

**The Joint Administrators of LB Holdings Intermediate 2 Limited (In Administration) v Lehman Brothers Holdings Scottish LP3 and Others**

**The Joint Administrators of Lehman Brothers Holdings plc (In Administration) v Lehman Brothers Holdings Inc and Others**

[2020] EWHC 1681 (Ch)

**Before Mr Justice Marcus Smith**

This high-level summary has been prepared in the hope that it is of assistance to creditors. It is not, and is not intended to be, a detailed summary of what is a lengthy, complex and detailed judgment, which is itself available to creditors for review. Similarly, this summary does not constitute any form of advice and does not address the particular arguments which were deployed in the proceedings.

Background

The Lehman Brothers Group included many different entities, the ultimate parent company being Lehman Brothers Holdings Inc ("**LBHI**") and the main trading company in Europe being Lehman Brothers International (Europe) ("**LBIE**"). LBIE's parent company was LB Holdings Intermediate 2 Limited ("**LBHI2**"). Above LBHI2 in the corporate chain were LB Holdings Intermediate 1 Limited, and then above that company Lehman Brothers Holdings plc ("**PLC**"). In previous website updates, PLC has sometimes been referred to as "LBH".

Following the 2008 collapse of the Lehman Brothers Group, both LBHI2 and PLC entered into administration. Both administration processes have distributed very substantial assets to creditors, such that there is now a prospect that each of LBHI2 and PLC may in the future be able to make distributions towards repayment of their respective subordinated debts. These proceedings concern the priority of subordinated claims which exist against each of LBHI2 and PLC, and certain related matters.

Priority Issues in the LBHI2 Estate

In high-level summary, there are two types of subordinated debt claim asserted against LBHI2. Those are:

- What is referred to in the Judgment as Claim A, being PLC's claim against LBHI2 which arises under two long-term subordinated loan facility agreements and one short-term subordinated loan facility agreement made between PLC as a lender and LBHI2 as a borrower (together, the "**LBHI2 Sub Debt**" and the "**LBHI2 Sub Debt Agreements**"); and
- What is referred to in the Judgment as Claim B, being the claim of Lehman Brothers Holdings Scottish LP3 ("**SLP3**"), an indirect subsidiary of LBHI, against LBHI2 which arises under floating rate subordinated notes issued by LBHI2 pursuant to an offering circular dated 26 April 2007 ("**LBHI2 Sub Notes**"), the terms of which notes were amended by LBHI2 and SLP3 on 3 September 2008.

As the terms of the LBHI2 Sub Notes had been amended, the Judgment considers the position under each of the Unamended LBHI2 Sub Notes and the Amended LBHI2 Sub Notes. The parties accepted that it was the Amended LBHI2 Sub Notes which applied by the point of LBHI2's administration, but SLP3 argued that the Unamended LBHI2 Sub Notes were also relevant because (in high level summary) (i) the Amended LBHI2 Sub Notes must be read in light of the Unamended LBHI2 Sub Notes; (ii) the amendments did not alter the priority of the LBHI2 Sub Notes; and (iii) if the Court decided that the amendments did in fact alter that priority, any such change was a mistake which should be rectified to bring the LBHI2 Sub Notes back to their priority position under the Unamended LBHI2 Sub Notes.

In the Judgment, the Court found that in the priority dispute between the LBHI2 Sub Debt and the LBHI2 Sub Notes, the LBHI2 Sub Debt ranks ahead of the LBHI2 Sub Notes – in other words Claim A ranks ahead of Claim B.

Without seeking to summarise the Court's detailed reasoning, in high level terms, the Court considered that, properly construed, the subordination provisions in the LBHI2 Sub Debt and the Amended LBHI2 Sub Notes placed the latter debts below the former in priority ranking. The Court concluded that the amendments to the LBHI2 Sub Notes had changed its priority in this respect, but that SLP3's rectification arguments were not made out and there was no basis for the Court to treat that change as a mistake justifying rectification.

#### Priority Issues in the PLC Estate

In summary, there are three types of subordinated debt claim asserted against PLC. Those are:

- What is referred to in the Judgment as Claim C, being LBHI's claim against PLC which arises under two long-term subordinated loan facility agreements and one short-term subordinated loan facility agreement originally made between Lehman Brothers UK Holdings Limited as lender and PLC as borrower (together, the "**PLC Sub Debt**" and the "**PLC Sub Debt Agreements**"); these claims have been assigned such that they are now asserted against PLC by LBHI ; and
- What is referred to in the Judgment as Claim D, being the claim of LB GP No 1 Ltd ("**GP1**"), another company within the Lehman Group which is the general partner of a number of Partnerships, which arises under four sets of subordinated notes issued by PLC (together, the "**PLC Sub Notes**"); and
- What is referred to in the Judgment as Claim E, being a claim against PLC in the hands of holders of certain types of securities known as 'ECAPS', preferred securities issued by the Partnerships. All parties took the position that Claim E ranked below Claim C and Claim D, irrespective of the order of priority between those two claims.

In the Judgment, the Court analysed the subordination provisions and found that in the priority dispute between the PLC Sub Debt and the PLC Sub Notes, those claims ranked *pari passu* – ie neither claim ranked above the other. In other words, Claim C and Claim D rank at the same level within PLC's subordinated debts. The Court also confirmed that it would declare, as part of the ruling, that Claim E does indeed rank below Claim C and Claim D.

#### Other Issues for Determination

In addition to determining the relative priority of the above claims, the Court considered the following issues which arose in the PLC Administrators' application:

- Whether the effect of certain release clauses contained in a Settlement Agreement to which, amongst others, PLC and LBHI were party, in combination with the transfer of Lehman Brothers UK Holdings Limited's original claims under the PLC Sub Debt Agreements (Claim C) to LBHI, had caused that claim (Claim C) to be released such that it could no longer be asserted.

On this issue, the Court found that the terms of the Settlement Agreement did not release Claim C.

- In the alternative to the above, whether Claim C fell to be reduced, discharged or diminished by virtue of the interaction of LBHI's claims under the PLC Sub Debt Agreements with other instruments.

On this 'partial discharge' agreement, the Court found that Claim C was not reduced, discharged or diminished by virtue of the interaction of LBHI's claims under the PLC Sub Debt Agreements with other instruments.

- The stated maturity dates under the terms of the PLC Sub Notes are in 2035 and 2036. Another issue before the Court was whether this meant that the claims under the PLC Sub Notes were future claims such that when calculating the value of such claims against PLC they fall to be discounted under Rule 14.44 of the Insolvency (England and Wales) Rules 2016 ("**Insolvency Rules**").

On this issue, the Court found that the PLC Sub Notes Agreements did not contain an acceleration clause which brought forward their due date for payment, nor could such a provision be implied into the agreement or that result otherwise be arrived at. Accordingly, the Court found that the PLC Sub Notes are future debts which fall to be discounted under the Insolvency Rules.