (which govern the conduct of civil proceedings in England and Wales) and the Guidance. You will find a checklist of the points which should be covered in your report in the Guidance Notes for experts.

5.2 Please let us know immediately if, at any time after producing your report, you change your views. It is also important to let us know promptly if you need to update your report, for example because new legal developments have occurred, so we can consider whether an amended version of your report or a supplementary report should be produced.

6 Timetable

6.1 We are aiming for you to provide your expert evidence in accordance with the timings set out in the Experts Order (and replicated in the Timetable for convenience).

6.2 In view of the timings, we would be grateful if you could liaise with us to ensure that the signed final-form copy of your first report in English (as drafted or by certified translator) is ready in good time in advance of the 26 June 2015, returning it via email to: kasimacopoulos@kirkland.com; pkar@kirkland.com; jifree.cader@kirkland.com; and gordon.davidson@kirkland.com, with the original documents to follow at your earliest convenience. Similarly please liaise with us to ensure that the other timings for discussions, post-discussions statement and any reply report are met.

6.3 Once you have read this letter please let us know so that we can call you to discuss the relevant issues and timings.

6.4 It is possible that you would be required to attend the hearing in November 2015, which is currently scheduled for 9-20 November 2015. Please let us know urgently if this is not possible.

7 Right to ask for Directions from the Court

7.1 Experts are entitled to ask the court for directions to assist them in carrying out their functions if they feel that this is necessary. Please do let us know if you intend to make an application for directions. We may be able to help with the matter, either by resolving any difficulties you may be experiencing and thereby avoiding the need to seek directions, or by helping you to formulate the request.

7.2 If you wish to seek directions in any event, we should mention that, unless the court has directed otherwise, you are required under the Civil Procedure Rules to:

(a) Let us have a copy of your proposed request for directions at least seven days before filing it at court; and

(b) Provide all other parties with a copy of your request at least four days before the request is filed.

8 Questions on Expert's Report

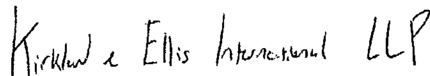
8.1 Please let us know immediately if you receive any questions from any persons relating to this matter, so we can discuss the appropriate action as they may be procedural rules and duties to adhere to. In particular, once a report has been served it is possible that the other parties may ask written questions for the purpose of clarifying your report.

9 Fees

9.1 Your fee arrangements are contained in a separate retention letter. However, please note that payments contingent upon the nature of the expert evidence given in legal proceedings, or upon the outcome of a case, should not be offered or accepted. To do so may contravene experts' overriding duty to the court and compromise their duty of independence (see further para 88 of the Guidance).

We look forward to discussing the relevant issues with you further once you have reviewed this letter and the enclosed documents. In the meantime, if you have any questions in relation to your role as an expert in this matter, please do not hesitate to let us know.

Yours sincerely,



Kirkland & Ellis International LLP

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

ANTHONY VICTOR LOMAS & OTHERS

- AND -

BURLINGTON LOAN MANAGEMENT LIMITED & OTHERS

EXPERT OPINION OF ROBERT S. SMITH AS TO MATTERS OF NEW YORK LAW