1. Claimants
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5. 12 June 2018

IN THE HIGH COURT OF JUSTICE **NO. 7492 OF 2008 / CR-2008-000012**

BUSINESS AND PROPERTY COURTS OF ENGLAND AND WALES **CR-2018-003713**

COMPANIES COURT (ChD)

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

-and-

IN THE MATTER OF THE COMPANIES ACT 2006

THIRD WITNESS STATEMENT OF RUSSELL DOWNS

I, Russell Downs, of PricewaterhouseCoopers LLP, 7 More London Riverside, London, SE1 2RT, say as follows:

INTRODUCTION

1 I am the same Russell Downs as has made two witness statements in these proceedings dated 2 May 2018 and 8 May 2018 (my "**First Witness Statement**" and "**Second Witness Statement**" respectively).

2 Save where otherwise expressly defined, capitalised terms have the meaning given to them in the Explanatory Statement.

3 There are now shown to me two paginated bundles of copy documents, marked "**Exhibit RD3**" and "**Exhibit RD4**", to which I refer in this witness statement. References to exhibited materials in this witness statement are in the form [exhibit/page].

A: EXECUTIVE SUMMARY

4 On 11 May 2018 I was appointed to act as Chairman of the Scheme Meetings to be held pursuant to an order made by Mr Justice Hildyard (the "**Convening Order**"). The Scheme and Explanatory Statement approved by the High Court (the "**Court**") at the convening hearing were circulated to Scheme Creditors on 14 May 2018. Amendments were subsequently made to those documents on 31 May 2018 in order to address issues raised by Higher Rate Creditors at the convening hearing and more generally. The most significant of those amendments was the removal of the right of the Subordinated Creditor to determine the level of a Counteroffer made to a Certifying Creditor (in circumstances where the Company and the Subordinated Creditor did not agree on that level), as explained further below.

5 On 5 June 2018, four Scheme Meetings were held in compliance with the Convening Order. The statutory majorities were comfortably met at all four Scheme Meetings, as explained in further detail below and in my report of the Scheme Meetings (the "**Chairman's Report**"). The Administrators are extremely pleased with the level of participation and support across all four Scheme Meetings, with the overwhelming majority of Scheme Creditors voting in favour of the Scheme. I note, in particular, that:

(a) 258 of 265 votes cast at Scheme Meetings 1-3 (i.e. the Scheme Meetings other than the meeting convened for the Subordinated Creditor), were cast in favour of the Scheme (representing 97.4% by number of votes cast);

(b) across Scheme Meetings 1-3, votes with a value of £5,266,102,773 were cast (out of a possible maximum value of £5,439,464,981 if all Scheme Creditors who were entitled to vote had done so); and

(c) turnout by reference to claim value was very high – 96.1% at Scheme Meeting 1, 94.9% at Scheme Meeting 2, and 100% at Scheme Meeting 3.

6 Of particular note is that two of the four Scheme Creditors who had contested the convening of the Scheme Meetings at the convening hearing (CRC Credit Fund Ltd ("**CRC**") and Marble Ridge Special Situations Fund LP ("**Marble Ridge**")) voted in favour of the Scheme and do not oppose its sanction. Both such Scheme Creditors also elected to certify their claims, rather than opt for the Settlement Premium (as further detailed below).

7 In the event only four Scheme Creditors voted against the Scheme, including Deutsche Bank AG ("**Deutsche Bank**") and Goldman Sachs International ("**GSI**"), who supported Deutsche Bank's submissions at the convening hearing. Other than Deutsche Bank, GSI and an entity affiliated with GSI, only one institution voted against the Scheme across the four classes. That institution submitted a request to vote at an amount significantly in excess of the amount the Administrators had originally calculated it should vote at, and even on that basis the statutory majorities were comfortably passed. The same creditor also elected to certify its

claim. Notwithstanding the fact that it voted against the Scheme, Deutsche Bank has recently confirmed that it does not intend to appear at the Sanction Hearing to oppose the Scheme and thus does not oppose the sanctioning of the Scheme. A copy of a letter from Clifford Chance (on behalf of Deutsche Bank) confirming its client's position is exhibited [RD3/22]. By letter dated 8 June 2018, GSI indicated it continues to consider the Scheme to be unfair but does not propose to be represented at the Sanction Hearing or to submit any evidence or submissions. A copy of the letter confirming GSI's position is exhibited [RD3/18-19].

8 As is known to the Court, Deutsche Bank has previously raised concerns about the Wentworth Group voting in the same class as other Scheme Creditors. The Administrators have also analysed what the outcome of Scheme Meetings 1 and 2 would have been had the members of the Wentworth Group not voted at those meetings. Had that been the case for Scheme Meeting 1, 115 votes would have been cast in favour of the Scheme, equating to 97.5% by number and 93.7% by value of the votes cast; and 3 votes would have been cast against the Scheme, equating to 2.5% by number and 6.3% by value of the votes cast (i.e. the statutory thresholds would still have been comfortably met). In relation to Scheme Meeting 2, 62 votes would have been cast in favour of the Scheme, equating to 93.9% by number and 62.2% by value of the votes cast; and 4 votes would have been cast against the Scheme, equating to 6.1% by number and 37.8% by value of the votes cast. This shows the overwhelming support for the Scheme outside of the Wentworth Group.

9 I understand that at the Sanction Hearing the Court will consider, among other things (i) whether the terms of the Convening Order have been complied with, (ii) the outcome of the Scheme Meetings and whether the requirements of section 899 of the Companies Act 2006 are met, and (iii) whether the Scheme is fair such that the Court will exercise its discretion to sanction it. This witness statement has been prepared in order to assist with these matters. I also explain certain amendments that have been made to the Scheme since the date of the Convening Order and certain other steps that have been taken since my First Witness Statement and Second Witness Statement were prepared.

10 The Court will be mindful of the upcoming Court of Appeal hearing in the Waterfall II Tranche C litigation. The Court of Appeal confirmed on 25 May 2018 that it was not minded to adjourn the hearing at the present time. As such it remains scheduled for 3 July 2018 [RD3/15].

11 I and the other Administrators believe that all matters referred to in the Convening Order have been properly addressed and notwithstanding that a few Scheme Creditors continue to have some concerns, the compromise offered up in the Scheme and supported overwhelmingly by the Scheme Creditors as a whole should be approved by the Court. Doing so will facilitate a distribution to Scheme Creditors in the coming weeks in an amount in excess of £5 billion.

B: COMPLIANCE WITH THE CONVENING ORDER

12 Pursuant to the Convening Order, on 14 May 2018, the notice convening the Scheme Meetings (the "**Notice**") [RD3/1-3], together with copies of the Scheme and the Explanatory Statement, were provided to Scheme Creditors by:

12.1 sending such documentation to persons whom the Administrators believe are or may be Scheme Creditors by email or post (to the extent that the Administrators hold such contact details);

12.2 making such documentation available to Scheme Creditors with Admitted Claims via the Portal; and

12.3 publishing copies of such documentation on the Website (see announcement [RD3/4-5]), with Scheme Creditors then directed to the Website by advertisements published in The Times, Financial Times, London Gazette and Wall Street Journal.

13 The Scheme and Explanatory Statement provided with the Notice were substantially in the form of the versions approved by the Court on 11 May 2018 (that is, they incorporated the amendments that were made during the convening hearing to the versions exhibited to my First Witness Statement).

14 In addition, at the same time as being provided with the documents referred to in paragraph 12 above, Scheme Creditors were provided with:

14.1 in the case of Scheme Creditors with Admitted Claims, UCC4s showing their allocated voting rights together with electronic forms of proxy; and

14.2 in the case of Scheme Creditors with Undetermined Provable Claims, Voting Rights Letters (showing the voting rights they had been allocated) together with hard-copy forms of proxy.

15 Pursuant to paragraph 12 of the Convening Order, Scheme Creditors holding more than one Admitted Claim but not controlling all such claims were given until 5.00 pm on 24 May 2018 to request that the Company split their voting rights so that their votes might be cast in accordance with the instructions of those persons controlling the claims. Details of the requests received are set out below at paragraphs 27 to 28*.*

16 Pursuant to paragraph 13 of the Convening Order, Higher Rate Creditors who consider that they are entitled to Statutory Interest at a rate greater than 8% simple were given until 5.00 pm on 31 May 2018 to request voting rights greater than those set out in their UCC4s and/or Voting Rights Letters by notifying the Company of the rate(s) of interest that they consider to apply to their Higher Rate Claims and the amount of interest they consider to be payable to them based on such rate(s). Details of the requests received are set out below at paragraphs 23 to 26.

17 As described in the Chairman's Report, four Scheme Meetings took place in accordance with paragraph 1 of the Convening Order. Subject to the observations in this statement, I confirm that the contents of the Chairman's Report are true and accurate.*

C: AMENDMENTS TO THE SCHEME

18 As I mentioned above, on 31 May 2018, certain amendments were made to the terms of the Scheme to take into account concerns that certain Higher Rate Creditors had raised, including at the convening hearing, as to the certification and adjudication processes. These were:

18.1 revising Part IV (*Scheme Distributions to Certifying Creditors*) so that Clause 12.2 of the Scheme, which sets out the provisions relating to the Company's obligation to consult with the Subordinated Creditor as regards the terms of any Counteroffer, reads (with emphasis added) as follows:

> *"Without prejudice to the generality of Clause 12.1, in the event that the Company determines to make a Counteroffer pursuant to Clause 11.2.3, it shall consult with the Subordinated Creditor regarding the terms of such Counteroffer; however, <u>the final decision regarding the terms of any Counteroffer shall be made by the Company in its sole discretion and having regard to the Relevant Principles</u>"*

(noting that Clause 12.2 previously provided that, in the absence of agreement between the Company and the Subordinated Creditor, the Company would "*issue a Decision Notice containing such Counteroffer as the Subordinated Creditor recommends*");

18.2 revising Part VI (*Dispute Resolution Procedure*) so as to expand the documentation to be treated as confidential and to clarify that the Subordinated Creditor must:

(a) only use confidential information it receives in relation to Certifications for the purposes of the Scheme;

(b) destroy (or return to the Company) such information once it is no longer reasonably required for the purposes of the Scheme; and

(c) ensure that such information is only provided to such individuals as is reasonably necessary for it to exercise its rights under the Scheme;

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* Shortly after the Chairman's Report was filed, it came to my attention that there was an error in one of the figures in paragraph 28. Instead of £126,795,278, the figure in line 7 of this paragraph should have been £126,794,828. An error in how the results of voting at Scheme Meeting 2 were recorded was also identified, with one Scheme Creditor's voting rights recorded as being £80 lower than their true value. Given that these errors do not affect percentage support figures cited for the Scheme Meetings, the Chairman's Report has not been reissued.

18.3 further revising Part VI (*Dispute Resolution Procedure*) to clarify that any person appointed to act as Adjudicator must be a former member of the England & Wales judiciary and/or an English law qualified Queen's Counsel.

19 Having made these revisions, to which the Subordinated Creditor consented, the Company provided a revised version of the Scheme, together with a revised version of the Explanatory Statement containing corresponding changes, to Scheme Creditors on 31 May 2018. This was effected by (i) posting an announcement with the revised documents on the Website [RD3/8-10] and (ii) sending an email or letter to all persons whom the Administrators believe are or may be Scheme Creditors (to the extent that the Administrators hold the necessary contact details) directing them to the announcement on the Website. The amended Scheme and Explanatory Statement were subsequently presented to Scheme Creditors at the Scheme Meetings.

20 Some Scheme Creditors (54 of those voting at Scheme Meeting 1 and 33 of those voting at Scheme Meeting 2) had given their voting instructions (and, in the case of Higher Rate Creditors, their Elections) before the updated versions of the Scheme and Explanatory Statement were circulated. Accordingly, the announcement and associated correspondence provided that Scheme Creditors could change their voting instructions and/or decision whether to elect for the Settlement Payment Option or the Certification Option in light of the amendments made. In the event, however, no Scheme Creditor did so.

D: OUTCOME OF THE SCHEME MEETINGS

21 Full results of the voting at the four Scheme Meetings are set out in the Chairman's Report filed at Court and published on the Website [RD3/12] on 9 June 2018. By way of summary:

(a) of the 132 votes cast by 8% Creditors and Specified Interest Creditors present and voting at Scheme Meeting 1, 129 votes cast were in favour of the Scheme, amounting to 97.7% support in terms of numerosity and 96.3% in terms of value;

(b) of the 78 votes cast by Higher Rate Creditors present and voting at Scheme Meeting 2, 74 votes cast were in favour of the Scheme, amounting to 94.9% support in terms of numerosity and 88.0% in terms of value;

(c) of the 55 Scheme Creditors who are members of the SCG present and voting at Scheme Meeting 3, all 55 voted in favour of the Scheme (one Scheme Creditor split its voting rights and abstained from voting in respect of one of its claims (which was of very small relative value), but because it voted in favour of the Scheme in respect of the remainder of its claims, percentage turnout remained 100%); and

(d) at Scheme Meeting 4, the Subordinated Creditor (being the only Scheme Creditor entitled to vote at that meeting) voted to support the Scheme.

22 Accordingly, the Scheme was approved by the requisite majority of Scheme Creditors present and voting at all four Scheme Meetings and, as set out above, it received an overwhelming level of support.

23 As noted at paragraphs 27 to 30 of the Chairman's Report, the above figures take into account Increased Voting Rights Requests received from a number of Higher Rate Creditors (including Higher Rate Creditors who opted to vote against the Scheme) pursuant to paragraph 13 of the Convening Order, all of which I accepted.

24 Of the nine Higher Rate Creditors who submitted Increased Voting Rights Requests, seven voted for the Scheme and two voted against the Scheme, as set out in further detail in the Chairman's Report.

25 As demonstrated by the figures in Table B of the Chairman's Report, any decision to accept these Increased Voting Rights Requests taken individually or collectively would have had no impact on the outcome of the Scheme Meetings and this was a principal consideration in carrying out a cursory review of those requests before concluding they all be allowed for voting purposes. If only those Increased Voting Rights Requests made by Scheme Creditors voting against the Scheme were accepted (and the value of the votes of those voting for the Scheme were calculated by reference to the Statutory Minimum interest rate of 8%), the Scheme would still have been approved by the requisite statutory majority.

26 Scheme Creditors who submitted Increased Voting Rights Requests were sent a letter on 6 June 2018 informing them that they had been accepted for the purposes of voting on the Scheme. My acceptance of Increased Voting Rights Requests for the purposes of the Scheme Meetings should not be taken as an indication that, in due course and applying the appropriate test, such Certifications will necessarily be accepted at that level.

27 As noted in paragraph 22(a) of the Chairman's Report, the Company also received a small number of requests from Scheme Creditors wanting to split their voting rights pursuant to paragraph 12 of the Convening Order. As at the deadline, five Scheme Creditors had submitted a Split-Holdings Request. All five Split-Holdings Requests were accepted and processed accordingly.

28 For the avoidance of doubt, it should be noted that, where a Scheme Creditor obtained split votes as a result of a Split-Holdings Request, it was not possible for such a Scheme Creditor to register multiple votes in favour or multiple votes against the Scheme at a single Scheme Meeting for numerosity purposes. Where a Scheme Creditor, having submitted a Split-Holdings Request, voted in favour of the Scheme in respect of one or more of its claims, and against the Scheme in respect of others, it was counted as casting one vote for the Scheme and one vote against it for the purposes of the numerosity test. As can be seen from the Chairman's Report, in the event, only a very small number of Scheme Creditors submitted

Split-Holdings Requests and thus the exercise of split votes had no impact on the outcome of the Scheme Meetings.

29 Further to the comments made by Mr Justice Hildyard on 11 May 2018, the Chairman's Report includes details of the number and value of votes cast for and against the Scheme by those Higher Rate Creditors who have elected for the Certification Option and the Settlement Payment Option.

E: THE FAIRNESS OF THE SCHEME

30 As explained in my First Witness Statement, the primary purpose of the Scheme is to provide a framework for the consensual determination of creditor entitlements to the Surplus, so as to facilitate an expedited payment to Scheme Creditors in respect of their Statutory Interest entitlements. In order to do this, the Scheme, among other things, brings an end to the long-running litigation concerning creditor entitlements to the Surplus and provides for a process by which Scheme Creditors can have their entitlements to Statutory Interest resolved outside of court and then paid.

31 In relation to claims arising under certain types of agreement (including 1992 and 2002 ISDA Master Agreements) pursuant to which there may be an entitlement to interest at a rate higher than the Statutory Minimum, the Scheme provides a process for (i) the certification of such claims; and (ii) the resolution of any issues arising from such Certification by means of reference to the Adjudicator (who will act as an independent expert). Certain Scheme Creditors have alleged that the process for certifying and the adjudication process under the Scheme are not fair and that the Scheme should not be sanctioned as a result. The Administrators' position on this is set out in the following paragraphs.

Certification

32 A Certifying Creditor must submit a Certification for the rate(s) and amount of interest applicable to its Higher Rate Claims. Such Certification must specify the rate(s) and amount of interest that the Certifying Creditor considers should apply to its Higher Rate Claim, having regard to the applicable Relevant Principles. As set out at paragraph 50 of my First Witness Statement, the Relevant Principles are as follows:

32.1 where a Higher Rate Claim is derived from an ISDA Master Agreement, the principles of the judgment of the Court in Tranche C, as set out in the declarations made by Hildyard J in an Order dated 12 December 2016 following his judgment (summarised in paragraph 11.2 of Part II of the Explanatory Statement);

32.2 where a Higher Rate Claim arises from an AFB Master Agreement or a FBF French Master Agreement, the AFB/FBF Agreed Position (as summarised in paragraph 11.3 of Part II of the Explanatory Statement);

32.3 in respect of all 8% Interest Claims, Specified Interest Claims and Higher Rate Claims, the judgments in Tranche A which are applicable to the calculation of Statutory Interest (summarised in paragraph 11.4 of Part II of the Explanatory Statement); and

32.4 for the purposes of calculating the amount of Statutory Interest payable in respect of (i) Specified Interest Claims, or (ii) Higher Rate Claims in respect of which the holder has elected to certify, where the applicable contract provides for a compound rate of interest, the principle that interest shall continue to compound in accordance with the contractual rate until the payment of a final dividend in respect of the applicable claim. This principle, although not specifically addressed in the Tranche A decision, reflects what the Administrators consider to be the correct interpretation of that judgment.

33 In response to a validly submitted Certification, the Company may engage in negotiations with a Certifying Creditor with the intention of reaching agreement as to which Decision Notice to issue. The Company will issue a Decision Notice pursuant to which the Company will either: (i) accept the Certification, (ii) propose a Counteroffer containing a Counteroffer Sum that is lower than the Certified Sum (which can then be accepted or rejected by the Certifying Creditor), (iii) reject the Certification without making a Counteroffer on the basis that the Company's decision is that the Certifying Creditor is entitled only to receive the Statutory Minimum, and/or (iv) make an Additional Information Request following which the Company will either accept or reject the Certification or make a Counteroffer.

34 The Company will consult with the Subordinated Creditor prior to issuing a Decision Notice. In circumstances where the Company and the Subordinated Creditor do not agree which Decision Notice to issue, the Company will make the decision in its sole discretion. In deciding which Decision Notice to issue, the Company must have regard to the Relevant Principles. In practical terms, the Company (in consultation with the Subordinated Creditor) will carry out an assessment of the Certification and will, in light of that (and following the provision of additional information if requested), consider (i) whether the Certification has been made in bad faith, irrationally or other than in accordance with the Relevant Principles, and (ii) whether a Counteroffer ought to be made.

35 In circumstances where the Company, having consulted with the Subordinated Creditor, concludes that the Certification has not been made in bad faith, irrationally or (unless justified) other than in accordance with the Relevant Principles, it will accept the Certification and the Certifying Creditor will receive the Certified Sum.

36 In circumstances where the Company, having consulted with the Subordinated Creditor, concludes that the Certification has been made in bad faith, irrationally or other than in accordance with the Relevant Principles, and that the Certifying Creditor is entitled only to

Statutory Interest at the Statutory Minimum of 8%, it will reject the Certification without making a Counteroffer.

37 In circumstances where the Company, having consulted with the Subordinated Creditor, concludes that the Certification has been made in bad faith, irrationally or other than in accordance with the Relevant Principles, but considers that the Certifying Creditor is entitled to Statutory Interest at a rate exceeding the Statutory Minimum (but less than the rate asserted in the Certification), it will reject the Certification and make a Counteroffer of such rate(s) and amount of interest as it considers accurately reflects such Certifying Creditor's entitlement to Statutory Interest having regard to the Relevant Principles (see Clause 12.2 of the Scheme).

38 Prior to the amendment of the Scheme referred to at paragraph 18.1 above, some Scheme Creditors expressed concern that the Subordinated Creditor could determine the level of the Counteroffer under the previous Clause 12.2 in circumstances where the Company and Subordinated Creditor could not agree on the level of that Counteroffer. Whilst the Administrators consider that such concern was overstated (as a result of the role of the Administrators as officers of the court, the discretion the Company retained over which Decision Notice to issue, the right the Certifying Creditor had to appeal the Decision Notice and the cost consequences of a failed Appeal) to the extent this was a concern it has now been addressed by the amendment to the Scheme referred to in paragraph 18.1 above.

39 Viewed as a whole, the Administrators consider the process for the submission and consideration of Certifications to be a fair one that provides an appropriate mechanism for the determination of entitlements to Statutory Interest in a timely manner.

Adjudication

40 As noted above, if there is a dispute between the Company and a Certifying Creditor in relation to Certification, this will be referred to the Adjudicator. The Dispute Resolution Procedure under the Scheme adopts a so-called "baseball" format, which has been a target for criticism among dissenting Scheme Creditors. The key feature of the "baseball" process is that, pursuant to Clause 24.7 of the Scheme, the outcome of any Appeal will be either the amount put forward by the Certifying Creditor in their Certification or the amount of the Counteroffer (or the Statutory Minimum where a Rejection Notice has been issued with no Counteroffer being made). Save in certain very limited circumstances – for instance where the Adjudicator concludes that there has been a mathematical or numerical error in either party's submission (in which case it may be corrected) – the Adjudicator is not permitted to determine that any other amount is the appropriate amount.

41 Having considered the matter carefully prior to launching the Scheme, it is the Administrators' view that the "baseball" approach is advantageous in that it encourages both parties to propose figures they believe are correct in the first instance, rather than figures that are speculative and submitted on the basis that the Adjudicator will seek to find a middle ground. The Administrators do not consider there to be anything unfair in encouraging the parties to put forward a position that they believe represents the "right answer" having regard in the first instance to the Relevant Principles. Limiting the possible range of outcomes of the Dispute Resolution Procedure moreover helps to simplify the process, thus promoting the expeditious determination of entitlements to Statutory Interest and an earlier payment of such Statutory Interest than would otherwise be achieved.

42 The Administrators further believe that the criticism of the "baseball" structure is misplaced on the basis that, as explained in paragraph 10.8.3 of Part II of the Explanatory Statement, the Adjudicator may only uphold the Company's Case if he or she is satisfied on the balance of probabilities that the Company has demonstrated that the Certification of the Certifying Creditor has been made in bad faith, irrationally or (unless justified) other than in accordance with the Relevant Principles. The burden of proof for establishing that one of these permitted grounds of challenge has been made out is on the Company. If the Company does not satisfy the burden, then the Adjudicator must uphold the Appellant Certifying Creditor's case.

43 The Administrators also note that both the Certifying Creditor and the Company are incentivised to refrain from putting forward cases which are speculative on the basis that there are cost consequences for the unsuccessful party. Under the terms of the Scheme:

43.1 if the Adjudicator finds in favour of the appellant Certifying Creditor, then the Company will bear, as an expense of the Administration: (i) its own costs, (ii) the reasonable legal costs of the Certifying Creditor incurred in connection with the Dispute Resolution Procedure (on an indemnity basis) and (iii) the fees, costs and expenses (inclusive of any VAT) of the Adjudicator and his or her Support Team; and

43.2 if the Adjudicator finds in favour of the Company, then the Certifying Creditor will bear: (i) its own costs, (ii) the reasonable legal costs of the Company incurred in connection with the Dispute Resolution Procedure (on an indemnity basis) and (iii) the fees, costs and expenses (inclusive of any VAT) of the Adjudicator and his or her Support Team.

44 At the convening hearing, Mr Justice Hildyard commented that "*the right which Wentworth sub has negotiated for itself, which caused most anxiety in terms of fairness is the provision that… if [the Adjudicator does] not accept the claim, you go straight down a slope - to the 8%... that raises a possibility that people will have to adopt a prudent, as opposed to their very best defensible position*…". I understand that "the right" that Mr Justice Hildyard refers to here is the right that the Subordinated Creditor had, prior to the amendment to the Scheme, to determine the level of the Counteroffer. By way of clarification, however, it was (and is) not the case that the certifying Creditor goes "straight down the slope - to the 8%".

In circumstances where the Company has made a Counteroffer and that Counteroffer has been rejected and then appealed, the Adjudicator chooses between the Certified Sum and the Counteroffer (being somewhere between the Statutory Minimum and the Certified Sum) and not the Certified Sum and the Statutory Minimum of 8%. It is only in circumstances where the Company has issued a Rejection Notice on the basis that it considers that the Certifying Creditor is entitled only to the Statutory Minimum of 8% that the Adjudicator will decide between the Certified Sum and the Statutory Minimum of 8% (and the Adjudicator will only select the latter if the Company is able to persuade the Adjudicator that the Appellant Certifying Creditor's Case was made in bad faith, is irrational or is otherwise not in accordance with the Relevant Principles).

45 It should also be borne in mind (as has been clarified – for the avoidance of doubt – by the amendments announced on 31 May 2018) that the Company will set the terms of any Counteroffer having regard to the Relevant Principles. This means that Scheme Creditors ought not to be deterred from putting forward their case out of concern that any Counteroffer will be made at a level which has been artificially depressed.

46 In all, I and the other Administrators consider that, while the Dispute Resolution Procedure necessarily differs to some extent from the process by which disputes might be resolved before a court, overall it is a reasonable one that contains the key elements one would expect to see in a fair and considered process for handling disputes, while at the same time promoting the expeditious resolution of disagreements.

Associated Issues

47 I deal here with other aspects of the process relating to Certifications and the Dispute Resolution Procedure which have been raised as the subject of concern, primarily in correspondence received in the run-up to the convening hearing.

48 The concerns raised are repetitive of those made previously and have been addressed by the Administrators in earlier correspondence, my First Witness Statement and the Administrators' skeleton argument for the convening hearing. However, I deal with them here again for convenience.

48.1 There is no requirement in the Scheme for the Company to give reasons for its Decision Notice, nor for the Adjudicator to give reasons for his or her decision. As noted above, one of the key advantages of the Dispute Resolution Procedure is that it is expeditious and will result in the determination of Scheme Creditors' interest entitlements sooner than would otherwise be the case. Requiring the Administrators or the Adjudicator to provide reasons for their decisions would inevitably slow this process down, watering down this key benefit. Notwithstanding this, however, the Scheme provides for a Consultation Period during which the Company may engage in discussions with the Certifying Creditor regarding their Certification (Clause 11.3 of

the Scheme). The Administrators envisage that, where that process is engaged, the reasons for rejecting a Certification will be discussed with a Certifying Creditor.

48.2 During the Consultation Period and prior to issuing a Decision Notice, the Company will consult with the Subordinated Creditor and may, in connection with this, provide it with confidential information. As stated at paragraph 77 of my First Witness Statement, I and the other Administrators consider it appropriate that the Subordinated Creditor be afforded such consultation rights taking into account (i) the economic impact of Statutory Interest payments to other Scheme Creditors on the Subordinated Creditor; and (ii) the fact that, if the Scheme did not accommodate the requirements of the Subordinated Creditor, the Wentworth Group would not support it. Having said this, in recognition of the potential concern, I and the other Administrators have amended the Scheme to provide further comfort in this regard (see paragraph 18.2 above). A Certifying Creditor does of course have the additional comfort that the Administrators are officers of the Court and will, thus, approach Certifications in a manner consistent with those obligations.

48.3 The Adjudicator will reach his or her decision without an oral hearing. The Administrators do not believe that the absence of an oral hearing gives rise to any fairness issues and consider that it is part and parcel of a streamlined adjudication process. The key point is that the parties have an opportunity to present their cases, which can include written evidence and written submissions, to the Adjudicator in advance of him or her reaching his or her determination.

48.4 Any decision by the Adjudicator will, insofar as the law allows, be final and binding and is the exclusive method for the determination of the subject matter of an Appeal. The Adjudicator’s decision can only be revisited in very limited circumstances (such as where a clerical error, miscalculation or mistake has been made by the Adjudicator and such an issue is brought to the Adjudicator’s attention within 10 Business Days of the decision being issued). The Administrators consider that this is an essential characteristic of a process designed to bring finality to creditor challenges with a view to achieving certainty as to the Surplus in order that distributions can be made as soon as possible.

48.5 If none of the Adjudicators identified in the Explanatory Statement is available, the Company and the Subordinated Creditor will seek to agree a replacement (but, where they cannot agree, the Company will appoint an alternate Adjudicator in its sole discretion). It has been suggested that the Subordinated Creditor should have no role in this regard. For the reasons explained at paragraph 48.2 above, I considered it appropriate for the Subordinated Creditor to have this right of consultation. Given that any Adjudicator will be former judiciary or Queen’s Counsel, it is not at all clear to me why there is any concern. In any event, given there will only ever be a few Appeals

(given that only nine Scheme Creditors have elected to certify) there is unlikely to be any issue in practice.

Other Fairness Issues

49 Various other "fairness" issues have been raised that are not directly related to the Certification and Dispute Resolution Procedure as follows.

49.1 A concern has been raised that Higher Rate Creditors who have chosen the Certification Option will only be paid after their entitlement has been determined, the suggestion being that there is no reason why, where 8% is the minimum rate they will receive in any event, they should not receive a payment reflecting this upfront (at the same time as Higher Rate Creditors who have chosen the Settlement Payment Option) pending resolution of their Certification. In the Administrators' view, however, this concern overlooks the fact that Certifying Creditors will still receive their Statutory Interest far sooner than they would but for the Scheme and any delay to receipt of their entitlement will be minor. This is because the Dispute Resolution Procedure is designed to be expeditious and streamlined. Payment in two instalments would, in itself, increase the costs involved with such a process. Further, a two-stage process might not be entirely straightforward given that, pursuant to the Scheme, the Company is entitled to deduct an amount payable in respect of its and the Administrators' costs in the event that the Adjudicator finds in favour of the Company. It may also increase the burden of compliance with the Company's obligations as regards withholding tax (which are not straightforward given the position in relation to withholding tax as described in paragraph 22 of Part II and paragraph 10 of Appendix 4 of the Explanatory Statement).

49.2 It is also the case that Higher Rate Claims that are controlled by the same party must all be subject to the same Election (i.e. a Higher Rate Creditor will not be able to choose the Settlement Payment Option in respect of some of the Higher Rate Claims that it controls and the Certification Option for others). This requirement is consistent with the proposal that the additional 2.5% payment be made in consideration for Higher Rate Creditors sparing the Company the time and expense associated with dealing with Certifications, i.e. a Scheme Creditor should not be entitled to receive such a payment while continuing to put the Company to the time and expense of dealing with Certifications in respect of other Higher Rate Claims that it owns. The requirement does not apply in respect of Higher Rate Claims which, although legally owned by the same Higher Rate Creditor, are not all controlled by that person (for instance because of sub-participations or similar arrangements). This is because imposing this requirement in such circumstances would effectively prevent any Election from being made where the persons controlling the underlying claims were not in agreement.

49.3 It is also suggested that the Scheme gives Higher Rate Creditors no form of compensation for the "loss of appeal rights" against the Tranche C judgment is being offered. I do not accept this. The conclusion of the Waterfall Proceedings (and other ongoing litigation) will greatly accelerate distributions to Scheme Creditors in respect of their entitlements to Statutory Interest. Absent the conclusion of the current litigation, it would be impossible to implement the accelerated timetable for distributions envisaged by the Scheme.

49.4 It has finally been suggested that it is unfair that a Certifying Creditor whose claim is rejected cannot subsequently claim the Settlement Premium. The Administrators reject this criticism and consider that the position is entirely fair in circumstances where the Settlement Premium is being offered to Higher Rate Creditors as a quid pro quo for choosing not to certify, as explained in paragraph 49.2 above).

Creditor Consultation

50 Following their appearance at the convening hearing, Deutsche Bank's solicitors, Clifford Chance, wrote to Linklaters requesting that the Company facilitate communication between Deutsche Bank and other Higher Rate Creditors so that they might consult together regarding concerns about the Scheme. On 22 May 2018, the Company posted an announcement on the Website inviting Scheme Creditors with concerns to come forward so that the Administrators might place them in contact with Deutsche Bank [RD3/6-7]. In the same announcement, the Administrators noted that Scheme Creditors might also wish to consult with the Wentworth Group and/or Goldman Sachs International, as other Scheme Creditors which had indicated a willingness to discuss the Scheme with others. By the date of the Scheme Meetings, no Scheme Creditors had contacted the Administrators seeking to be placed in contact with Deutsche Bank, Goldman Sachs International or the Wentworth Group. At the Scheme Meetings, Deutsche Bank appointed me as proxy to vote on their behalf against the Scheme which I duly did at the Scheme Meetings.

51 The Court will also recall that Marble Ridge and CRC appeared at the convening hearing to contest the class composition. Both Scheme Creditors are now supportive of the Scheme having voted to approve it and having elected to certify. A copy of a letter from CRC explaining its position is exhibited [RD3/20-21].

F: THE FAIRNESS OF THE SCHEME MEETINGS

52 Having acted as Chairman of the four Scheme Meetings, I consider that they were conducted in a fair manner and I have no reason to believe that there were any irregularities relating to the voting process.

53 Notwithstanding this, for completeness, in the run up to the deadline for Submitting Split-Holdings Requests, I note that Deutsche Bank raised concerns regarding the process set out in paragraph 7 of Part III of the Explanatory Statement whereby Scheme Creditors who hold claims that are beneficially owned by multiple parties may apply to split their voting rights for the various claims they hold so that they are able to vote in accordance with voting instructions received from the parties who control them. In particular, Deutsche Bank identified a potential issue with how the votes cast by the legal holder of a split claim would be treated for the purpose of calculating whether the Scheme had been approved by a majority of Scheme Creditors in number. In circumstances where the legal holder and the other party or parties controlling the claim(s) do not agree, the Explanatory Statement provided that one vote would be deemed to have been cast for the Scheme and one vote would be deemed to have been cast against the Scheme (with such votes effectively cancelling each other out). This mechanism follows what I understand to be the generally accepted practice for schemes of arrangement and in the opinion of the Administrators fairly records partial support and partial opposition to the Scheme without unfairly manipulating the results of the Scheme Meetings. In any case, as noted in the Chairman's Report, the small number of Split-Holdings Requests received means that this feature of the voting process had no impact on the outcome of the Scheme Meetings.

54 On 17 May 2018, Clifford Chance (on behalf of Deutsche Bank) wrote to Linklaters noting that Deutsche Bank was concerned "about both the fairness of the Scheme and the potential for abuse" and that answers to the questions set out therein would "also be relevant to the records of the voting at Scheme meetings that Mr Justice Hildyard [had required the Company] to keep" [RD3/13-14]. Linklaters responded to the points raised by Clifford Chance on 25 May [RD3/16-17], although in doing so they noted that most of the questions asked were not relevant to the matter of the voting records required to be kept by the Administrators.

G: STORM AND SHAREHOLDER UNDERTAKINGS

55 As explained in paragraph 3 of Part II of the Explanatory Statement, the Shareholder (in its capacity as the Company's parent) has agreed to enter into the Shareholder Undertaking pursuant to which it consents to the Scheme and, on and from the Effective Date, in consideration for third party rights and undertakings granted in its favour, undertakes certain obligations in connection with the Scheme, including (as applicable) granting or agreeing not to challenge or disturb the releases provided for by the Scheme.

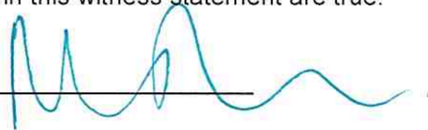
56 In addition, Storm, which has agreed its Statutory Interest entitlement with the Company (as further explained in paragraph 18.1.1 of Part II of the Explanatory Statement) also entered a deed of undertaking pursuant to which it agrees to be bound by the Scheme on and from the Effective Date (notwithstanding the fact that Storm is not a Scheme Creditor).

57 The Storm Undertaking was executed on 17 May 2018, while the Shareholder Undertaking was executed on 4 June 2018. The undertakings are exhibited to this statement at [RD4/1-74] and [RD4/75-177] respectively.

H: SUMMARY

58 The Administrators are extremely pleased with the level of support that has been shown for the Scheme as evidenced in the Chairman's Report. I strongly hold the view that this Scheme is the most appropriate way to resolve creditor entitlements to the Surplus, resulting in a distribution to creditors far sooner than would otherwise be the case. The Administrators have considered the fairness issues raised during the course of this process and amendments have been made to the Scheme to accommodate those where considered appropriate. I strongly believe that the issues we understand to be live do not impact on the fairness of the Scheme and I respectfully request that the Court make its order to sanction the Scheme.

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



RUSSELL DOWNS

Dated the 12 day of June 2018

Claimants
R Downs
Third Witness Statement
Exhibits RD3 to RD4
12 June 2018

IN THE HIGH COURT OF JUSTICE
BUSINESS AND PROPERTY COURTS OF
ENGLAND AND WALES
COMPANIES COURT (ChD)

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

-and-

IN THE MATTER OF THE COMPANIES ACT 2006

THIRD WITNESS STATEMENT OF
RUSSELL DOWNS

Linklaters LLP
One Silk Street
London EC2Y 8HQ

Tel: +44 (0) 20 7456 2000
Fax: +44 (0) 20 7456 2222
Ref: Susan Roscoe/Tony Bugg/Richard Hodgson