

Proposed Respondent
JPK Kelly
Second
22 June 2015

Waterfall II Application

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

B E T W E E N :

- (1) ANTHONY VICTOR LOMAS
- (2) STEVEN ANTHONY PEARSON
- (3) PAUL DAVID COPLEY
- (4) RUSSELL DOWNS
- (5) JULIAN GUY PARR

(THE JOINT ADMINISTRATORS OF LEHMAN BROTHERS INTERNATIONAL
(EUROPE) (IN ADMINISTRATION))

Applicants

- and -

- (1) BURLINGTON LOAN MANAGEMENT LIMITED
- (2) CVI GVF (LUX) MASTER S.A.R.L
- (3) HUTCHINSON INVESTORS, LLC
- (4) WENTWORTH SONS SUB-DEBT S.A.R.L
- (5) YORK GLOBAL FINANCE BDH, LLC

Respondents

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GOLDMAN SACHS INTERNATIONAL

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SECOND WITNESS STATEMENT OF
JONATHAN PATRICK KNOX KELLY

I, **Jonathan Patrick Knox Kelly**, a partner in the firm of Cleary Gottlieb Steen & Hamilton LLP, 55 Basinghall Street, London, EC2V 5EH say as follows:

INTRODUCTION

1. I am a solicitor of the Senior Courts of England and Wales and a Partner in the firm of Cleary Gottlieb Steen & Hamilton LLP, solicitors for Goldman Sachs International (“**Goldman Sachs**”) as holder of a claim against Lehman Brothers International Europe (In Administration) (“**LBIE**”). I have conduct of this matter and I am duly authorised to make this witness statement on behalf of Goldman Sachs.
2. The facts and matters set out in this witness statement are within my knowledge from my handling of this matter or are based on information and documents provided to me by Goldman Sachs, and I believe them to be true.
3. For the avoidance of doubt, nothing I say in this witness statement is intended to be, nor should be taken to be, a waiver of any legal professional privilege vesting in Goldman Sachs.
4. I make this witness statement in response to the First Witness Statement of Johannes Weber dated 18 June 2015 and served on 19 June 2015 (“**Weber 1**”). I also refer to my First Witness Statement dated 8 May 2015 (“**Kelly 1**”), which I made in support of Goldman Sachs’ application that it be added as an additional Respondent (the “**Joinder Application**”) to the application for directions issued by the Joint Administrators of LBIE on 12 June 2014 (the “**Waterfall II Application**”).
5. Regrettably, Mr Weber’s Witness Statement was not provided to my firm until the early hours of Friday, 19 June 2015 and was not filed with the court until later that day, after Goldman Sachs’ skeleton argument for its Joinder Application was served on the parties and two business days before the hearing of the Joinder Application. This was despite the fact that, as described in my First Witness Statement, Goldman Sachs and my firm have been engaged in correspondence with the existing parties’ solicitors for over three months since 16 March 2015 [Kelly 1/27] and Goldman Sachs’ Joinder Application was issued on 8 May 2015.

6. This response is, therefore, brief and Goldman Sachs reserves the right to respond further in relation to the matters raised by Mr Weber if Goldman Sachs is permitted to join the Waterfall II Application and those matters are said to be relevant to the issues before the court.

RESPONSE TO MR WEBER'S EVIDENCE

7. As an initial point, I would note that the matters in question in this part of the Waterfall II Application are broader than Goldman Sachs' particular claims against LBIE. They are concerned with the proper interpretation of the meaning of "Default Rate", and are likely to determine that issue definitively. As I explained in my First Witness Statement, the court's decision on the cost of funding issues will impact countless other ISDA Master Agreements, of which financial institutions like Goldman Sachs are among the principal counterparties [Kelly 1/12C]. Consequently, Goldman Sachs has a broader interest in these matters.
8. Nevertheless, Goldman Sachs does have a direct interest in the outcome of the Waterfall II Application.
9. Mr Weber states that the "*cost of funding of the Goldman Sachs Group is and was likely to result in a Default Rate, as defined under the ISDA Master Agreement, at a rate substantially lower than 8% per annum*" [Weber 1/8]. This evidence forms the basis for a submission by Wentworth that Goldman Sachs will not be able to certify a Default Rate in excess of the rate of 8% set by the Judgments Act 1838 and so should not be allowed to join the Waterfall II Application.
10. Goldman Sachs rejects this suggestion. I have been advised by Goldman Sachs, and believe, that Goldman Sachs expects to certify a Default Rate in relation to its ISDA claim against LBIE that would result in a claim to Statutory Interest in excess of 8% per annum (which equates to approximately 6.5% compound) reflecting its actual cost of funding, including equity costs.
11. In any event, insofar as the court is now asked by Wentworth to rely on Mr Weber's evidence to assess Goldman Sachs' likely Default Rate, it is in reality being asked by Wentworth to perform an early adjudication of Goldman Sachs' claim to Statutory Interest, solely on the basis of Mr Weber's observations from afar, and in the absence

of the requisite certification from Goldman Sachs (which is still to be given). This is obviously premature.

12. As to the three specific matters addressed by Mr Weber, Goldman Sachs' position is that (a) they do not in fact demonstrate that the Default Rate to be certified by Goldman Sachs would result in a claim to Statutory Interest of less than 8% simple (c.6.5% compound); and (b) in any event, they are not relevant to the point of construction at issue in the Waterfall II Application, being the only issue now before the court as regards Default Rate.
13. The latter point will be developed in submissions if required, but should be uncontroversial. The correct interpretation of the term "Default Rate" would not be affected by the particular circumstances of Goldman Sachs, or indeed by matters which post-date the formulation of the contract (which Wentworth accepts in paragraph 11(1)(c) of its skeleton).
14. As to the first point, none of the factual evidence advanced by Mr Weber demonstrates that Goldman Sachs' Default Rate would (on Goldman Sachs' construction of the term) be less than 8% simple (c.6.5% compound). Mr Weber cites three heads of factual evidence, and I deal with each in turn below:

Proofs of claim

15. First, the proofs of claim referred to by Mr Weber at paras. 11 to 18 were filed in 2008 and 2009 in relation to claims Goldman Sachs held in the bankruptcies of Lehman Brothers Holdings Inc. ("**LBHI**") and Lehman Brothers Special Financing Inc. ("**LBSF**"). Although it has not been possible to verify the position definitively in the time since Mr Weber's Witness Statement was provided, I am informed and believe that the back office administrative staff responsible for these forms at the time of their completion did not analyse or include all the actual costs of funding, including equity funding, in these forms because they did not expect there to be any real possibility of recovering interest.
16. In any event, the proofs of claim were subject to express reservations of rights, both generally: "*GSI reserves the right to withdraw, amend, clarify, modify or supplement this Claim [...] GSI also reserves all rights accruing to it or its affiliates against*

[LBHI/LBSF] or its estate, and the submission of this Claim is not intended to be and shall not be construed as [...] (b) a waiver or limitation of any rights of GSI or its affiliates” [JW1/22; JW1/33] and specifically in relation to interest, costs and expenses [JW1/21; JW1/32-33].

17. For completeness, I also note that it does not appear to be in dispute that parties are entitled to revisit their entitlements to interest at the Default Rate, once it can be fully established. On Wentworth’s own case as stated in its Revised Position Paper dated 7 May 2015, the cost of funding “*can only be known, and the per annum rate to be derived from it can thus only be calculated, at the end of the period*” (paragraph 17). The fact that (lower) interest rates may be implied from proofs of claim filed in the insolvency of different parties six years ago is therefore immaterial to the issue of what Default Rate can be certified now in LBIE’s insolvency.
18. These proofs of claim are therefore not relevant to the rate that Goldman Sachs expects to certify under the ISDA Master Agreement.

S&P Capital IQ data

19. Second, the S&P Capital IQ data referred to by Mr Weber [**Weber 1/19 to 23**] does not equate to the cost of funding that Goldman Sachs expects to certify in its claim against LBIE, in particular, as the S&P Capital IQ data shows a “cost of borrowing” and does not on its own terms purport to show costs of “funding,” including cost of equity funding. I therefore do not see how the S&P Capital IQ data relates to either the Joinder Application or the substantive construction issue before the court in relation to the Waterfall II Application.

Public statements

20. Third, Mr Weber also refers to public statements made by The Goldman Sachs Group, Inc. and the Board of Governors of the Federal Reserve System (U.S.) [**Weber 1/24 to 25**]. Those statements do not relate to the funding of Goldman Sachs’ claims against LBIE but to a third party borrowing source that may have been available to The Goldman Sachs Group, Inc. from time to time. These statements do not take into account the market and regulatory requirements applicable at the time that caused Goldman Sachs to raise equity funding, and I do not see what relevance they have to

either the Joinder Application or the substantive issues before the court in relation to the Waterfall II Application.

21. For these reasons, and for the reasons set out in my First Witness Statement, I respectfully submit that the court should make an order joining Goldman Sachs as a respondent to the Waterfall II Application.

STATEMENT OF TRUTH

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

Signed:

A handwritten signature in black ink, appearing to read "Jonathan P. Kelly", written over a horizontal line.

Jonathan Patrick Knox Kelly

Date: 22 June 2015

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SECOND WITNESS STATEMENT OF
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