

1 Wednesday, 13 November 2019

2 (10.30 am)

3 MR PHILLIPS: My Lord, just a short matter of housekeeping,
4 if I may, before we restart --

5 MR JUSTICE SMITH: Yes, indeed.

6 MR PHILLIPS: -- with Mr Miller.

7 At the end of his evidence yesterday, there was an
8 exchange, which your Lordship will no doubt recollect,
9 involving -- with your Lordship and Mr Miller, in which
10 Mr Miller explained that the formula he used for the
11 senior creditors was in use in the lower tier 2 dated
12 subordinated debt market, but he has said he has never
13 been able to pinpoint the exact precedent he used.

14 I want to make it absolutely clear, and my learned
15 friend Mr Beltrami said, that there is no single
16 document in the files that use this formula.

17 To assist your Lordship, we address this point at
18 paragraph 336 of our skeleton and, to a certain extent,
19 327, which refers to Mr Miller's correspondence with
20 Mr Barnett in November 2006, which your Lordship will
21 recollect has been shown to both Mr Miller and Mr Grant,
22 and I can give your Lordship the reference, but I don't
23 think we need it for this purpose.

24 If I could just perhaps go to our skeleton at 336,
25 and I promise I will --

1 Does your Lordship see that?

2 MR JUSTICE SMITH: Yes, I do.

3 MR PHILLIPS: The subordination mechanism reflected by the
4 entities in the marketplace at the time; so much is
5 clear from publicly available materials; and then we
6 refer to two dated subordinated note instruments issued
7 by, for example, Anglo-Irish and Standard Bank.

8 These are publicly available, they are publicly
9 available and to make it clear; we cannot say these are
10 the -- Mr Miller made that absolutely clear.

11 MR JUSTICE SMITH: Mr Miller was absolutely clear about
12 that.

13 MR PHILLIPS: Absolutely, we have done this exercise. But
14 just so your Lordship appreciates, my learned friend
15 Mr Beltrami's solicitors have not allowed these
16 documents into the trial bundle, so they are in
17 something called bundle K, which is miscellaneous
18 documents, which may of course explain why my learned
19 friend Mr Beltrami had not come across them.

20 For your Lordship's note, the references to the
21 senior creditors in those two documents, and I hope,
22 my Lord, you have bundle K, somewhere?

23 MR JUSTICE SMITH: I do.

24 MR PHILLIPS: Excellent. Well, I won't go any further than
25 just give your Lordship the references; it is not

1 appropriate at this point.

2 MR JUSTICE SMITH: No of course.

3 MR PHILLIPS: The senior creditors' definitions are at
4 tab 2, internal page 5, and tab 3, internal page 18.

5 MR JUSTICE SMITH: So K/2/5 and K/3/18.

6 MR PHILLIPS: Yes. To be absolutely clear, we are not
7 saying these are the precedents Mr Miller saw.
8 I thought that might assist you.

9 MR JUSTICE SMITH: Thank you very much.

10 MR BELTRAMI: Not wanting to raise the temperature too much
11 at the moment, but just to clarify a couple of things
12 under the guise of housekeeping.

13 If I had seen bundle K when I asked the questions
14 yesterday -- there has been quite a lot of
15 correspondence about bundle K, I won't take
16 your Lordship to it, where my learned friend's
17 solicitors sought to introduce it, and my solicitors
18 said: what is the relevance, no witness speaks to any of
19 these documents. And we never had an explanation of the
20 relevance. We may get an explanation in due course, but
21 insofar as any other point has been made subliminally,
22 those drafts, for whatever relevance they might have,
23 are not identical to this draft anyway. They are
24 different. So I don't know -- what we still don't know
25 what relevance is supposed to be afforded to them.

1 MR JUSTICE SMITH: Sorry, the drafts --

2 MR BELTRAMI: The drafts in bundle K.

3 MR JUSTICE SMITH: -- in the entirety or the drafts of the
4 relevant clause are different?

5 MR BELTRAMI: Yes, the relevant clauses in the documents in
6 bundle K are not the same as the clause that we have to
7 deal with.

8 So we have not -- we are no further forward, bundle
9 K doesn't take us any further forward from the point
10 that we left it yesterday, which is that the "identical
11 version" isn't anywhere in the court.

12 MR JUSTICE SMITH: Yes.

13 MR BELTRAMI: But if we can argue about that in the future,
14 so be it, but I am not entirely sure it is a matter of
15 housekeeping.

16 MR JUSTICE SMITH: It may be an argument for the future, but
17 it seems to me that Mr Miller was quite properly seeking
18 to assist the court with the origin of the wording; his
19 assistance, as I think he would be the first to accept,
20 was highly limited, but I regard even that qualification
21 as helpful because it means as matters stand, I am not
22 sure that I am particularly assisted by these documents,
23 whether they be identical or not.

24 MR BELTRAMI: Yes.

25 MR JUSTICE SMITH: Simply because Mr Miller can't say: I had

1 this document in mind when drafting or inserting these
2 particular changes. So there we are. If that
3 assists --

4 MR BELTRAMI: I think that is where we are in the evidence.

5 MR JUSTICE SMITH: -- then I am grateful to have all
6 information. That is how I at the moment regard it.

7 MR BELTRAMI: My Lord, yes, I am grateful. Thank you.

8 MR STEPHEN MILLER (continued)

9 Cross-examination by MR BELTRAMI (continued)

10 MR BELTRAMI: Mr Miller, good morning. I only have a few
11 more questions.

12 A. Morning.

13 Q. Can you be handed bundle C again, which is your witness
14 statement, and bundle F9. We were looking at 5250. And
15 in a sense, following on from the discussion I just had
16 with his Lordship, 5257 is the paragraph dealing with
17 status and subordination, which was amended from the
18 base document to the operative version which we know
19 about.

20 As his Lordship recapitulated, and as you indicated
21 yesterday, your evidence is this would have come from
22 a form, a different -- sorry, I use the word "form",
23 a different document, but you don't know the source of
24 that different document. But in any event, it wasn't
25 one of the regulatory forms?

1 A. I am sure I would have recollected if we had looked at
2 an actual regulatory form, although it is perfectly
3 possible that the model had some shared provenance with
4 those forms.

5 Q. I understand that. And just to absolutely clarify this,
6 if you go to 5257 and if you follow the version down,
7 and if you get to where it says B, do you see that about
8 half way down?

9 A. Yes.

10 Q. One of the changes that has been made from the PLC base
11 version to the operative version is a change in the
12 solvency condition attached to the subordination clause.
13 Whereas, as you will see with the crossed-out bit, there
14 was one solvency condition, namely "obligations which
15 are not payable ... issuer and excluded liabilities".
16 That was replaced by two solvency conditions, (i) able
17 to pay its debts as they fall due, and (ii) assets and
18 liabilities tax.

19 That is the change that was made, and the only
20 question I want to ask you, to be absolutely clear about
21 it, that didn't come from any regulatory form either,
22 did it, as far as you are remember?

23 A. I have no active recollection. But I can't remember
24 looking at regulatory form directly when looking at
25 this. I can't remember.

1 Q. Thank you. Just keep that bundle there for moment. Go
2 back to your witness statement, please, at paragraph 45.
3 First of all, paragraph 45, the first sentence, you say
4 there was no regulatory requirement for subordinated
5 debt to rank ahead of lower tier 2 debt such as the
6 sub-notes. But that is just another way of saying,
7 isn't it, that there was no regulatory requirement or
8 prohibition; the regulations were neutral on that point,
9 weren't they?

10 A. At that stage that would be correct.

11 Q. You then go on to say that the reference to subordinated
12 creditors reflected a general preference within
13 Lehman for flexibility, and what you mean by that,
14 I think, is this right; flexibility in having layers of
15 sub-debt?

16 A. Yes. I mean, there is two points here, I think.

17 When I did the correspondence with Mr -- responded
18 to Mr Barnett, I wasn't aware -- this was six months
19 before I was aware of the -- even the existence of the
20 other instruments.

21 So I am casting my mind back to that environment,
22 and I had that general recollection. So there is,
23 certainly if one is doing GENPRU, the model of the
24 expectation would be that you would layer lower tier 2,
25 upper tier 2 and innovative tier 1, one below each

1 other. Largely for market pricing reasons, I believe,
2 rather than because the regulations at that -- at the
3 iteration of where they stood at this time required it.

4 Q. Yes, but you also had flexibility, if required, to layer
5 between -- layer debt even if it had the same regulatory
6 capital tier?

7 A. Yes, or not.

8 Q. Yes or not. And when you say reflected, are you saying
9 that the drafting was done for that specific purpose, or
10 just that is the outcome, if you like; it reflects in
11 a sense that it achieves that general purpose?

12 A. I think it is just me trying to say that is my general
13 recollection of -- of the environment at the time.

14 Q. I understand, thank you. In this paragraph, you then go
15 on to refer to a different base prospectus for European
16 medium term note programme. It is in the bundle,
17 I won't take you to it necessarily, unless we need to,
18 but I don't think we do. But as I understand it, is
19 this right, what you are saying in this second half of
20 the paragraph is that there is another prospectus that
21 also allows for flexibility, rather than that that
22 prospectus is of any relevance to the drafting of this
23 document?

24 A. Correct.

25 Q. Thank you. Can you go back, please, to bundle F9/5264.

1 And just remembering what this document is, this was the
2 base document amended contemporaneously on 10 April, and
3 you will see on 5264, what is now paragraph 8 under
4 events of default enforcement has, I think, one change
5 to it, which is paragraph C at the bottom. There is an
6 addition of something in parentheses to change that
7 paragraph.

8 Keeping that open, could you also be handed bundle
9 F4, and go to 2022. This is, if you like, the other
10 side of the story, having looked at the internal -- what
11 was then the internal A&O amended version; if you look
12 at the bottom e-mail on 2022, dated 10 April, so the
13 same date, Mr Fletcher is sending to Jackie Dolby first
14 drafts of the offering circular, and Jackie Dolby is
15 replying on 12 April with a few changes.

16 We don't have, I think, in the bundle the attachment
17 to Mr Fletcher's e-mail. What we do have, if you go on
18 to 2024, are the amendment -- the version as amended by
19 Jackie Dolby. So as with these things, you can tell
20 what the base is and then you can see the amendments?

21 A. Yes.

22 Q. If you go to 2024, for example, at the top of the page,
23 he has changed the number from 6 billion to 6.139 to
24 make it accurate et cetera. The only thing I want to
25 ask you about, and it may be that we cannot take it any

1 further, but I want to ask it anyway.

2 If you go to page 2033, the paragraph 8, or clause 8
3 events of default and enforcement, which is not tracked
4 so I assume this -- it seems it may have come from A&O
5 at this point. It is very different to the version at
6 5264. I say it is very different; you see the first
7 paragraph --

8 A. Yes.

9 Q. -- has an addition to it, the second paragraph is,
10 I think, completely different and the third paragraph
11 has some changes to it as well. So someone has come in,
12 between the base document that we have looked at and the
13 document sent to Lehman, and decided to change
14 paragraph 8 as well. We can go through the detail, but
15 in a fairly material way. If you look at 8B, for
16 example, on 5264, it has all been crossed out and
17 something different has been put in in 2033.

18 So my only question, I say we may not be able to
19 take this any further, is do you have any recollection
20 as to why that change was made?

21 A. Based on this, no. It -- I am conscious we haven't got
22 the attachment to Mr Fletcher's e-mail.

23 Q. No, of course. Okay, maybe we cannot take that any
24 further, thank you. Now, can we -- if you still have
25 bundle F4, can you go, please, to page 2243.

- 1 A. Sorry, I didn't catch that.
- 2 Q. 2243. This is the letter which I think is your
3 reference; you are SMM, are you?
- 4 A. Yes.
- 5 Q. And this is the 1 May letter, the GENPRU compliant
6 letter sent by Allen & Overy to the -- not to the
7 company, but for the purpose of satisfying the GENPRU
8 requirement that the notes comply with the rule?
- 9 A. Yes.
- 10 Q. Therefore it is a matter -- plainly it is a matter of
11 importance, and you would need to satisfy yourself that
12 the letter was accurate in every respect? Can you look,
13 please, at -- can you go over the page, just to see the
14 structure. The structure is on 2243, you have set out,
15 you can see the second hole punch, bits of GENPRU, that
16 is 2.2.159, that is GENPRU, isn't it?
- 17 A. Yes.
- 18 Q. You set out bits of GENPRU and then indicated that --
19 you give your confirmation that the bit of GENPRU is
20 complied with and referred to at LB (inaudible).
- 21 A. Yes.
- 22 Q. So the first two, you don't need to worry about them but
23 over the page, the last bit of GENPRU that you set out,
24 number 3:
25 "To the fullest extent permitted under the laws of

1 the relevant jurisdiction, the remedies available to the
2 subordinated creditor in the event of non-payment or
3 other breach of the terms of the capital instrument must
4 be limited to petitioning for the winding up of the firm
5 or proving for the debt in the liquidation or
6 administration."

7 That is an extract from the GENPRU rule.

8 And you have confirmed this is explicitly provided
9 for in clause 8. The remedies available do not go
10 beyond those outlined in 2.2161.

11 Keeping that document there, can you go, please, to
12 bundle E, tab 4, page 59. This is the finalised
13 version. Page 59 has got clause 8 on it, the one we
14 just looked at, about events of default and enforcement,
15 which is the clause you just referred to in your letter
16 for regulatory purposes.

17 And if you look at clause 8A, which is again the
18 clause you referred to, it says:

19 "If a default is made for seven days or more in the
20 payment of principal due or 14 days ... interest,
21 noteholders may, at their discretion, and after taking
22 such preliminary steps as may be necessary, enforce
23 payment by instituting proceedings for the capital
24 insolvency of the issuer."

25 Do you see that?

- 1 A. Yes.
- 2 Q. Now, if you go back to page 53, the definition section
3 in clause 1, the definition of insolvency, capital I
4 insolvency, includes liquidation, winding up,
5 bankruptcy, sequestration, administration,
6 rehabilitation and dissolution, or the equivalent in any
7 other jurisdiction to which the issuer may be subject,
8 yes?
- 9 A. (Nods).
- 10 Q. So going back to page 57 clearly. Clause 8 permits
11 expressly the noteholders to enforce payment by
12 instituting proceedings for any one of those types of
13 insolvency; that is what it says, doesn't it?
- 14 A. It does.
- 15 Q. Can you go back to bundle F4, page 2244. The bit we
16 just looked at, re-reading the GENPRU section at the top
17 of the page, what is allowed under GENPRU, as you see:
18 "The remedies available to the co-ordinated creditor
19 must be limited to petitioning for the winding up of the
20 firm."
21 Which you said is expressly provided for.
22 So my question is: how did you satisfy yourself that
23 clause 8 was expressly consistent with GENPRU?
- 24 A. I must have done so at the time.
- 25 Q. Yes?

1 A. The definition of insolvency is from the standard form
2 IPRU loans. But I accept that it goes -- in terms of
3 the defined terms, goes beyond the words "winding up and
4 proving in administration".

5 Q. It does, but this is a very important regulatory
6 document, and you clearly did satisfy yourself at the
7 time, and the reason you satisfied yourself at the time
8 is you read, as everyone read, I suggest, "limited to
9 petitioning for the winding up of the firm" as being
10 broader than an Insolvency Act winding-up, but includes
11 those other forms of insolvencies, and that is
12 inevitably what you thought, wasn't it?

13 A. Yes.

14 MR BELTRAMI: Thank you, Mr Miller. My Lord, I think we may
15 have some furniture removal, so can we take maybe two
16 minutes?

17 MR JUSTICE SMITH: Yes, of course. I will rise for two
18 minutes.

19 (10.51 am)

(A short break)

21 (10.57 am)

22 Cross-examination by MS HILLIARD

23 MS HILLIARD: Good morning, Mr Miller. I am Lexa Hilliard
24 and I represent the general partner of the limited
25 partnerships. Could you turn up volume K. I understand

1 that this has been a bit of a subject of controversy,
2 but I hope there is not going to be any controversy over
3 the document I am going to take you to.

4 It is at tab 1 of volume K, and this is a paper that
5 Allen & Overy issued in November 2008, and I for one
6 have found it quite useful in understanding in basic
7 terms the capital adequacy regime, and I would like to
8 take you through it, in the hope that you will be able
9 to assist the court and me to just appreciate more what
10 was going on in this case. Is this a document that you
11 recognise, Mr Miller?

12 A. My name is on the back of it, so ...

13 Q. Exactly. I am not asking you to say that you wrote
14 every word of it, but it is something that you are not
15 unfamiliar with?

16 A. Correct. My colleagues wrote it and I read it.

17 Q. Yes. But you wouldn't hopefully disagree with the
18 content of it? Let's go through it, and if you disagree
19 with anything, you can say that you disagree with it and
20 why. If you just go over to the first page, background
21 and scope. The first paragraph there says:

22 "Capital adequacy provisions protect depositors and
23 other senior creditors of banks and other regulated
24 entities and help to maintain confidence in the
25 financial systems and promote financial stability."

1 So you would agree, wouldn't you, that the purpose
2 of the capital adequacy provisions therefore is to
3 protect depositors and senior creditors?

4 A. Yes, I would.

5 Q. And therefore you would agree, wouldn't you, that it is
6 no part of the capital adequacy provisions to protect
7 subordinated creditors or if I can say regulatory
8 capital creditors?

9 A. Yes, that's right.

10 Q. Would you also agree that the capital adequacy regime,
11 the directives IPRU/GENPRU say nothing about how
12 different layers of regulatory capital are to be treated
13 between themselves. So if you have got two sets of debt
14 within a particular tier, they say absolutely nothing
15 about how they are to be treated between themselves?

16 A. Yes, that must be right. In terms of do they qualify in
17 the tier or not, once they qualify in the tier, then
18 correct; as between tiers there will be differences.

19 Q. Yes, because you have got tier 1 which at its most basic
20 is ordinary share capital?

21 A. Yes.

22 Q. Of course once you get into tier 2, then it is no longer
23 ordinary share capital at best or at worst, it's
24 preference shares, cumulative preference shares, and
25 they would obviously always rank above ordinary shares?

- 1 A. Quite so.
- 2 Q. Okay. So if we can just now look at page 2 and
3 underneath the heading, "Capital structure". If you
4 just have a quick read of that, down to the end of that
5 section, just above "Features of capital in each tier"?
- 6 A. Okay.
- 7 Q. Now, you set out -- or not you, but your colleagues, set
8 out here the percentage limits imposed by the FSA in
9 relation to the tiers. Now, they were the same, weren't
10 they, in the period of time that we are talking about?
- 11 A. Yes, that is right.
- 12 Q. And in this -- in this paragraph, you introduce the
13 concept of regulatory capital that would otherwise
14 qualify for one tier but being pushed into another tier
15 because the regulatory capital in the tier that it would
16 otherwise qualify is already -- the percentage is
17 already too high, yes?
- 18 A. Yes --
- 19 Q. And the example that you give is, for example, if a bank
20 has core tier 1 capital of 100 million and issues
21 110 million sterling of capital securities which meet
22 the requirements for non-core tier 1, the rule requiring
23 at least 50 per cent of total tier 1 to be core tier 1
24 limits the bank to including over only 100 million of
25 the new issue as non-core tier 1, and therefore the

1 10 million excess, the overflow amount can be treated as
2 upper tier 2; yes?

3 A. Yes.

4 Q. So theoretically, then, if you had too great
5 a percentage of upper tier 2, it could be pushed to
6 lower tier 2?

7 A. Yes.

8 Q. And if that happened, that wouldn't change the ranking
9 between the upper tier 2 instrument and the lower tier 2
10 instrument?

11 A. Correct.

12 Q. Now, just below the features of capital in each tier,
13 there you go through the different types of tier 1
14 capital. You just turn -- read that and then turn over
15 the page and read down to the end of the description of
16 tier 1 capital.

17 A. Yes.

18 Q. So are you there?

19 A. Yes.

20 Q. So you would accept, wouldn't you, that with tier 1,
21 there can be different ranking, different priorities,
22 depending, for example, whether you have got shares that
23 have been created on terms that they are ordinary shares
24 only, or they are non-innovative as you call it,
25 preference shares?

- 1 A. That --
- 2 Q. Yes?
- 3 A. Yes.
- 4 Q. Now, if you would just read the section dealing with
5 tier 2.
- 6 A. Yes.
- 7 Q. At the end of that section, you say:
- 8 "On a winding-up, claims of the holders of upper
9 tier 2 instruments rank above claims in respect of tier
10 1 securities. Lower tier 2 claims rank in priority to
11 upper tier 2 claims but must be subordinated to all
12 subordinated creditors."
- 13 Yes?
- 14 A. Yes.
- 15 Q. Then if you just read the bit on tier 3. So there you
16 say tier 3 ranks pari passu with lower tier 2?
- 17 A. Yes.
- 18 Q. But having looked at the position in relation to tier 1,
19 and you having accepted that there is nothing in the
20 regulations that prohibits different rankings within the
21 tiers, it is not necessarily the case, is it, Mr Miller,
22 that tier 3 ranks pari passu with lower tier 2; it
23 depends on the terms of the particular instrument,
24 doesn't it?
- 25 A. That would be right. Perhaps the way to explain this is

1 that the ranking or the -- there is the regulatory
2 requirement, and then the reason I believe why upper
3 tier 2, for example, ranks below lower tier 2 is
4 an overwhelming custom in the market, which may
5 originally have been a function of pre Basel I rules
6 which go back to the mid-1980s. By that stage, or
7 surely by the stage we got to this stage, there was
8 a huge stock of capital which continued to roll and be
9 refinanced and refinanced over the years.

10 So the precedent was strongly set, not least because
11 the market could then price the refinancing costs of
12 capital as it came to be redeemed. Is this helpful to
13 explain this? So if we take upper tier 2 being
14 perpetual, so it has no stated maturity, it is, as
15 I understand it, nearly impossible to price the cost of
16 capital into perpetuity other than as equity, because as
17 a fixed income, what is the fixed rate; but it has
18 a call date, so the expectation but not the obligation
19 was that it would be refinanced periodically. So at any
20 point in time, the financial institution would be
21 monitoring those -- those baskets to make sure that it
22 was running its capital stack in accordance with its
23 policy for prudence and increasing shareholder value,
24 I suppose.

25 Q. But there you were just talking about upper tier 2, yes?

1 A. Yes, tier --

2 Q. And what I was asking you about is the statement, tier 3
3 ranks pari passu with lower tier 2.

4 A. Yes.

5 Q. You don't actually say --

6 MR PHILLIPS: Let him answer.

7 MR JUSTICE SMITH: Continue your question.

8 MS HILLIARD: Thank you very much, my Lord. That was the
9 question I was asking, in relation to your statement
10 that tier 3 ranks pari passu with lower tier 2, and
11 I was asking you, that wouldn't necessarily always
12 follow, it would depend on the terms of the instrument,
13 wouldn't it? There is no absolute rule to that effect.

14 A. There is no absolute rule to that, but the reason why
15 one would do it would be the practical reason of, unless
16 there is a reason, a commercial reason to layer it like
17 that, there is no reason.

18 MR JUSTICE SMITH: So to be clear, this last sentence is
19 a description of the default that you would -- that
20 would pertain, absent a contrary provision in the
21 instrument?

22 A. That would be right. This would be the convention or
23 default setting.

24 MR JUSTICE SMITH: And the former position may, as you said
25 earlier, reflect -- though I appreciate you are talking

1 about different tiers then, may reflect custom in the
2 market as to how these instruments are regarded relative
3 to each other.

4 A. That is right, and I would say, I would add, if it's
5 helpful, that tier 3 was something that was introduced
6 laterally after established practice upper tier 2 and
7 lower tier 2 came in. And my experience was there was
8 not a huge amount of tier 3 was issued, simply because
9 it wasn't worth it, because it needed to be refinanced
10 so quickly, is it short term, but that was just my
11 impression. We were very rarely instructed on tier 3s.

12 MS HILLIARD: But I think really what you are saying,
13 Mr Miller, as far as you were concerned, you know, you
14 would expect instruments within lower tier 2 and 3 to
15 rank pari passu between themselves?

16 A. As a general matter, yes.

17 Q. But you would also accept that ultimately, it depends on
18 the terms of the agreements itself, doesn't it?

19 A. Yes, yes, it does.

20 Q. Could you turn up bundle E and just turn to tab 9, which
21 is the first sub-note issued by Lehman Brothers Holdings
22 PLC. And just to remind you, that was issued on, you
23 can see at the bottom, 29 March 2005?

24 A. Yes.

25 Q. If you could just turn to page 139, what the note says

1 is that -- use of proceeds:

2 "The net proceeds of the issue of the notes,
3 expected to amount to 225 million euros, will be used by
4 the issuer to strengthen the regulatory capital base of
5 the group, to pay off existing loans and for general
6 corporate purposes."

7 Do you see that?

8 A. Yes, I do.

9 Q. Yes. So the notes in there is not just providing for
10 strengthening the regulatory capital base of the group,
11 yes?

12 A. Yes.

13 Q. It could, on this terminology, be used to strengthen the
14 regulatory capital base of the group, but also to pay
15 off existing loans and for general purposes, yes?

16 A. (Nods).

17 Q. And you would accept there is no distinction made in
18 this description between the three?

19 A. It could be doing all three.

20 Q. Yes, all three or only one, possibly?

21 A. Well, certainly it will do the first, strengthen the
22 regulatory capital base of the group.

23 Q. I think that's something probably for his Lordship.

24 But --

25 A. Sorry to clarify. By virtue of it being regulatory

1 capital.

2 Q. Well, this is something you might be able to assist us
3 with, because of course Lehman Brothers Holdings PLC was
4 not a regulated entity. So how was it regulatory
5 capital?

6 A. Within the consolidated framework.

7 Q. Well, Lehman Brothers Holdings PLC had not become
8 consolidated --

9 A. Okay.

10 Q. -- with the operating company, the European operating
11 company at this time.

12 A. Then I can't assist you on -- on why the group decided
13 to raise it in this particular format.

14 Q. I mean, just to put your mind at rest, an application
15 was made for a waiver?

16 A. Yes.

17 Q. And we will look at it?

18 A. Yes, indeed.

19 Q. But it is a bit confusing, I mean, it is all such a long
20 time ago but it is a bit confusing, because on the face
21 of it, I am not clear and nobody has been able to tell
22 me yet, why that was necessary if PLC was not
23 a regulated entity.

24 MR JUSTICE SMITH: Is there significance in the fact that it
25 is referring to the regulatory capital base of the

1 group?

2 A. Yes, I would say so, because it's -- as I understand it,
3 the FSA regulated on a consolidated basis. The facts of
4 that, I was not -- as an external solicitor, I was not
5 privy to how much capital a regulated entity required or
6 where in its group it would require it; but -- but what
7 it looked like once they figured out how much they
8 require and in what format.

9 MS HILLIARD: Thank you.

10 MR JUSTICE SMITH: Just one question. You put to the
11 witness that strengthening the regulatory capital base,
12 paying off existing funds and general corporate purposes
13 were in a sense three alternative purposes.

14 What I don't understand is whether if one, for
15 instance, paid off an existing loan, that might
16 nevertheless at the same time also strengthen the
17 regulatory capital base of the group. Is that possible?

18 A. If you replaced senior debt with subordinated debt,
19 I would say so.

20 MR JUSTICE SMITH: Yes, so it would either strengthen or
21 leave the same, the regulatory capital base --

22 A. Yes, yes.

23 MR JUSTICE SMITH: -- depending on the nature of the loans
24 being paid off.

25 A. Yes.

1 MR JUSTICE SMITH: Thank you.

2 MS HILLIARD: Mr Miller, could you now go to volume F2,
3 page 763.

4 A. Yes.

5 Q. This is an e-mail from one of your colleagues, Ms Smith,
6 who I understand is no longer employed by Allen & Overy,
7 yes?

8 A. Yes.

9 Q. And you can see that it is concerned -- it is dated
10 15th April 2005, and it is concerned with the
11 Lehman Brothers' subordinated note package.

12 Now the e-mail is dated, as I say, 15 April 2005.
13 So this was after the 225 million euro notes had
14 actually been issued.

15 A. That is right.

16 Q. Is that typically how these things were done with the
17 FSA? I mean, one issued the notes, one issued the
18 ECAPS, because the ECAPS were issued on the same day --

19 A. Yes.

20 Q. -- and then one sought approval after the event, as it
21 were?

22 A. I mean, that is clearly a matter for the relationship.

23 Q. I understand entirely, but ...

24 A. So the -- to give some background to this, the ECAPS
25 themselves, the focus was on getting the ECAPS into the

1 market, because once they were in the marketplace, they
2 were -- the investors had them and would -- if you
3 wanted to change them, you would need to convene the
4 investors.

5 The loan, I think, which was the partnership asset,
6 was something that could be done in-house, as it were,
7 or separately. So I think the timing of this was driven
8 by Mr Bowen and Mr Rushton --

9 Q. When you say loan, you are talking about the notes?

10 A. Sorry, the notes, forgive me, forgive me.

11 Q. It is a loan, we will come on to that in a minute, but
12 that is what you are talking about, yes?

13 A. Yes.

14 Q. So you have the copy letter to the FSA, that would have
15 been drafted by your firm, yes, Mr Miller?

16 A. Yes.

17 Q. And the way that application form, that would have been
18 essentially reviewed and topped and tailed by Allen &
19 Overy, yes?

20 A. Yes. This -- I think this package was prepared by us
21 and sent to the Lehman team for comment and review.

22 Q. Yes, and then a copy of the final version of the
23 offering circular, including the terms and conditions of
24 the note?

25 A. Yes.

1 Q. And then a copy of the standard terms in -- obviously
2 you didn't -- you might have drafted the memorandum
3 articles, but not at that time, and then a copy of the
4 standard terms in the FSA's Form 10.6 for the purposes
5 of consolidated supervision, annotated to show
6 cross-reference to the relevant terms and conditions of
7 the notes. And then a copy of a letter from your firm,
8 confirming that the terms and conditions of the notes
9 are materially identical to the FSA standard form. Now,
10 the signed version of that letter is actually at
11 page 760. Can we just look at that, please.

12 A. Yes.

13 Q. Now, that letter again is dated 15 April, so after the
14 issue, and you can see at the top of that letter, it has
15 got the initials SMM; so those are your initials?

16 A. Yes.

17 Q. So this was a letter that would have been drafted or at
18 least signed off by you on behalf of the firm?

19 A. Yes, it is. That is my writing, signed on the note
20 here.

21 Q. And that what you say in the first paragraph is that:

22 "We hereby confirm that subject to ... set out
23 below, the terms and conditions of the issue of the
24 issuer of the 225 million euro fixed rate subordinated
25 notes, due 2035, are materially identical to the

1 corresponding standard terms in the Financial Services
2 Authority's Form 10.6."

3 Then just at the next paragraph, you say:

4 "... but the terms and conditions of the notes
5 differ materially from the corresponding provisions in
6 ... standard form in the following ways ..."

7 So they are materially identical but there are some
8 material differences, yes?

9 A. Yes.

10 Q. Okay. So if we can just turn over the page. I think
11 possibly -- I am sorry I am asking you to turn up so
12 many documents, but I think if we can turn up J2, which
13 is the regulatory documents, and, in particular, Form
14 10.6 which is at page 765 of J2, tab 10. Are you there?

15 A. Yes.

16 Q. And the notes in effect were based, what you were trying
17 to do was saying: we are following 10.6 but we need
18 a waiver for this particular instrument that we are
19 going to use, because under the rules, the rules said
20 you have to use the standard forms unless you get
21 a waiver; yes?

22 A. Yes.

23 Q. So if I can just ask you to look at page 764 of J2.
24 That at the top -- 767, I gave you the wrong number,
25 767 -- that at the top, under 7, paragraph 7, heading is

1 loan or facility, with reference to paragraph 2 of the
2 standard terms?

3 A. Yes.

4 Q. And if we can just move forward to page 771. You have
5 "advance":

6 "... means where this agreement is for a loan
7 facility, an amount drawn or to be drawn down by the
8 borrower or otherwise made available by the lender under
9 this agreement as that amount may be reduced from time
10 to time by any repayment or pre-payment permitted under
11 this agreement."

12 And then if you go over the page, you have the
13 definition of a loan, and that means:

14 "The indebtedness of the borrower to the lender
15 referred to in paragraph 2.1 as that indebtedness may be
16 reduced from time to time by any repayment or
17 pre-payment permitted under this agreement."

18 Then just drop to paragraph 2, "whereas indicated in
19 the variable terms", and of course we were looking at
20 page 76 at the variable terms:

21 "Whereas indicated in the variable terms this
22 agreement is for a loan, the borrower hereby
23 acknowledges its indebtedness to the lender in the sum
24 mentioned in the variable terms as an unsecured loan
25 upon the subject of the terms and conditions of this

1 agreement."

2 And then subparagraph 2:

3 "Whereas indicated in the variable terms this
4 agreement is for a loan facility, the maximum aggregate
5 principal amount of each advance outstanding at any time
6 under the facility shall not exceed the maximum amount
7 specified in the variable terms ..."

8 Then B:

9 "The facility will be available until the last
10 available date specified in the variable terms."

11 And so it goes on. I assume you are pretty familiar
12 with that paragraph 2?

13 A. Yes, yes.

14 Q. You have also, on page 772 of J2, got the definition of
15 subordinated liabilities, and if we now go back to
16 F2/761, and your letter, you take that definition on the
17 left-hand side, "subordinated liabilities" means:

18 "All liabilities to the lender in respect of the
19 loan or each advance made under this agreement, and all
20 interest payable thereon."

21 And you say that the change that you want to make is
22 that it is "all liabilities to the noteholders in
23 respect of the notes and all liabilities of the issuer
24 which rank or expressed to rank pari passu with the
25 notes"?

1 A. Yes.

2 Q. And your explanation is below that. Do you want to just
3 read that explanation?

4 A. I have read it, yes.

5 Q. Okay. Now, in that explanation, you are saying that the
6 reason why you made this material change is because it
7 better reflects borrowing in a bond rather than a loan
8 format, and then you go on to say, "in particular, no
9 reference is made to the concept advances".

10 But in the regulated forms, there is a provision for
11 having an advance or a loan. So it is not apparent to
12 me why the extra language, "and all liabilities of the
13 issuer which rank or expressed to rank pari passu with
14 the notes", was necessary, as you say, to better reflect
15 borrowing in a bond rather than a loan format?

16 A. There is a point of background and an explanation. So
17 the point of background was that this was modelled --
18 I mean, copied might be a better word -- from
19 a transaction for a company called
20 Collins Stewart Tullett.

21 I will explain the challenge around that definition
22 of subordinated liabilities in a second, or the
23 thinking, shall we say.

24 But since this -- this came out, the problem with
25 this definition was something that I think people who

1 had been working in capital markets transactions had
2 been aware of before the creation of the FSA, but
3 Collins Stewart Tullett was the -- the entity that had
4 gone through this precise process of taking the loan
5 format and changing it into bond format, and also going
6 through the process of getting the FSA, who had been
7 going at that stage, I think, since the end of 2001,
8 comfortable, and they did that in 2004 but it was the
9 same regime.

10 So Lehman issuer here wanted to achieve the same
11 result and therefore did it in the same way, and indeed,
12 the waiver application references the precedent, because
13 it is one of the FSA's -- indeed they are set up to say:
14 if you have got a precedent or we have given a waiver,
15 please cite it. So it is cited in the waiver
16 application form for Collins Stewart Tullett.

17 So from memory, we went through a slightly iterative
18 process with the FSA, who had questions, and they would
19 ask the same question different ways, and this is where
20 this is where the language landed. And --

21 Q. Carry on?

22 A. Okay. So I think the -- when the problem with the
23 definition of subordinated liabilities under the form
24 was "means all liabilities to lender in respect of the
25 loan", I think we -- we didn't think of an advance

1 because an advance suggests a facility where you can
2 draw down amounts under that facility over time. The
3 bond issue, the notes issue was a one-off. It was more
4 like a bilateral loan.

5 Q. Yes --

6 A. Sorry.

7 Q. Go on.

8 MR JUSTICE SMITH: Do finish.

9 A. And the problem that people sort of struggled with was
10 that loan -- indebtedness referred to 2.1, which is the
11 indebtedness under this agreement.

12 So when we -- and that -- maybe one does several of
13 these agreements.

14 And I think that, I don't know if the point has been
15 made to your Lordship, but this is what people were
16 grappling with: is how do they interact with each other.
17 And perhaps it is one thing when you have got a private
18 loan arrangement, but when you take that to the capital
19 markets, and you are offering the securities to --
20 complying with rules concerning offering securities to
21 investors, then you have to ask the question, it is not
22 just -- you have to answer also the question: what are
23 the disclosure obligations?

24 Collins Stewart Tullett was listed on the London
25 Stock Exchange, it was marketed via an institutional

1 roadshow, and the question was: when you juxtaposed, it
2 is not going to be the loan, it is going to be the
3 notes, well, what happens if we do a second one? Where
4 does it rank amongst each other?

5 So it was to address this concern, and -- which had
6 been done previously and subsequently. So that is the
7 background as to why this formula, or this -- how this
8 was expressed to the FSA.

9 MS HILLIARD: Can we just look at the terms and conditions
10 of the notes in volume E, tab 9. Because on page 127.

11 A. 127, thank you.

12 Q. Are you there? At the top of the page it says, the
13 225 million euro fixed rate notes due 2035, notes,
14 "which expression includes any further notes issued
15 pursuant to condition 15, further issues, and forming
16 a single series therewith".

17 So that deals with your concern, doesn't it, that
18 there was a concern about any further issues under this
19 note, because it is clearly envisaged by the definition
20 that the term "notes", within the terms and conditions,
21 include any further issues under the notes?

22 A. That is dealing with a different point. So if you
23 increase the size of the issue, so if there is -- if
24 there's demand for more of this paper in the market,
25 then you issue more of them, so they become fungible,

1 with the outstanding issue.

2 What the concern was was if you -- your capital need
3 increased, and you needed to do -- to raise some more
4 supplementary capital, you could do it by -- if market
5 conditions made it economically viable, by increasing
6 the size of your existing transaction, but it may be
7 more economically viable to issue a second series priced
8 to a call date at a different point in the future.

9 So you wouldn't have it under the same agreement on
10 the same trust deed. It would be a copy of it, the
11 second one. Is that --

12 MR JUSTICE SMITH: And presumably it would reflect market
13 conditions at the time of this further issue, so you
14 would have to price, perhaps adjust other terms of the
15 notes to reflect the fact that you are coming later?

16 A. Yes, that would be a matter for the -- that would be the
17 daily business of the syndicate, now it's got a fixed
18 income, investment bank, revising their issuing clients
19 as to optimal market conditions to -- to raise the
20 finance in the best way that also meets their
21 regulatory, in this instance, the regulatory objectives.

22 MS HILLIARD: Just going back to your description,
23 I understand what you are saying about the first two
24 lines, about it better reflecting borrowing in a bond
25 rather than a loan format. It is what you say

1 afterwards when you say in particular, in other words to
2 justify that first sentence, you say: no reference is
3 made to the concept advances.

4 And all I am getting at is that advances is really
5 not relevant for the purposes of justifying that because
6 the -- the form has two possibilities; a loan or an
7 advance. So what you say about the advances is --
8 really doesn't take the matter any further, does it?

9 A. No, it just completes why it is not in there.

10 Q. And you say that you used the Collins Stewart format?

11 A. Yes.

12 Q. You would agree that the Collins Stewart format wasn't
13 exactly on all fours with the Lehman Brothers; the
14 clause was, but there were lots of other clauses
15 within --

16 A. The -- we could do a comparison, but I recall, I think
17 it -- I think it was constituted by a trust deed.

18 Q. Yes?

19 A. And -- rather than pursuant to a fiscal agency
20 arrangement.

21 Q. Yes, so that is fine.

22 So you said that the reason why you used, or
23 Lehman Brothers uses the standard form is because they
24 wanted the same result. When you are referring to the
25 same result, you mean you wanted the FSA to give the

1 waiver?

2 A. Yes, the same waiver.

3 Q. Can we drop now to the differences that you make from
4 clause 5 of the standard form. And you set out again on
5 the left the provisions in clause 5 of the standard
6 form, which are all to do with, if payments are received
7 by the lender, in circumstances where they shouldn't
8 have been done. I mean, in circumstances, for example,
9 where they hadn't obtained the permission of the FSA to
10 receive the payments when they should have done, but
11 those payments are held on trust by the lender.

12 And what you say in clause -- the reason why you say
13 you make the changes to clause 5 is because you say that
14 the notes are in global form, and it is envisaged that
15 the notes will remain in global form throughout their
16 life, and so that on each payment date, the common
17 depository holding the global note will present it for
18 payment to the principal paying agent.

19 And then you -- in the last paragraph, you say:

20 "The interest in the notes remain capable of being
21 freely transferable within the clearing system because
22 interest in the notes are held in the clearing systems.
23 It may not be possible to claw back the payment in the
24 way that one would in a loan context since it may not be
25 possible to identify precisely the ultimate recipients

- 1 of such payment."
- 2 A. That is right.
- 3 Q. And that is because the global note is held by the
4 depository, and then you have investors who actually
5 acquire interest through Clearstream in the issue, if
6 you like?
- 7 A. Yes.
- 8 Q. And they are not -- it is not necessarily easy to
9 identify who they are, is that right?
- 10 A. Yes, the clearing system won't tell you.
- 11 Q. No. And yesterday you explained to Mr Beltrami that
12 another way of issuing notes is that you -- rather than
13 issue a global note is that you issue a definitive note,
14 and that one would be likely to issue a definitive note
15 if you wanted to save costs, because it is actually more
16 expensive, you have to pay custody fees and so forth if
17 you issue it in a global form?
- 18 A. Yes, and that is quite so, and the reason why one puts
19 it into a clearing system is because that is what the
20 investors want. That is how they find it convenient to
21 hold the instrument.
- 22 Q. So the terminology that you used was on the basis that
23 this global note would be registered, listed on the
24 Channel Islands Stock Exchange, and interest in the
25 global note would be traded. That was why you used that

- 1 terminology, yes?
- 2 A. Sorry, that may be conflating a couple of things. We
3 are talking about the commentary on clause 5 to 8.
- 4 Q. Yes.
- 5 A. Again --
- 6 Q. 5, 6, 7, I was going to go on to clause 7, but we could
7 combine 5 and 7, yes.
- 8 A. Again, modelled on the Collins Stewart Tullett format,
9 and -- which was publicly tradeable, indeed, I think was
10 traded, so that Lehman, because they wanted to make sure
11 no differences, and it worked perfectly well because it
12 had a custody account, went that mechanic. And GP1
13 would have been -- I suppose it would have been held for
14 GP1.
- 15 Q. But, there was a capability, wasn't there, because that
16 is what the terms said, of using the notes and trading
17 the interest through Clearstream.
- 18 A. The instruments themselves needed to be tradeable. That
19 is the basis upon which the clearing system will accept
20 them, and that is also a listing requirement. If they
21 were to be traded, GP1 would have to agree to it,
22 because the notes were partnership assets and to be
23 dealt with in accordance with the Partnership Agreement.
- 24 Q. Yes. But the Partnership Agreement didn't preclude GP1
25 from disposing of the notes?

1 A. I -- I would need to look at it, I think.

2 Q. Okay, take it from me it didn't, and if I am wrong,
3 I will be corrected. Can we just go to F1/407. This is
4 another e-mail from your colleague, Ms Smith, and you
5 are copied into it. And she is attaching a draft of the
6 agency agreement for the subordinated notes. And then
7 she also attaches a current draft of the offering
8 circular for the subordinated notes and that:

9 "We anticipate receiving comments from the Channel
10 Islands Stock Exchange on this document during the
11 course of tomorrow."

12 So I think we have established the objective was to
13 get these notes listed on the Channel Islands Stock
14 Exchange?

15 A. Yes.

16 Q. Yes. Why was that?

17 A. So they could be a quoted eurobond.

18 Q. Why was that? Why was that important?

19 A. I am not a tax expert, but my understanding is that
20 because it is intra-group UK to UK, there would
21 otherwise be withholding on the payment. So these
22 instruments were done or this -- for that reason it
23 needed to be a quoted eurobond in format.

24 Q. So the process is that you send the document to the
25 Channel Islands, and they comment on it. What type of

1 comments would you expect from the Stock Exchange when
2 you forward those kind of documents? What are you
3 looking for them to say?

4 A. They have listing rules based on what -- the basic
5 disclosure rule is what an investor would expect to find
6 there, and there would be some specific, like
7 a box-ticking type information requirements, names of
8 directors, this sort of thing.

9 Q. Okay. Can you now just turn back to your witness
10 statement, that is at tab 1 of volume C.

11 A. Yes.

12 Q. What you say there is that -- at paragraph 24 -- in the
13 opinion that we were looking at earlier, it was
14 explained that a slightly different definition of
15 subordinated liabilities was used as it better reflected
16 borrowing in a bond rather than a loan format:

17 "This change did not affect the degree of
18 subordination of the LP1 sub-notes."

19 But I think you will agree that essentially that is
20 a matter for his Lordship and not you?

21 A. I would agree.

22 Q. Yes. And likewise, when you said in the opinion:

23 "In addition we hereby confirm that the terms and
24 conditions of the notes provide equivalent subordination
25 to that in the FSA standard form and that each note is

1 similarly and identically bound by the subordination
2 requirements ..."

3 That again is likewise a matter for his Lordship?

4 A. Yes, that was our opinion as stated.

5 Q. And if you could now just turn to paragraph 27. You say
6 at paragraph 27:

7 "I have since been shown the direction dated
8 26 May 2005 granted by the FSA in response to the waiver
9 application. Among other things it required that (a)
10 the degree of subordination of the loan capital is no
11 less than that provided for by Form 10.6 ..."

12 Yes? And you say a similar process was repeated for
13 the PLC sub-notes issued at LP2 and LP3. But the
14 direction that you got was dated 26 May 2005, so that
15 was after -- some two months after the issue of the
16 notes and the issue of the ECAPS. So if the degree of
17 subordination was in fact more than provided for by Form
18 10.6, it was too late.

19 A. Correct. One would have to change it.

20 Q. Yes. And I think you would agree, wouldn't you, that
21 when the FSA used that terminology, "degree of
22 subordination of the loan capital is no less than that
23 provided for by Form 10.6", that what the FSA was
24 referring to is essentially that it was no less than
25 required to ensure that non-regulatory capital creditors

1 got paid first because they had no interest?

2 A. Yes, one could put it that way, yes.

3 MS HILLIARD: I have no further questions, Mr Miller. Thank
4 you very much.

5 A. Thank you.

6 MR JUSTICE SMITH: It looks like it is you, Mr Phillips.

7 MR PHILLIPS: My Lord I have no questions in re-examination.
8 Does your Lordship have any questions?

9 MR JUSTICE SMITH: No. Thank you very much, Mr Miller.

10 I have no questions and you are released.

11 MR PHILLIPS: My Lord, that is a convenient moment for the
12 shorthand writers' break? That would be convenient
13 because I think there is going to be some more moving
14 around.

15 MR JUSTICE SMITH: In that case I will rise for five
16 minutes.

17 (11.45 am)

18 (A short break)

19 (11.50 am)

20 MR PHILLIPS: My Lord, before I call Mr O'Grady can
21 I mention one thing. I understand that there is going
22 to be a fire alarm at 12.45.

23 MR JUSTICE SMITH: I see.

24 MR PHILLIPS: And I also understand that we are supposed to
25 leave the building, but I may be completely wrong about

1 that. I thought I ought to mention it in case
2 Mr O'Grady is in the witness box and wonders what on
3 earth is going on.

4 MR JUSTICE SMITH: Right. Thank you for that intelligence.
5 That hadn't crossed my desk. If we do have a fire alarm
6 at 12.45, we ought, I think, then to take the short
7 adjournment then and resume at 1.45. What I will do now
8 is I will warn the witness, because I probably won't
9 have the chance to do so, given the fire alarm if it
10 occurs, that you are not to talk about your evidence
11 when you are in the middle of it to anyone. I would
12 normally give that warning when you rise, but in those
13 circumstances, it is probably best to say it now.
14 Thank you.

15 MR PHILLIPS: My Lord, may I call Mr Raymond O'Grady,
16 please.

17 MR RAYMOND O'GRADY (affirmed)

18 Examination-in-chief by MR PHILLIPS

19 MR PHILLIPS: Mr O'Grady, do you have file C?

20 A. Yes, I do.

21 Q. And if you could turn, first of all, to tab 8?

22 A. Yes.

23 Q. Do you see a witness statement of Raymond O'Grady, and
24 in the top right-hand corner, you can see it is dated
25 18 April 2009?

1 A. Yes.

2 Q. And if you look at page 127, 127, the last page, do you
3 see, is that your signature?

4 A. Yes, it is.

5 Q. And can I ask you to go over into tab 9, and you will
6 see a second witness statement, which is dated 9 May of
7 2019.

8 A. Correct, yes.

9 Q. And if we can go to the last page, do you see on
10 page 131 your signature?

11 A. Yes, I do.

12 Q. And do you have tab A?

13 A. A, yes.

14 Q. Do you see a document entitled "Errata to first witness
15 statement of Raymond O'Grady"?

16 A. Yes, I do.

17 Q. And over the page, is that your signature?

18 A. Yes, it is.

19 Q. Those two witness statements, subject to the errata, are
20 those your evidence to this court?

21 A. Yes, they are.

22 MR PHILLIPS: If you would wait there, there will be some
23 questions from my learned friend.

24 Cross-examination by MS TOLANEY

25 MS TOLANEY: Good morning, Mr O'Grady.

- 1 A. Morning.
- 2 Q. From 2000 to 2008 you worked in the Lehman Group's
3 financial control team in London, is that right?
- 4 A. Yes.
- 5 Q. And you describe the responsibilities of the financial
6 control function in paragraph 11 of your first
7 statement, is that correct?
- 8 A. That is the standard responsibilities that I describe.
- 9 Q. And broadly they comprise bookkeeping, accounting,
10 financial reporting and managing intercompany balances?
- 11 A. Correct.
- 12 Q. And it was no part of your role to structure capital
13 transactions or advise on structuring, was it?
- 14 A. That is correct.
- 15 Q. In your witness statements, Mr O'Grady, that is both of
16 them, subject to the errata, you describe how payments
17 due under the subordinated debts in issue in these
18 proceedings were made in practice?
- 19 A. I do, yes.
- 20 Q. And you don't say anything in your witness statements
21 about the contractual terms of those subordinated debt
22 instruments, do you?
- 23 A. No, I don't.
- 24 Q. Are you aware that PLC's and LBHI2's subordinated debt
25 instruments all contain contractual solvency conditions

- 1 to payment?
- 2 A. I am aware that it does contain them, but my statement,
3 as I set out, was just to deal with how things were
4 settled from the bookkeeping perspective, how the
5 Lehman entities settled these instruments.
- 6 Q. So your statement is to do with how payments that were
7 due were settled in practice?
- 8 A. Correct.
- 9 Q. And not to address the question of how payments became
10 due?
- 11 A. I am not quite clear, when you say how payments became
12 due.
- 13 Q. Under the terms of the contract, you didn't address the
14 contractual terms relating to how payments became due in
15 your statement?
- 16 A. Not directly in terms of I haven't specified certain
17 debt was settled, but the interest was paid monthly.
18 What I have set out to do is how those payments actually
19 occurred, without specifically addressing the terms to
20 say: this was paid monthly, this was paid annually.
- 21 Q. I am asking a different question, Mr O'Grady. The
22 question is not about whether they were paid monthly, or
23 the basis on which or the regularity on which they were
24 paid, but rather whether they were due at all under the
25 terms of the contract, and you don't address that at

- 1 all?
- 2 A. I do not address that, no.
- 3 Q. Were you aware of the contractual solvency terms at the
4 time when you are describing the settling of the books?
- 5 A. I would have read the terms of the PLC sub-notes and
6 I would have read the partnership agreements at the time
7 because of the role, and what we were expected to do to
8 support the partnerships. So I would suspect that I was
9 aware. But obviously I did not give it a lot of
10 attention.
- 11 Q. Because it was no part of your role to determine whether
12 a solvency condition had been satisfied?
- 13 A. I was never requested to check for a solvency condition
14 as part of my role.
- 15 Q. I don't need to take you to all of the contracts,
16 Mr O'Grady, but let's look together at the terms of the
17 ECAPS. So could you be given bundle E and turn to
18 tab 10, please. Have you seen this document before,
19 Mr O'Grady?
- 20 A. Yes, I have.
- 21 Q. Did you read it at the time it was issued? You can see
22 the date on the bottom, March 2005?
- 23 A. I would have read it in 2005. I couldn't say if it was
24 at the time of issue or just shortly afterwards.
- 25 Q. But you have read it in preparation for these

- 1 proceedings?
- 2 A. I did not read it in preparation for these proceedings.
- 3 Q. Could you turn to page 154, please. And can you see in
- 4 the middle of the page, "distribution rate"? On the
- 5 left-hand side, do you have that?
- 6 A. Yes.
- 7 Q. So if you just then read the text on the right, the
- 8 preferred securities, that is the ECAPS, will entitle
- 9 the holders to receive cash distributions, so
- 10 distributions, you have got that?
- 11 A. Yes.
- 12 Q. And then if you drop down to the penultimate paragraph,
- 13 you will see there, the holders will be entitled to
- 14 receive distributions only if the issuer has received
- 15 sufficient funds under the subordinated notes, which are
- 16 the PLC notes, or the eligible investments, which there
- 17 were none of, as the case may be. Do you see that
- 18 clause?
- 19 A. Yes.
- 20 Q. So no payments would fall due under the ECAPS unless
- 21 payments were made under the PLC sub-notes, that's
- 22 correct?
- 23 A. That is the contractual terms that have been laid out on
- 24 this document.
- 25 Q. Thank you. If you could go in the same bundle, back

1 a tab, to tab 9, please. These are the terms of the PLC
2 notes, the first tranche, and I think you said you would
3 have read these as well at the time?

4 A. Yes, I would have.

5 Q. And if you go to page 129, please, paragraph 3, and if
6 you read that clause from the second sentence in
7 subparagraph (a), that the rights of the noteholders in
8 respect of the notes are subordinated to the senior
9 liabilities, and so on.

10 And accordingly payment of any amount, whether
11 principal, interest or otherwise in respect of the notes
12 is conditional upon, and then if you drop down to (ii),
13 the issuer being solvent; do you have that?

14 A. Yes.

15 Q. And if you read clause B as well, please, that is the
16 definition of solvency in the contract.

17 A. Yes.

18 Q. So the effect of these clauses is that PLC is
19 contractually solvent, as defined in clause B, if it can
20 make the payments in question and be able to pay its
21 liabilities in full, excluding subordinated and excluded
22 liabilities, correct?

23 A. It states that:

24 "The issuer shall be solvent if it is able to pay
25 its liabilities other than the subordinated liabilities

1 in full, disregarding obligations which are not payable
2 or capable of being established and determined in the
3 insolvency of the issuer and the excluded liabilities."

4 Q. Yes, so you understand that what that is saying is it
5 has got to pay its liabilities, with a capital L,
6 excluding what it says there, the subordinated and the
7 excluded liabilities; that is the solvency condition?

8 A. Okay.

9 Q. And you see, going back to 3A, that payment of any
10 amount, whether principal, interest or otherwise, is
11 conditional on that solvency requirement, isn't it?

12 A. That is what it states; the note is payment of any
13 amount is conditional upon what is set out in 1 and 2.

14 Q. So if PLC couldn't meet the solvency test, then no
15 payments would fall due or be payable under the PLC
16 sub-notes?

17 A. I have not set out to cover this in my witness
18 statement. My witness statement covers how payments
19 actually took place at the time of these various
20 issuances. I have not offered a view on the terms
21 within the notes around the solvency conditions.

22 Q. I understand that, Mr O'Grady; it is simply that you
23 said that you were familiar with the solvency
24 conditions, and I am just asking you to confirm that you
25 understand that that was the effect of the solvency

- 1 condition?
- 2 A. I have read the solvency conditions, but I don't feel
3 I am in a position to offer a view as to what exactly
4 they mean, and I am not -- as part of my witness
5 statement, not looking to do that.
- 6 Q. But you can see what it says on the page?
- 7 A. I can see what it says, and I believe that is the -- the
8 interpretation of that is subject to these proceedings.
- 9 Q. So, just so that his Lordship is clear, you can't engage
10 with the meaning of the solvency test, you can only talk
11 about how payments were made in practice?
- 12 A. That is what my witness statement is focused on.
- 13 Q. Now, could you go then, to paragraph 70 of your witness
14 statement, please and this is of your first witness
15 statement, please. So in the second sentence of
16 paragraph 70, you talk about when interest was due for
17 payment on the PLC sub-notes, a payment would be made
18 from LBHI UK's bank account with an offsetting book
19 entry to its intercompany with PLC; can you see that?
- 20 A. Sorry, can you ...
- 21 Q. It is the second sentence, do you want to read that to
22 yourself, of paragraph 70 of your first witness
23 statement. (Pause)
- 24 A. Yes.
- 25 Q. So LBHI UK would be discharging a liability of PLC to

- 1 make that payment?
- 2 A. LBHI UK will be making a payment on behalf of PLC.
- 3 Q. Exactly?
- 4 A. And a resulting intercompany would be generated between
- 5 LBHI UK and PLC.
- 6 Q. And because the payment would be made on behalf of PLC,
- 7 as you have just said, a book entry would be made to
- 8 show the increase in PLC's liability to LBHI UK, would
- 9 it not?
- 10 A. An entry will be made to book a credit entry to PLC's
- 11 intercompany with LBHI UK. At each individual point,
- 12 I couldn't say if it was a net receivable or a net
- 13 payable, but it would result in an additional liability
- 14 from PLC to LBHI UK.
- 15 Q. And could you look at the sentence dropping down,
- 16 I think one sentence, in the same paragraph of your
- 17 witness statement, which starts:
- 18 "The payments to Euroclear in respect of interest on
- 19 the PLC sub-notes would fund the payment ..."
- 20 Do you have that sentence?
- 21 A. Yes, I have that sentence.
- 22 Q. So in other words, when a payment was due under the PLC
- 23 sub-notes, from PLC to the ECAPS partnerships, and then
- 24 a corresponding payment was due from the ECAPS
- 25 partnerships to the ECAPS holders, what you are

- 1 describing there is that LBHI UK would make the cash
2 payment through Euroclear to the ECAPS holders?
- 3 A. What I am describing there is that LBHI UK would make
4 a payment to PLC, sorry, to Euroclear, in respect of the
5 debt due between PLC and the partnerships, and that
6 payment then funded the payments to the -- to the ECAP
7 holders. So the point I am trying to make is that the
8 cash always originated from an LBHI UK bank account, not
9 from a PLC bank account.
- 10 Q. I understand the point you are trying to make, but just
11 to understand where that takes us, Mr O'Grady, what you
12 are discharging is the liability of PLC to the ECAPS
13 partnerships and the partnership's liability to the
14 holders by that cash payment?
- 15 A. It is that liability that had been discharged by the
16 payment by LBHI on behalf of PLC.
- 17 Q. And you refer in your evidence to PLC's ability to
18 source cash for payments under the ECAPS from LBHI UK,
19 as you have just mentioned. Now, nothing would be
20 payable to the holders of the ECAPS in the first place
21 if PLC didn't owe them money; you accept that, do you
22 not?
- 23 A. My understanding is that the source of the funds for the
24 partnerships was conceptual receipt from PLC. If that
25 payment was not made, I could not offer a view on

1 whether that cash could be sourced from elsewhere.

2 Q. I think it is a different question, Mr O'Grady. It is
3 simply that you were -- let's put it differently.

4 Payments were only being put through the books on the
5 basis that you understood that they were to be made
6 because they were owed on behalf of PLC?

7 A. Correct. During my time, any payments that were being
8 made was to settle the liability, for LBHI to make the
9 payment on behalf of PLC, to settle that liability
10 between PLC and the partnerships.

11 Q. And at paragraph 95 of your witness statement, you say
12 that pre insolvency, there would never have been
13 a situation in which LBHI2 had insufficient cash to make
14 payments under the LBHI2 sub-debt.

15 A. Pre insolvency, my understanding is that, yes, if
16 a payment needed to be made, it would be sourced from an
17 LBHI bank account.

18 Q. But that is a statement of the obvious, isn't it,
19 because you say in the same paragraph that the payments
20 were made by book entry and not cash?

21 A. The payment -- yes. Sorry let me rephrase that.

22 All payments of principal on the LBHI2 sub-debt,
23 LBHI2 sub-note and PLC were made by book entry. I have
24 stated that specifically because of what was asserted in
25 the Deutsche Bank position paper where it talked about

1 physical payments of cash to settle the PLC sub-debt,
2 the LBHI sub-debt and the LBHI2 sub-notes. It is to
3 emphasise that no physical cash moved. It was all done
4 by book entry.

5 Q. And I think, though, your point when you are emphasising
6 that, you say in response to Deutsche's position paper,
7 you were making that statement on the assumption that
8 the payments were in fact due, and that is what Deutsche
9 was referring to?

10 A. I was talking about the payments as they actually
11 occurred.

12 Q. You also say that a Lehman entity could simply borrow
13 from LBHI UK to fund any intercompany payments?

14 A. An entity would simply increase its intercompany
15 liability to fund a payment to another entity.

16 Q. And that would be an unsubordinated unsecured loan,
17 wouldn't it?

18 A. That would be booked as an unsecured intercompany, yes.

19 Q. Unsubordinated unsecured loan?

20 A. Unsecured, not subordinated, yes.

21 Q. Every dollar or pound borrowed would increase the assets
22 of the borrowing entity, but also its senior liabilities
23 correspondingly?

24 A. Yes.

25 MS TOLANEY: Thank you very much, Mr O'Grady, I have got no

1 further questions.

2 MR PHILLIPS: My Lord, there is no re-examination. I don't
3 know if your Lordship has any questions.

4 MR JUSTICE SMITH: No, Mr O'Grady, I don't have any
5 questions for you. Thank you very much for your
6 evidence and you are released.

7 A. Thank you.

8 MR PHILLIPS: My Lord, according to the trial timetable, the
9 next witness should be my learned friend's witness,
10 Ms Dolby.

11 MR BELTRAMI: I call Ms Dolby to come and give evidence, but
12 before I do so, my Lord, just to clarify this slightly
13 unusual situation. Your Lordship has probably picked up
14 the slightly unusual circumstances we are in, which is
15 that Ms Dolby is giving evidence on two sides of the
16 action, as it were. Your Lordship has probably picked
17 it up from bundle C, tab 12. There is my learned
18 friend's hearsay notice in which he puts in evidence.
19 Because we don't have a trial where one side goes first
20 and the other side follows, we are having a mix and
21 match, I have assumed it is all potentially taken as
22 done; he is putting in evidence a number of transcripts,
23 including two transcripts from Ms Dolby, and
24 your Lordship has seen them, at tab 14 and tab 21.

25 MR JUSTICE SMITH: Yes.

1 MR BELTRAMI: So that is, through my learned friend's
2 hearsay notice, her evidence on his side, if you like.
3 And I call Ms Dolby now to give her oral evidence.

4 MS JACQUELINE DOLBY (affirmed)

5 Examination-in-chief by MR BELTRAMI

6 MR BELTRAMI: Ms Dolby, good afternoon. Could you be handed
7 bundle C, please. There are a number of tabs in that
8 bundle. Please turn to tab 3 on page 31. You will see
9 a document which is entitled "First witness statement of
10 Jacqueline Dolby". Do you have that?

11 A. Yes, I do.

12 Q. If you turn on now, please, to page 44, there is
13 a statement of truth:

14 "I believe the facts stated in this witness
15 statement are true."

16 Is that your signature?

17 A. It is.

18 Q. Does this statement represent the evidence you wish to
19 give to the court?

20 A. It does.

21 MR BELTRAMI: Thank you. Please wait there for some further
22 questions.

23 Cross-examination by MR PHILLIPS

24 MR PHILLIPS: Ms Dolby, good afternoon. Ms Dolby, you may
25 have heard the exchange that I had with his Lordship

1 about the fire alarm, and I suspect that you are in fact
2 going to be the person affected by that, and I don't
3 know, my Lord, whether ...

4 MR JUSTICE SMITH: You are probably right. Ms Dolby,
5 I normally give this warning when we rise, but since we
6 may be rising in somewhat unusual circumstances, I will
7 ask you now when we rise not to discuss your evidence
8 with anyone at all. And please do bear that in mind.
9 It is unusual for me to give that warning; I normally
10 give it when we rise. But I suspect we will be exiting
11 the courtroom with the promptitude that is expected of
12 us when there is a fire alarm. Thank you.

13 A. Thank you, my Lord.

14 MR PHILLIPS: Ms Dolby, do you have your witness statement
15 in tab 3? We will be looking at that from time to time.
16 Could you please go to page 36 which is paragraph 29 and
17 30 of your witness statement, please. Do you see that
18 you start by describing the 2007 restructuring?

19 A. Yes, I do.

20 Q. And you will see that -- what you say in 29 and 30.

21 Would you like just to cast your eyes over that to
22 refresh your memory?

23 A. If I could, thank you.

24 Q. Of course. (Pause)

25 A. Yes, I have, thank you.

1 Q. And we see that one of your key roles was to work with
2 external tax advisers and US colleagues to devise and
3 implement the structures to reduce the overall tax
4 charge; you see that?

5 A. Yes, I do.

6 Q. And it is right, isn't it, that the 2007 restructuring
7 had a tax objective?

8 A. The 2007 restructuring had a US tax objective.

9 Q. Yes. And correct me if I am wrong, because you are
10 going to be much better at this than me, but that was to
11 reduce LBHI's consolidated overall profit and loss from
12 a US tax perspective, is that right?

13 A. That is correct.

14 Q. Thank you very much. And if you wouldn't mind just
15 going forward, the other document we might look at from
16 time to time is in tab 21. If you wouldn't mind just
17 going forward to tab 21. Do you see that this is the
18 a transcript of an interview that you had on 10 April?

19 A. Yes, I do.

20 Q. You see that you were faced with an awful lot of people,
21 and we see an awful lot of people ask you lots of
22 different questions.

23 MR JUSTICE SMITH: 10 April? It is 9 April, the transcript,
24 isn't it?

25 A. My Lord, I think I made an amendment to say that

1 actually it took place on 10 April.

2 MR PHILLIPS: Yes, there is a manuscript, there should be
3 a manuscript; maybe it is only on mine.

4 MR JUSTICE SMITH: There isn't on mine.

5 MR PHILLIPS: I am terribly sorry. The amendment, my Lord,
6 is in tab 22; yes, I can see what has happened on mine.

7 MR JUSTICE SMITH: I am sure it is right, I just wanted to
8 make sure I was looking at the right document. I have
9 corrected it.

10 MR PHILLIPS: Absolutely. If we could just look at page 11,
11 please, do you have page 11, and do you see between
12 lines 27 and 31, Mr Lawford, and he is my instructing
13 solicitor from Weil Gotshal, Mr Lawford puts a question
14 to you:

15 "... it is fair to say that the entire purpose of
16 issuing the LBHI2 sub-note and the quoted eurobond was
17 to get to a place where there was no tax at all on the
18 interest on the quoted eurobond?"

19 And you say:

20 "... no current year booked tax, yes. At some point
21 you might trigger it at a later point, yes, but that was
22 the driver for it."

23 So what you were explaining is the purpose of the
24 eurobond, the LBHI2 sub-notes, was to get to a place
25 where there was no current tax, no current year tax

- 1 booked on it, and that was right, wasn't it?
- 2 A. No current year tax booked on the interest income earned
3 by SLP3 on the quoted eurobond, yes.
- 4 Q. Yes, so that was right. And you were the lead person in
5 the London tax department driving the process, that's
6 right, isn't it? You said that between -- if you look
7 at line 32, you see Mr Wilson asks about the "we". And
8 he asks:
- 9 "Were you the central person in the tax department
10 who was driving the process?"
- 11 And you said:
- 12 "In the London-based tax department yes, but I would
13 have been working with my colleagues in the US
14 tax department and with advisers, third-party advisers."
- 15 And that was right, wasn't it?
- 16 A. That's correct. From a tax perspective I was the lead.
- 17 Q. Yes. Now, let's have a look, if you could be handed F4,
18 and if we can turn to 2278. Do you see that there is an
19 e-mail at the top that you send on the 2 May at 8?
- 20 A. I do.
- 21 Q. You see there is then in the middle, just picking it up
22 in the middle, you send an e-mail -- at the bottom,
23 sorry, the 9.17 am e-mail which is the 8.17 e-mail you
24 send an e-mail to a number of people and you are
25 congratulating your corporate division team work. You

1 point out it brings to an end a 4-month project to
2 create a tax efficient funding structure that will
3 result in an ongoing tax benefit of \$200 million
4 per annum. And you say that you are very proud to have
5 led the following individuals in the tax project, all of
6 them made key contributions to ensure smooth
7 implementation within the tight time frame, demonstrated
8 excellent cross-corporate division team work. And you
9 are saying to everyone: Please congratulate all the
10 members of your team.

11 So it is a congratulatory e-mail to everyone at the
12 end of the project. And if we just go over the page we
13 see a list of various individuals and we see at the top
14 Sophie Hutcherson, Sarah McMorrow, Emily Upton,
15 Ray O'Grady, Gareth Bowen; names that we will see.

16 It doesn't mention Mr Katz. Mr Ben Katz?

17 A. No, it doesn't.

18 Q. Is that because he was not on the 2007 refinancing?

19 A. He was nothing -- to my memory, he was nothing to do
20 with the -- it was a corporate initiative he wasn't
21 involved in.

22 Q. Yes. And in this congratulatory language you confirm
23 that you were the team leader on the 2007 refinancing
24 and that is right, isn't it?

25 A. Yes, from a UK perspective.

1 Q. Yes. And you wanted to advise. You see in the first
2 paragraph, you wanted to advise that it had all come to
3 an end and it created a tax efficient funding structure
4 resulting in an ongoing tax benefit of about 200 million
5 a year. So the purpose was to create a tax efficient
6 funding structure, that's right, isn't it?

7 A. That's correct.

8 Q. And you achieved that through the new structure; in
9 other words, the creation of the LBHI2 sub-notes, that
10 is right, isn't it?

11 A. The LBHI2 sub-notes, yes, being invested in by SLP3,
12 that is right.

13 Q. Thank you very much. Now, can we just have a look at
14 paragraph 52 of your witness statement in tab 3.

15 A. Sorry, paragraph 52?

16 Q. 52, please. Thank you very much. Do you see that what
17 you are there describing, you say:

18 "In the course of the steps to put in place the
19 LBHI2 sub notes, I didn't think about what might happen
20 in any insolvency of LBHI2. There was no reason to do
21 so. Similarly I didn't think about what the relative
22 priority of the sub-notes in the remaining sub-debt
23 would be on any insolvency."

24 Can I just ask you, could you be handed bundle E,
25 please. Could you turn to tab 4, please. You probably

1 recognise this. This is the offering circular for the
2 sub-notes and I wonder if you would be so kind as to
3 turn to page 55. And you will be pleased to know I am
4 not going to ask you to try and construe it. But do you
5 see there the status and subordination provision in
6 paragraph 3?

7 A. Yes.

8 Q. And you didn't have any issues with the terms of
9 clause 3, did you?

10 A. Clause 3 status and subordination, no. It wasn't of
11 a tax concern to me.

12 Q. And you have told us in the paragraph we just looked at,
13 that you didn't think about relative priority between
14 the sub-notes or the sub-debt; you told us that in the
15 paragraph we just looked at. And that was right, wasn't
16 it?

17 A. Yes. My colleagues in treasury and regulatory might
18 have had a different view and might have had an interest
19 in the tiering of the subordinated debt, but it wasn't
20 a tax concern for me.

21 Q. You can only help his Lordship with what you thought and
22 what you did, so I am going to try to focus in on that,
23 to really help you. Paragraph 53 of your statement, do
24 you see in paragraph 53, you say:

25 "It was important to the transaction that A&O

1 confirmed that the LBHI2 sub-notes complied with the
2 relevant regulatory rules for lower tier 2 capital.
3 There was no reason for us to think about or seek advice
4 on the relative priority of the different subordinated
5 debts in the case of insolvency."

6 Can you just deconstruct that a bit.

7 You didn't think that Lehman would become insolvent,
8 did you?

9 A. No.

10 Q. You did not consider what would happen in an insolvency
11 agreement?

12 A. That is correct.

13 Q. You didn't think about the ranking of the regulatory
14 capital sub-debt?

15 A. I did not.

16 Q. You didn't think about the relative priority of the
17 regulatory capital sub-debt?

18 You are pausing?

19 A. No, the relative priority I wouldn't have thought of,
20 no.

21 Q. Please, if any of my questions are not clear to you,
22 just tell me and I will have another go.

23 A. No, no, that's fine.

24 Q. And you didn't seek advice on or think about the
25 relative priorities or ranking of that sub-debt in an

1 insolvency; it is not something you took advice on
2 either, is it?

3 A. It isn't, no.

4 Q. You did tell -- sorry. I will restart that.

5 You did not tell either HMRC or the FSA that the
6 refinancing debt, which is the LBHI2 sub-notes, would
7 rank differently to the refinanced LBHI2 sub-debt;
8 that's right, isn't it?

9 A. Unless I looked specifically at the documents,
10 I couldn't confirm that categorically but I don't recall
11 that.

12 Q. Okay. Let's have a look if you may, if you have got
13 bundle F4 still and if you can go forward -- have you
14 got --

15 A. Yes.

16 Q. Sorry, I put it in the wrong cubbyhole.

17 Can we look at 1897, please. Do you see that -- do
18 you have that?

19 A. Yes, I do.

20 Q. Excellent, thank you. Do you see that this is a letter
21 of 30 March 2007 and it is addressed to Andrew Martyn at
22 HMRC, do you see that?

23 A. Yes, I do, yes.

24 Q. And if you would just go to page 1906, which is the
25 final page, do you see that this is a letter signed --

1 sorry. Do you have it?

2 A. By myself.

3 Q. A letter signed by you, yes. Okay. Now, if we look at
4 the first page, go back to 1897. This was a clearance
5 application, a request for clearance under sections 24
6 to 31 and schedule 3 of the Finance Act. So it is a tax
7 clearance application that you are making on behalf of
8 Lehmans.

9 If we look at, do you see the second paragraph, you
10 refer to a previous clearance application, do you see
11 that?

12 A. Yes.

13 Q. And then if we go on to the third paragraph, you say
14 that you have complied with some procedures, but you
15 then say:

16 "Lehman Brothers hereby request clearance that
17 a notice will not be issued under the above provisions
18 in relation to the series of transactions set out below
19 which will involve ..."

20 Amongst other things, three Scottish limited
21 partnerships and two US check-the-box entities.

22 You see that?

23 A. I do.

24 Q. And you then say the restructuring is being driven by
25 commercial inefficiencies in the current structure and

1 US tax considerations.

2 So that was the tax consideration that you described
3 to his Lordship at the beginning of your evidence, is
4 that right?

5 A. That is correct.

6 Q. And you then say the main purpose of the transactions is
7 not to provide a UK tax advantage, and you explain that
8 the UK tax deductions remained the same. And then --
9 that was right?

10 A. That's correct.

11 Q. Yes, and then you get on to the background to the
12 transaction, and we can just cast our eyes over that.
13 And then if I could just perhaps pick up at paragraph 7,
14 do you see you say:

15 "In recent years, there has been a significant
16 expansion of Lehman Brothers' activities in Europe,
17 resulting in an increase in business booked to LBIE. To
18 ensure LBIE continues to meet its regulatory capital
19 requirements, LBIE has received significant equity
20 injections drawn down on increased intercompany
21 subordinated debt facilities, always maintaining a ratio
22 of debt to equity within regulatory limits and within
23 thin capitalisation limits agreed with HMRC."

24 Do you see that?

25 A. I do.

1 Q. And as far as you are aware, that was correct?

2 A. It was.

3 Q. And then if we move over the page on to 1899, after you
4 see, sort of going through those paragraphs, you cast
5 your eye quickly over 12, you see that you identify
6 the -- the long-term and short term sub-debt, and then
7 proposed new entities in 15:

8 "It has been resolved to change the financing
9 structure as a consequence of US tax and commercial
10 inefficiencies in the current structure."

11 And you come back to that in C below. Could you see
12 that?

13 A. I do.

14 Q. Again, that is -- and you are going to explain it in
15 more detail, but that is those tax concerns, isn't it?
16 Is that right? That was the tax concerns that you have
17 been describing?

18 A. Well, I wouldn't call it a tax concern. We were trying
19 to create a tax benefit.

20 Q. Sorry, you are quite right, a tax benefit rather than
21 a concern. To someone like me, whenever I hear the word
22 tax, I always get concerned.

23 Then we get on to paragraph 16, and you refer to the
24 restructuring involving various steps, and if we look at
25 C, you will see that the intention was to remove

1 LB Spain from the structure at some point. And then in
2 paragraph 17, you say:

3 "It is important to note that following the
4 implementation of the proposed transaction, the
5 Lehman Brothers European Group will be claiming exactly
6 the same net UK tax deduction that it has been claiming
7 under the current financial structure i.e. there is no
8 disadvantage to the UK tax base as a consequence of the
9 new proposals which are driven by Lehman Brothers'
10 commercial, regulatory and US tax objectives."

11 So correct me if I am wrong, but what I understand
12 from this is you are explaining to HMRC that as far as
13 UK tax is concerned, this is tax neutral, this is not
14 going to make any difference; is that right?

15 A. That is right.

16 Q. You say:

17 "The subordinated debt will continue to be provided
18 for general business purposes. However, it should be
19 noted that future funding of LBIE may be provided
20 through SLP2 and SLP3."

21 Do you see that?

22 A. I do.

23 Q. If we move on, you then see that you have a section on
24 clearance details and the details of the participation
25 of the various entities. And I am not proposing to take

1 you through the details of all the entities, and
2 I wonder if you could go forward to 1902, please. Do
3 you see that you there set out the details of the
4 transaction?

5 A. I do.

6 Q. And this is setting out how the finance was to be
7 provided to LBIE. So do you see it says:

8 "Under the new arrangements, finance will be
9 provided to LBIE as follows ..."

10 A. I do.

11 Q. And of course, LBIE was a regulated entity, that is
12 right, isn't it?

13 A. It was.

14 Q. So LBUK2 issues a debt instrument. LB PLC transfers
15 debt instrument 1 to LB Holdings. LB Holdings transfers
16 a debt instrument. SARL transfers a debt instrument.
17 And you see a series of transfers of debt instruments.
18 Do you see that?

19 A. I do.

20 Q. And at the bottom you say:

21 "Subject to capitalising any part of LBIE ... LBUK2
22 subordinated debt by way of an issue of preference
23 shares in LBIE ..."

24 Do you see that?

25 A. I do.

- 1 Q. "... this will mean that LBIE will still claim tax
2 deductions for the interest payments on its loans."
- 3 It is right, isn't it, that by issuing debt rather
4 than shares, you were able then to claim the interest
5 when it came to tax matters; is that right?
- 6 A. Yes. So you would ordinarily, if you had to pay
7 interest on a -- on a debt that you had, you should get
8 a tax deduction for that interest expense, and
9 ordinarily, if you had preference shares, you wouldn't
10 get a tax deduction from any coupon on those preference
11 shares.
- 12 Q. And the notes are instruments which are treated as debt
13 for US GAAP purposes, that's right, isn't it?
- 14 A. Sorry, which -- which instruments?
- 15 Q. The notes, the debt notes. They are treated as debt for
16 US --
- 17 A. The subordinated debt?
- 18 Q. -- GAAP. Yes.
- 19 A. Yes.
- 20 Q. So they are treated as debt for GAAP purposes, but
21 equity for tax purposes, is that right?
- 22 A. No, the subordinated debt is treated as debt for GAAP
23 regulatory and tax purposes.
- 24 Q. Yes. But they are not treated as shares?
- 25 A. That's correct.

1 Q. So if we can then look over the page to 1904. Do you
2 see that under identification and explanation of the
3 arbitrage arising, under that, there are some bullet
4 points, tax consequences. And if you can go five
5 bullets down, do you see that you explain that the
6 overall tax impact of the transaction is a US tax timing
7 benefit?

8 A. Yes, I do.

9 Q. And that was right, wasn't it?

10 A. That's correct.

11 Q. And then you move on in C to the purpose of the
12 transaction.

13 My Lord, I am going to go through section C. I am
14 looking nervously at the clock, and I am not sure
15 whether to start or whether to pause at this point.

16 MR JUSTICE SMITH: What we will do is, fire alarm or not, we
17 will rise now, and we will resume at 1.45 if that suits
18 the parties.

19 MR BELTRAMI: My Lord, yes.

20 MR PHILLIPS: I am obliged my Lord.

21 MR JUSTICE SMITH: I am much obliged.

22 (12.42 pm)

23 (The short adjournment)

24 (1.47 pm)

25 MR JUSTICE SMITH: Good intelligence, Mr Phillips.

1 MR PHILLIPS: Yes, no, absolutely, my Lord. Not mine
2 though, I hasten to add.

3 Ms Dolby, we were just looking at the letter, you
4 may remember. Do you still have that letter in front of
5 you?

6 A. I do.

7 Q. Excellent, thank you. And we had just got to section C,
8 the details and purpose of the transaction. In this
9 section, as you can see from the heading, you explain
10 the purposes of the transaction, do you see that?

11 A. I do.

12 Q. Then you go on to say:

13 "As noted above, in recent years there has been
14 a significant expansion of Lehman Brothers' activities
15 in Europe, resulting in an increase in business booked
16 to LBIE. To ensure that LBIE continues to meet its
17 regulatory and capital requirements, LBIE has received
18 significant equity injections and has drawn down on
19 increased intercompany subordinated debt facilities."

20 So you see what you are describing there, that was
21 correct, wasn't it?

22 A. That was correct.

23 Q. And we then go to the primary purposes of the proposed
24 restructuring, and the first bullet point:

25 "The funding provided through the current group

1 structure must be provided to members of the regulated
2 group."

3 Do you see that?

4 A. I do.

5 Q. Yes, and that was right, wasn't it? Yes?

6 A. Yes.

7 Q. And under the current structure, if funding was provided
8 by LBHS LP1, this would cause interest income in LBHS
9 LP1 to build up, would give a negative impact on the
10 group's regulatory capital position.

11 You then go on to deal with replacement of funding
12 by LBIE. You say:

13 "Any income accrued in SLP1 in such a scenario would
14 not be permitted to be lent outside of the current UK
15 regulatory chain structure i.e. the structure outlined
16 in appendix 1."

17 That was right, wasn't it?

18 A. Yes.

19 Q. And then if we go forward to the second bullet point,
20 where you say:

21 "As well as the regulatory driver, the new structure
22 provides US tax advantages as described above in section
23 B."

24 So you see that you again refer to the US tax
25 advantages, do you see that?

- 1 A. Yes, I do.
- 2 Q. You then go on to say the use of the two Scottish
3 partnerships provides flexibility from a US tax
4 perspective on any future redemption note 1 and note 2;
5 yes?
- 6 A. Yes.
- 7 Q. And then further down, do you see the next, it is not
8 the next paragraph but the paragraph after that:
9 "As the proposed transaction does not displace or
10 alter the existing amount of debt funding to the UK
11 group, it would seem that no comparison needs to be made
12 here. The same loan amount is in place before and after
13 the transaction and fulfils the same purpose, that of
14 providing capital to support the general UK business
15 activities."
- 16 A. Yes, I see that.
- 17 Q. That was right?
- 18 A. Yes, that was right.
- 19 Q. Then you say the loan was made for the same amount and
20 that was right, wasn't it?
- 21 A. Yes.
- 22 Q. And under the same terms and conditions, and that was
23 right, wasn't it?
- 24 A. Yes.
- 25 Q. "... prior to the insertion of the hybrid entity ... in

1 the absence of the structure involving a hybrid entity,
2 the UK tax deduction would remain the same."

3 And you then talk about an arbitrage opportunity?

4 So can we then go to your interview, please, which
5 is in C -- so that's the letter that you sent to HMRC?

6 A. It was.

7 Q. I then want to pop back, if I may, to your interview at
8 276, and I am just looking at something slightly
9 different which is the intention to transfer. So if we
10 look --

11 A. Sorry I have lost which folder you are looking at.

12 Q. It is in bundle C. I am so sorry, why don't we put the
13 other two bundles back for the moment and clear the
14 decks a little bit. Do you have bundle C?

15 A. I do now, thank you.

16 Q. Excellent, thank you. C/21. You will remember this is
17 the transcript of your interview. I wonder if you could
18 turn to page 13 of the interview, that is 276 and the
19 bottom right-hand corner.

20 A. 276.

21 Q. Yes, I can pick it up, do you see 275 and 276?

22 A. Yes.

23 Q. So if I pick up Mr Lawford's question at the bottom of
24 page 12 at line 33 where he says:

25 "The purpose for having it as a eurobond was a tax

1 purpose rather than because of any intention to transfer
2 it out of the Lehman Group."

3 And you answer at the top of page 13:

4 "To my knowledge there was never an intention to
5 transfer it out of the Lehman Group."

6 And that was right, wasn't it?

7 A. That was right to my knowledge.

8 Q. And further down, on lines 5 and 6, you say:

9 "I would have to think about the tax but that was
10 never contemplated. This was an internal structure."

11 So you are saying that transfer out was never
12 contemplated, this was an internal structure; and that
13 was right as well, wasn't it?

14 A. That was right.

15 Q. If I can then take you back to your witness statement at
16 tab 3 on page 36. Can you see paragraph 33? Where you
17 explain that by treating this Scottish
18 Limited Partnership as a corporation for US tax purposes
19 and making an APB 23 election on it, which is a US
20 accounting concept, to the extent that the Scottish
21 Limited Partnership did not repatriate its profits to
22 the US, the interest income in the Scottish partnership
23 would not be subjected to any current year -- any US
24 tax, current year US tax either.

25 So what you are explaining, as I understand it, is

1 that the Lehman Group had made something called an
2 APB 23 tax election on SLP3, is that right?

3 A. That's correct.

4 Q. And that was for US tax purposes, yes?

5 A. (Nods).

6 Q. Is that right?

7 A. That is correct.

8 Q. And if SLP3 had transferred the LBHI2 sub-notes out of
9 the Lehman Group, then Lehman Group would have lost that
10 tax benefit; that is right as well, isn't it?

11 A. Well, if it transferred it out, and it received interest
12 income on that, it depends what the terms of the
13 transfer was at, but yes, the aim was to make an APB 23
14 election on SLP3, so the income in -- interest income on
15 the quoted eurobond in SLP3 was not subject to tax in
16 the UK or the US.

17 Q. Thank you. And then just flipping forward to
18 paragraph 37. You say that it was important that
19 subordinated debt to be held in the partnership should
20 be in the form of a quoted eurobond, listed in a
21 stock exchange. Then you explain this:

22 "This is because interest paid on such listed
23 instruments would not be subject to UK withholding tax
24 and so the interest could be paid gross."

25 And that is right, isn't it, from a UK tax

- 1 perspective?
- 2 A. Yes. So the interest was -- interest on the eurobond
3 was annual interest, it was being paid by
4 Intermediate 2. If that was paid to a company, that
5 interest was paid to a company who wasn't in the charge
6 to UK corporation tax in respect of that interest, then
7 there would be UK withholding tax on it. One of the
8 exemptions, there is a number of exemptions to get round
9 UK withholding tax, and one of those was to have
10 a quoted eurobond that had to be listed on a recognised
11 exchange.
- 12 Q. Yes, thank you very much. So as far as you were aware,
13 there was no intention that these sub-notes should be
14 traded freely, was there?
- 15 A. Not to my knowledge, no.
- 16 Q. Now can we just have a look, if you don't mind, could
17 you be given bundle F4 again. And if you could find at
18 1894, please, do you see that this is an e-mail that you
19 sent on 30 March at 10.26 and you sent it to
20 Sarah McMorrow, do you see that?
- 21 A. Yes, I do.
- 22 Q. And you see the title, "Quoted bond to be issued by
23 LBHI2"?
- 24 A. Yes.
- 25 Q. Yes. And I just wanted to look at the paragraph that

1 has a sort of mini-heading, "Purchaser Lehman Brothers
2 Holdings PLC"; do you see that?

3 A. I do.

4 Q. And you say:

5 "Initial purchaser will be PLC though eurobond will
6 then be sold all the way up LB corporate chain in
7 satisfaction for outstanding sub-debt. Ultimate holder
8 of eurobond will be Scottish LP 3. Therefore bond needs
9 to be transferable."

10 Do you see that?

11 A. I do.

12 Q. So what you are explaining is that PLC is the initial
13 purchaser, yes?

14 A. Yes.

15 Q. And that it would be transferred internally up
16 to Scottish LP 3?

17 A. It will be transferred up to Delaware and then dropped
18 down to Scottish LP 3; yes.

19 Q. Yes, thank you. And also if the initial purchaser was
20 PLC, there would be a brief moment when PLC held both
21 the sub-debt and the sub-notes?

22 A. Well, I think PLC would have received the -- the quoted
23 eurobond in satisfaction for the debt it was owed by
24 Holdings Intermediate 2, so one should replace the
25 other.

1 Q. Insofar as there was some sub-debt left?

2 A. Yes. If there was a remainder over and above the
3 6.139 billion, then PLC would still have that sub-debt
4 in place.

5 Q. Yes. Can we then move forward to 1895, please. Now,
6 this is an e-mail, do you see, at the top from
7 Sarah McMorrow on 30 March to Mr Miller, and it is
8 copied to you, and the subject matter is "quoted bond to
9 be issued by LBHI2"; do you see that?

10 A. I do.

11 Q. And Ms McMorrow forwards an e-mail from you that we see
12 further down the page, the e-mail we have just looked
13 at, and she forwards it to Mr Miller and Ms McMorrow
14 says:

15 "Stephen, we have another intercompany listed note
16 to do. Jackie has summarised below, but I am sure you
17 will have a number of questions. The issue will be
18 listed on the Channel Islands ... I assume in physical
19 form as well ... I am assuming by transferable Jackie
20 just means it can be transferred between Lehman entities
21 which should be possible with a physical registered
22 name."

23 So you can see what is being passed on by
24 Sarah McMorrow, and that was a correct description,
25 wasn't it?

- 1 A. It was.
- 2 Q. And so probably a cross between UK re-issues and the
3 Holdings plc issues, and then she goes on to deal with
4 some mechanical matters. But this is in effect the
5 instructions to Mr Miller at Allen & Overy being given
6 by Sarah McMorrow, is that right?
- 7 A. Yes, it would appear to be.
- 8 Q. Yes. And again, it's clear that nobody had in mind that
9 the sub-notes would be transferred outside out of the
10 Lehman Group; that's right, isn't it?
- 11 A. That is right.
- 12 Q. And as a physical registered note, it could be
13 transferred internally between different
14 Lehman entities, couldn't it?
- 15 A. I am not really sure on that. I am presuming from this
16 it should be, but that was my legal colleagues to work
17 out which was the best way to have the note.
- 18 Q. Okay. Can we then just have another look at your
19 witness statement, which is in file C at 3. I hope you
20 still have it there?
- 21 A. Yes.
- 22 Q. Paragraphs 54-68, and just to give you a little bit of
23 context. In this part of your witness statement, you
24 are looking at the 2008 amendments to the LBHI2
25 sub-notes, okay?

- 1 A. Yes.
- 2 Q. To give you your reference point. And you can see that
3 you deal with that starting in paragraph 54. Can
4 I start by looking at paragraph 60, please, which is on
5 page 41. You see?
- 6 A. I do.
- 7 Q. You say:
- 8 "I recall that as the amendment was needed for tax
9 reasons, again, I was co-ordinating the amendment
10 project steps."
- 11 And that was right, wasn't it, on --
- 12 A. Yes, tax was asking for a change, so we were -- I was
13 instigating the change to be made.
- 14 Q. You were in charge of the tax team, so it's not
15 surprising?
- 16 A. Well, it is US tax as well, so I wasn't working in
17 isolation from a tax perspective.
- 18 Q. No, of course. And you recall that the amendments were
19 needed for tax reasons, and that is right, isn't it,
20 that is what you say?
- 21 A. That is right.
- 22 Q. Yes, and those were primarily US tax reasons, were they
23 not, is that right?
- 24 A. No, I wouldn't say that actually. The benefit from the
25 structure was US tax.

1 Q. Yes.

2 A. But because of the profitability of the UK group at that
3 time, we weren't going to be able to maximise that US
4 tax benefit.

5 Q. Right?

6 A. And therefore we needed amendments to defer taking the
7 benefit.

8 Q. Yes. So actually you make that very point in
9 paragraph 55 of your statement. If you look at
10 paragraph 55, where you say:

11 "The 2008 amendments permitted the deferral of
12 LBHI2's obligation to settle interest on the LBHI2
13 sub-notes."

14 Yes, so you needed to or you wanted to defer LBHI2's
15 obligation to settle interest on the sub-notes for tax
16 reasons?

17 A. To maximise our tax benefit.

18 Q. Yes, because you say:

19 "... I could recall it was ultimately for US tax
20 reasons ..."

21 You say:

22 "Whilst I could recall it was ultimately for US tax
23 reasons, until I went back through my notebooks for the
24 purposes of these proceedings, I had no clear
25 recollection as to what precisely the tax reason was."

1 And that is right, obviously, if it is in your
2 statement. And in paragraph 56, you explain this,
3 because -- you explain that you have been through your
4 notebooks and you identified the tax driver?

5 A. That's correct.

6 Q. And by settling greater amounts of interest than it
7 received for LBIE, potentially useful tax losses could
8 accrue in LBHI2:

9 "However, in very high level terms such losses were
10 only useful for US tax purposes if Lehman had sufficient
11 current year UK tax profits in certain UK entities to be
12 set off against those losses."

13 A. That's correct.

14 Q. That is an accurate description of the problem?

15 A. That was the crux of the problem.

16 Q. So you needed, just forgive me if I am way too
17 simplistic. You needed to defer the interest payments
18 so that they could be taken at a time when it was
19 advantageous to take those -- the interest payments, is
20 that right?

21 A. Yes, because at this time in 2008, the companies
22 in the UK that were APB 23 companies that were going to
23 use the losses from Intermediate 2 were in a loss
24 themselves. So it wouldn't have been able to use
25 Intermediate 2's losses, so we wouldn't have been able

1 to maximise the US tax benefit.

2 Q. Yes, and you explain that in paragraph 57 where you say
3 that:

4 "In this period, we did not have sufficient UK tax
5 profits in the specific UK group companies, and so
6 the US advantage would be reduced."

7 A. That's correct.

8 Q. And so that is why you wanted to defer the interest
9 obligation; that's right, isn't it?

10 A. That's right.

11 Q. Yes. And if we just flip forward to your interview
12 again, which is in tab 21, could you go to 294, do you
13 have --

14 A. Yes.

15 Q. This is page 31 of the transcript. And Mr Taylor from
16 Sidley Austin asks you:

17 "Okay, you talked about the tax reasons behind the
18 2008 amendment being the deferral."

19 You say:

20 "Yes.

21 "Do you recall whether there were any other reasons
22 for that amendment?"

23 And you said:

24 "Not to my knowledge, no."

25 And that was right, wasn't it?

- 1 A. That was right.
- 2 Q. Yes, you were not aware of there being any other
3 reasons?
- 4 A. No.
- 5 Q. And it -- as far as you were aware, it was the sole
6 commercial purpose for putting the amendments in place?
- 7 A. It was.
- 8 Q. And as far as you were concerned, the only intention you
9 had through all of this was to achieve, to defer -- was
10 to defer interest so you could get the tax benefit, is
11 that right?
- 12 A. Yes. So the two things were I needed to get -- defer
13 the interest to get the tax benefit, and by doing that,
14 we had to amend the notes, but the notes, once amended,
15 still had to meet the regulatory requirements. They
16 still needed to be lower tier 2.
- 17 Q. Thank you. And you didn't intend to change it from
18 lower tier 2, did you?
- 19 A. No, that was the requirement from my regulatory
20 colleagues. They said: you can do this but it still
21 needs to be lower tier 2.
- 22 Q. Yes. Can we just go back to 67 to 68 in your witness
23 statement, please. This is a section in which you deal
24 with the insolvency point, and you say:
25 "As with the position in the 2007 restructuring

1 [which we have talked about], at no time as part of the
2 2008 amendments process did I think about what would
3 happen in the event of an insolvency of Lehman Brothers
4 or LBHI2."

5 And of course that's right, isn't it?

6 A. That's correct.

7 Q. "I didn't have any reason to think about that or about
8 the order in which the LBHI2 sub-notes and sub-debt
9 would be paid in any such insolvency, as it simply
10 wasn't a relevant consideration."

11 And you just explained your thinking about that.

12 But then you say this:

13 "Had Tom Grant or anyone else told me that the
14 amendments did or might mean that the LBHI2 sub-debt
15 would take priority over the LBHI2 sub-notes in the
16 event of an insolvency, it is difficult to say what
17 I would have thought at the time. I would likely have
18 discussed the situation with my legal and regulatory
19 colleagues if I had been made aware of the change."

20 Do you see that?

21 A. I do.

22 Q. So if Tom Grant had said to you: this means that the
23 sub-debt is going to take priority over the sub-notes,
24 or vice versa; what you are saying is that if that had
25 been drawn to your attention, you would have discussed

- 1 it with your legal and regulatory colleagues, is that
2 right?
- 3 A. Yes. It wouldn't have created me a tax problem, but it
4 might have created the other guys in the team, in the
5 other departments, a problem, I don't know.
- 6 Q. And if you had been made aware of that change, you would
7 have discussed it with them, is that right?
- 8 A. I would have hoped to have discussed it with them.
- 9 Q. Yes, so it would have been the sort of -- a change like
10 that would have warranted some discussions, wouldn't it?
- 11 A. Yes, but I can't recall any discussions happening.
- 12 Q. No. What you wouldn't have done is you wouldn't have
13 just signed off without there being any discussions,
14 would you?
- 15 A. I think it is unlikely, but I can't -- I can't
16 recall can't recall.
- 17 Q. And you wouldn't have just signed it off, if Mr Grant
18 had said to you: I am changing all of this; you wouldn't
19 have just signed off on it because Mr Grant had come up
20 with it, would you?
- 21 A. As I say in my statement, I think I would have raised it
22 with my colleagues, who were probably more interested in
23 it than I was.
- 24 Q. And I don't know if you were in court yesterday, but
25 Mr Grant told us that if the amendments had meant that

1 the sub-debt would take priority over the sub-notes, he
2 would have told Ms McMorrow and taken instructions, and
3 that is what he told us yesterday. So he would have --
4 says he would have raised it and you would have
5 discussed it; that's right, isn't it?

6 A. I would hope so, yes.

7 Q. Can we look at F5 -- can you be handed F5, please.

8 A. Sorry, what was the page number?

9 Q. 2574.

10 A. Thank you.

11 Q. 2574. This is an e-mail of 2 June, and it is sent by
12 you to Ms McMorrow, and it is headed, "Question for you
13 re LBHI2 eurobond". And what you say, you say to
14 Ms McMorrow:

15 "Not sure if you can answer the following ..."

16 And you say:

17 "You will recall the eurobond ..."

18 I am shortening that, the first sentence:

19 "... listed on CIX ... under the terms of the note
20 interest is accrued and payable monthly ..."

21 Then you say this:

22 "We would like to continue to accrue interest in
23 2008 before the interest pay down i.e. the cash payment
24 not to be made until late in 2009."

25 So you are describing there the desire that you want

1 to defer the interest payment, is that right?

2 A. That's correct.

3 Q. Yes. And you then say:

4 "As the note is between two Lehman entities, does
5 deferring payment of the interest matter?"

6 You see the question you are asking, which arises
7 out of the fact that it is between two Lehman's
8 entities. And you say:

9 "I note condition 6C of the note states that if
10 interest which falls due is not paid in full, the
11 registrar will annotate the register accordingly. As
12 LBIE is the registrar, do we care ..."

13 And you ask for her views.

14 So what you are asking there is, you know, do we
15 really need to make an amendment? Is it okay because
16 this is internal? That is the question that you raised
17 at that point, is that right?

18 A. Yes, I am asking from -- her view from, you know, she is
19 the legal person.

20 Q. Absolutely. Believe me, there is no criticism involved
21 in those questions. And then 2575, we can see we get
22 the response from Ms McMorrow, or she forwards your
23 e-mail and copies you, and she forwards it to Allen &
24 Overy and says:

25 "Daniel, please see below. Could SLP3 as holder

1 just sign a waiver letter without changing the terms and
2 conditions? If the terms and conditions were not
3 changed, presumably this would be something that would
4 need to be advised to the CISX."

5 So you see, what she is asking at the moment is: can
6 we deal with the deferral of interest by just a waiver
7 letter? That's right, I am not misunderstanding, yes?

8 A. Yes, I mean, that is legal terms that I -- you might be
9 more familiar with than me, but that is what it
10 suggests.

11 Q. So can I just then turn to your interview, which is in
12 21, in tab C. If we can look at page 281. It is
13 page 18, and I wanted just to look at lines 21 and
14 following, and you will see that Mr Lawford says:

15 "On 2 June Sarah McMorrore forwarded your e-mail to
16 Daniel Fletcher ..."

17 So he is talking about that e-mail.

18 "Do you recall anyone ... within Lehman discussing
19 or giving instructions to A&O to change the extent of
20 the subordination or quantum payable?"

21 And you say no, and that's right, isn't it?

22 A. That is right.

23 Q. And he then says:

24 "So is it fair to say that the sole instruction
25 would have been to permit the deferral of interest?"

1 And you say:

2 "From me, yes."

3 And that was right, wasn't it?

4 A. Yes.

5 Q. And you said:

6 "I wasn't aware that anyone else was directing A&O

7 to change anything else."

8 And that was right as wellwasn't it?

9 A. That's correct.

10 Q. So what we can see is that the purpose of the

11 transaction was to defer the interest, that's right?

12 A. Yes.

13 Q. We see that there was a discussion as to whether or not

14 this needed to go as far as amending the terms and

15 conditions, or whether there could be some other

16 mechanism like a waiver, yes?

17 A. Yes.

18 Q. And as far as you are aware, there was no-one else

19 directing Allen & Overy in relation to this matter at

20 that time, and that is what you tell us and that was

21 right?

22 A. I think Sarah McMorrow would have been their main point

23 of contact, and I don't think there was anyone else.

24 Q. And the reason for all of that was that the sole purpose

25 of the transaction was to secure this tax benefit by

1 deferring the interest?

2 A. From my perspective, yes.

3 Q. Now, could you be handed bundle F5 again, please.

4 I hope you still have it. If we could go forward to
5 2607, do you have that? This is an e-mail from Mr Grant
6 to Ms McMorrow, and the heading is "Amendment of LBHI2
7 notes". And he starts by giving the Law Society
8 requirements, where he explains that Anne-Claude Mozel
9 was going to have overall responsibility. He then
10 identifies a fixed fee of £2,500 plus VAT and
11 disbursements for the transaction. Do you see that?

12 A. I do.

13 Q. And that he then goes on to say:

14 "Please see attached amended conditions together
15 with an amended certificate. I'll have these blessed by
16 Amrit over the next day or so. Please let me know if
17 you have any comments."

18 And then "finally, the conditions specify" -- do you
19 see the "finally" paragraph:

20 "... conditions specify you need FSA written consent
21 to make any change. As discussed yesterday, you will
22 take care of this. You will need to include in the
23 notice confirmation ... the opinion we delivered on
24 1 May 2007 continues in full force and effect after the
25 proposed amendment. We are happy for you to make this

1 confirmation."

2 So Mr Grant confirms to Ms McMorrow, and I am not
3 suggesting you are a party to this e-mail, but you can
4 see Mr Grant confirms that Allen & Overy were happy to
5 continue the confirmation that they had already given.

6 So can we just have a look at the first draft, which
7 I have got at 2609. Again, you will be pleased to know
8 I am not going to ask you to actually construe them, but
9 if you look at 2612, or in fact if you look at 2611, you
10 can see the heading, "Interest", and you see that what
11 has been done is subject to condition 4F, and then we
12 can see over the page at F, and there is a provision
13 dealing with interest. And if you look at clause 3 on
14 2611, so you can see there is an amendment to the
15 interest provision, and you look at clause 3, you can
16 see there were no changes to 3A at all. Do you see
17 that?

18 A. I can, yes.

19 Q. And then if we go forward to 2676, so if you look at the
20 top, Ms McMorrow to Tom Grant copied to you and to
21 Mr Bowen, do you see that?

22 A. I do.

23 Q. And this is about those amendments. And she says:

24 "That is fine. We don't need any opinion ..."

25 And he is talking then about their continuing --

1 confirming their opinion, and then says:

2 "We don't have any comments other than the holder on
3 the resolution, so if you can send a revised version..."

4 And so on.

5 So "we don't have any comments". So "we don't have
6 any comments" at that stage would be Sarah McMorrow, the
7 regulatory team, you, on the tax front, so you didn't
8 have any concerns about the lack of an amendment to
9 clause 3?

10 A. No.

11 Q. And then if we go to 2689, do you see that this is an
12 e-mail from Mr Grant to Mr Bowen and Ms McMorrow, and
13 again copied to you, and it is sent on 11 June?

14 A. I do.

15 Q. And it says:

16 "GENPRU just says that when you give notice to the
17 FSA of the change, you include confirmation that our
18 opinion will remain in force after the proposed
19 amendment."

20 And he then deals with some practical matters, the
21 name of the holder, and the resolutions. Do you see
22 that?

23 A. Yes.

24 Q. And then if we go to 2819, we see an e-mail from
25 Mr Grant on 12 June, do you see up at the top?

1 A. Yes.

2 Q. And that e-mail is to you, to Mr Dave --

3 A. That is actually Parul Dave.

4 Q. Ms Dave, I am so sorry, I am so sorry?

5 A. That's all right.

6 Q. To Emily Upton and to Sarah McMorrow, and then to

7 Anne-Claude Mozel at Allen & Overy, and Sophie Tomlinson

8 at Allen & Overy. This is amendment of the LBH

9 Intermediate 2 Limited notes. You can see that what

10 Mr Grant attached was the draft business board minutes,

11 you see that, a board minute for the general partner of

12 SLP and a short note on corporate benefit.

13 Do you know whether or not this and its contents

14 went to anyone else?

15 A. I -- I wouldn't know.

16 Q. So you are not aware of it having gone to anyone else

17 internally at Lehmans?

18 A. I -- I couldn't recall.

19 Q. Thank you. If we can just look at the memorandum which

20 is 2837. Do you see, this is a memorandum, it is

21 written to Ms McMorrow, it is written by Mr Grant, it is

22 dated 12 June 2008. And the subject matter is: Lehman

23 Brothers Holdings, Scottish LP corporate benefit. Do

24 you see that?

25 A. I do.

1 Q. And so this was attached to the e-mail that you have
2 just seen. Do you remember reading it at the time?

3 A. Yes, I do.

4 Q. Thank you. And it says:

5 "You have asked us to provide you a short note on
6 certain corporate benefit aspects of the proposed
7 amendment of the floating rate subordinated notes issued
8 on 1 May ..." and so on.

9 And then it says:

10 "As the amendment involves changing the terms and
11 conditions of the notes to allow the issuer to defer
12 payment of interest on the notes at its discretion, the
13 issuer and the sole holder of the notes, Lehman Brothers
14 Scottish LP, will approve the amendment via written
15 resolution."

16 That accorded with your understanding, is that
17 right?

18 A. Yes.

19 Q. Then he goes on to consider corporate benefit. He talks
20 about section 172 of the Companies Act and identifies
21 a number of factors, do you see that?

22 A. Yes.

23 Q. And then over the page he says:

24 "The question that must be asked is whether the
25 board of directors of the general partner properly

1 considered the interests of the noteholder rather than
2 those of its ultimate parent or sister companies."

3 So you see that what it is saying is that the
4 general partner has to consider the interest of the
5 noteholder, do you see that?

6 A. Yes.

7 Q. And he says:

8 "Where the directors are common to both companies,
9 the problem becomes acute. The court will look at the
10 circumstances ... of the directors at the time. The
11 resolution was passed to assess whether it was given for
12 the benefit of the company."

13 Okay. So the company is the noteholder and that is
14 SLP3; is that right?

15 A. Yes.

16 Q. And there had been quite a lot of discussion about the
17 need for this memorandum about corporate benefit, that's
18 right, hadn'tn't there, asking for it; you wanted it?

19 A. From memory, I don't think it was a point I raised,
20 I think it was my legal colleague, Parul Dave, had
21 raised the issue. So she was kind of running with that
22 and getting herself comfortable on it. I was on the
23 periphery.

24 Q. And this was -- it is quite an important point, isn't
25 it? And the type of questions the directors may need to

1 consider is -- in balancing the advantages to the
2 company against the risk of entering into such
3 arrangement are: talks about the relationship between
4 the two companies, is the relationship between the two
5 companies -- and that is LBHI2 and SLP3, is that right?

6 A. Yes.

7 Q. -- sufficiently valuable to justify the amendment? What
8 advantages do or may the noteholders, that is SLP3, gain
9 from the amendment being made; do you see that?

10 A. Yes.

11 Q. And if the interest payments are deferred, can the
12 noteholder meet its obligations and still remain
13 solvent?

14 In relation to the bullet point in the middle, this
15 is the advantages to SLP3. If the amendments made the
16 sub-notes junior to the sub-debt, that would have
17 affected the advantages to the noteholder, wouldn't it,
18 because that would have been to the disadvantage of
19 SLP3; do you follow?

20 A. In an insolvency, you mean?

21 Q. Yes, well, it is a -- it is a disadvantage, obviously in
22 an insolvency, I quite understand that, but it is
23 a disadvantage. So it is something SLP3 following this
24 advice would need to have considered, is that right? Do
25 you follow?

- 1 A. You would have thought so, yes.
- 2 Q. Yes, and so you would expect Mr Grant to have pointed
3 out to the readers of this corporate benefit memorandum,
4 that when they consider the benefits or the
5 disadvantages, that they should have regard to the fact
6 that the ranking was being changed; do you follow?
- 7 A. Yes.
- 8 Q. And of course we don't see that in here, do we?
- 9 A. No.
- 10 Q. So can we just go on then to 283 -- 2839 which is on the
11 next page. Do you see that, Mr Grant, this is an e-mail
12 from Mr Grant, to you, on 12 June at 11.27. It is to
13 you and to Ms Dave and copied to Emily Upton,
14 Sarah McMorrow, Anne-Claude Mozel and Sophie Tomlinson
15 again, and it is reamendment of LBHI2 notes.
- 16 And again, this attaches the amended conditions for
17 the FSA, a comparison showing the changes to the last
18 draft you saw. While we are mentioning, once I have got
19 Ms Dave's name correct, she, as I understand it, was on
20 the corporate counsel team; that's right, isn't it?
- 21 A. That's correct.
- 22 Q. Thank you. And Emily Upton was the legal counsel in the
23 corporate advisory team, is that right?
- 24 A. No, both Parul and Emily were in the same team.
- 25 Q. In the same team?

- 1 A. Yes.
- 2 Q. So that is the corporate counsel team. And we see he
3 sends a second draft, and then he says here -- so he
4 sends a draft which shows the changes, and he says
5 "deferral provisions" -- so that is deferral of the
6 interest, is that right?
- 7 A. That's right.
- 8 Q. "Deferral provisions introduce tax sensitivities. The
9 amendments are designed to ensure these sensitivities
10 are met."
- 11 Do you see that?
- 12 A. I do.
- 13 Q. So what you were being told by Mr Grant is that the
14 deferral provisions, which is what you had asked him to
15 do, created some tax sensitivities, and so he was -- he
16 put in some amendments designed to meet those tax
17 sensitivities, is that right?
- 18 A. Yes, that is what that suggests, yes.
- 19 Q. And in your statement, if you have got bundle C, at
20 tab 3, again, page 42, paragraph 64, what you say is
21 that you think it is likely that you would have reviewed
22 the amended conditions at the time, and would have
23 approved them as part of the process by which they came
24 to be executed. You say you don't recall any
25 conversations about the amendments to condition 3, and

1 that is -- is that right?

2 A. Yes, the fact that the wording is tax sensitivities, it
3 would have been very remiss of me not to pick up on the
4 word tax, and have a look at the amendments he had made
5 to address those tax sensitivities, so ... but I can't
6 recall speaking to anyone about them. It is just too
7 long ago.

8 Q. Yes, and you say in paragraph 66, to make it absolutely
9 clear:

10 "Looking back at these documents now, I am slightly
11 surprised I didn't pick up on the tax sensitivities
12 language in Mr Grant's e-mail and ask Mr Grant to
13 explain what tax sensitivities he was referring to."

14 Do you see that?

15 A. Yes.

16 Q. Because whether or not you noticed them at the time, and
17 whether or not you noticed them at the time, there is no
18 evidence, is there, that you engaged on the tax
19 sensitivities, so called?

20 A. No evidence I could find, no.

21 Q. And you didn't connect the tax sensitivities to the
22 amendments to condition 3A, did you?

23 A. Sorry, remind me what condition 3A is.

24 Q. Of course. If you would like to go back to bundle F5,
25 and if we look at 2849, this is the version that

1 Mr Grant sent to you, and you can see that we get a lot
2 of underlining, a lot of amendments, and the new part of
3 it turns up from the words, "the conditionality referred
4 to".

5 So that was those amendments, and you didn't connect
6 those amendments to 3A to whatever the tax sensitivities
7 were supposed to be?

8 A. I can't confirm or deny. That was just too long ago.

9 Q. Yes, and one of the reasons why you are slightly
10 surprised is because, as you have absolutely rightly
11 told us, the amendments were tax driven, and you are the
12 tax person co-ordinating the amendment project steps,
13 yes, so it is slightly surprising that when you get an
14 e-mail that refers to tax sensitivities, or put it this
15 way, it is slightly surprising, you are slightly
16 surprised that when you see something that refers to tax
17 sensitivities, that you didn't pick up and run with
18 that; is that what you are telling us?

19 A. I can't remember. You know if I get a document, it's
20 got amendments in, I am going to look at the amendments,
21 but if it didn't really impact me from a tax
22 perspective, you know, I am not sure I would have taken
23 them any further.

24 Q. Yes. Can we put away F5 for a moment and flip forward
25 into F6. If we could go to page 3060, please. What you

1 can see here is an e-mail from you to Claire Edwards and
2 Gareth Bowen, and you are referring to the LBHI2 bond,
3 deferral of interest payments is the heading that you
4 give it. Do you see that?

5 A. Yes.

6 Q. And this one is on 23 June and you say:

7 "Claire, further to our discussion this morning
8 I attach the A&O reg ..."

9 Is "reg" for regulatory?

10 A. Yes, correct.

11 Q. "... reg opinion dated 1 May confirming that the quoted
12 eurobond is LT2. Secondly, the OC ..."

13 A. Offering circular.

14 Q. Offering circular, am I right about that? Yes.

15 "... dated 26 April and thirdly a letter of A&O
16 dated 17 June, confirming that if the terms of the
17 quoted eurobond are amended to allow deferral of the
18 cash payment ... their first opinion still stands."

19 So you are there describing what you understand you
20 have got in your pack, do you see that?

21 A. Yes.

22 Q. Is that right?

23 A. Yes.

24 Q. And if we could just go to 3006, this is the A&O opinion
25 of 17 June which you have just sent on, and can you see

1 that what Allen & Overy write here, and you will see
2 that it is addressed for your attention, top left-hand
3 side, you see that?

4 A. Yes.

5 Q. They refer to the notes, and they say in the second
6 paragraph:

7 "At the time of the issue of the notes, you asked us
8 to confirm whether the notes would qualify for inclusion
9 as lower tier 2 capital resources under GENPRU published
10 by the FSA. We provided this confirmation in a letter
11 to you of 1 May 2007."

12 So they refer to their first letter in which they
13 had given an opinion for GENPRU purposes that it
14 qualified as lower tier 2 capital. They then say:

15 "You intend to procure an amendment to the
16 conditions to allow the issuer to defer payment on the
17 notes."

18 Do you see that?

19 A. Yes.

20 Q. And that accorded with your understanding, that's right,
21 isn't it?

22 A. Yes.

23 Q. They then attach as appendix 1 the conditions, and they
24 then say:

25 "On the basis of the foregoing, we confirm that the

1 confirmations provided in the original letter will
2 continue in full force and effect in relation to the
3 notes after the amendment."

4 What we can see from this is that they record that
5 the -- what was intended was to procure an amendment of
6 the conditions to allow the issuer to defer payment on
7 the notes, so that records the nature of the amendment,
8 and that is what you understood, wasn't it?

9 A. It was.

10 Q. And we don't see any other purpose for these amendments
11 in this letter, do we?

12 A. Doesn't appear to be, no.

13 Q. And the reason for that is, as you have explained, is
14 that all you intended was that the interest should be
15 deferred or could be deferred to achieve the tax benefit
16 that you very helpfully described, and that's right,
17 isn't it?

18 A. Yes.

19 Q. And then they say on the basis of the foregoing, they
20 confirm their confirmations in the original letter, and
21 that was required by GENPRU, yes?

22 A. Yes.

23 Q. And you saw that confirmation at the time, that the
24 intention, that the deferral of interest did not affect
25 their confirmation that it ranked as LT2. Is that

1 right?

2 A. That's correct.

3 Q. Can I then just move on. Can we go back to your witness
4 statement and to a section that you describe as
5 corporate governance, please. Do you have C3 in your
6 witness statement?

7 A. Yes, I do.

8 Q. Excellent, thank you. Page 43, and the section starts
9 at paragraph 69. And it runs through to paragraph 72.

10 A. Yes.

11 Q. What you are doing is you are describing corporate
12 governance at Lehmans, and I just wanted to pick up
13 paragraph 72 where you say:

14 "Whilst the company directors engaged with the
15 matters which were to be dealt with at any particular
16 board meeting, and would sometimes ask questions, my
17 experience was that the directors usually trusted the
18 expert members of the team who had worked on or were
19 bringing forward the initiative to be taken."

20 So what you are describing is that the board members
21 at a particular board meeting would sometimes ask
22 questions, but you explained that in your experience,
23 they usually trusted the expert members of the team who
24 had been working on the job in question, is that right?

25 A. That is what my statement says, yes.

1 Q. And that's right, isn't it?

2 A. Yes.

3 Q. So they wouldn't -- you actually say further down:

4 "They would not typically seek to investigate or
5 second-guess the proposed initiative to be taken."

6 And that is right as well, isn't it?

7 A. Yes, because initiative would have gone through various
8 levels of hierarchy and sign-off before it was
9 ultimately signed off by the board.

10 Q. Yes.

11 A. So quite a lot of due diligence had been undertaken
12 before it got to the board.

13 Q. That is what you say. You say:

14 "It was recognised that the proposal had been
15 considered and signed off by the relevant teams with
16 particular expertise ... responsible for whatever the
17 initiative was."

18 So what we see from this, in relation to the general
19 processes from your evidence, is that the directors, the
20 individuals who were directors of the various Lehmans'
21 companies, and of course there were a lot of them, they
22 trusted the expert members of the teams who were putting
23 things up to them; that's right, isn't it?

24 A. Yes.

25 Q. Yes. And they wouldn't second-guess the team, the

- 1 expert teams, would they?
- 2 A. No. You know, they would sometimes ask questions or
3 maybe you get a phone call, or asked to attend a board
4 meeting, just to explain something, if they didn't
5 understand it. It depended who the directors sitting at
6 the board meeting were, so, for instance, in my case, if
7 Anthony Rush was there, he would already be fully aware
8 of the tax consequences because, you know, he was my
9 boss and I would have been briefing him on a regular
10 basis around the structure so ...
- 11 Q. He would have known all about what it was you were
12 trying to do?
- 13 A. He would. I mean, normally, if the tax structure went
14 to be signed off by the board of directors, Anthony
15 would be at the board meeting, so he would be able to
16 answer any questions.
- 17 Q. Yes. What we see is a strong element of reliance by the
18 directors on the expert teams; that's right, isn't it?
- 19 A. Yes, that was kind of the norm at Lehman.
- 20 Q. Yes, and I think you have told us that the teams would
21 consider the different elements of the transaction, so
22 you are focusing on the elements that you have
23 described, so people would focus on the different
24 elements of the transaction. That's right?
- 25 A. That's right.

1 Q. And you would come up with -- you would make the
2 relevant decisions about what the structure should look
3 like, and between you, make the relevant decisions about
4 what the structure would look like, what the terms
5 needed to be to achieve what you wanted to achieve, and
6 that is how it workedwasn't it?

7 A. That sounds quite simplistic. You know, this -- many
8 months of work, you know, presentation to oversight
9 committees, various levels of management had to sign off
10 on it, so it is just not me working in isolation. There
11 would have been a whole team this side of the ocean and
12 the other side, working out what worked from a tax
13 perspective, a regulatory perspective, a legal
14 perspective and a compliance perspective, and a GAAP
15 perspective actually. So it was ...

16 Q. And then by the time it goes up to the board, when the
17 board meeting, whoever that may be, a couple of people,
18 we are going to look at that in a minute, they know that
19 you have looked at what it is you are intending to do
20 and how to achieve it, and they trust you?

21 A. Yes, they might ask questions, so, for instance, we have
22 spoken about Parul Dave and the -- you know, why
23 companies might enter into this transaction, corporate
24 benefit. She would have briefed Ian Jameson who was her
25 boss, he was corporate counsel. He might have asked

1 questions: have you looked into this, where are you
2 coming out; as Anthony did with me on a tax perspective.

3 Q. Yes so let's have a look at the 2008 amendments
4 themselves. Can we start, I am afraid we need to go
5 back to F5.

6 A. Okay.

7 Q. And I want to look at page 2682. Do you have that?

8 A. Yes, I do.

9 Q. Thank you. You can see that this is an e-mail that you
10 sent on 11 June to Mr Bowen, Sarah McMorro,
11 Emily Upton, Parul Dave and again it is amendment of the
12 LBHI2 notes. You say:

13 "We are looking to amend the terms of the qualifying
14 eurobond issued by ... currently held by SLP3 ..."

15 Then you explain the purpose. Then you say this:

16 "My view is that the board of both companies, or the
17 GP in the case of SLP3, should have a quick board
18 meeting to ratify this. Thoughts?"

19 So we can see from this that you thought, given the
20 structure and how your thinking and your intention would
21 go up to the board, that they would just need a quick
22 board meeting to ratify what the expert teams had come
23 up with, is that right?

24 A. I think the focus is on the word "quick".

25 Q. Yes.

1 A. I might view that slightly differently. I was saying
2 this is a significant change, you know, it is
3 6.1 billion of debt. It is significant enough for there
4 to be a board meeting for the directors to approve it.
5 Now, albeit that board meeting might be a quick board
6 meeting, but it was a significant event that it should
7 go to board level, we shouldn't approve it at our level,
8 we should take it up to the directors.

9 Q. Okay. You can see you have in mind a quick board
10 meeting; what you mean by that, you don't mean next
11 week, you mean quick in terms of length of time?

12 A. I don't know what I meant when I used the word "quick".

13 Q. Just checking. And then you go on to say as an aside:
14 "We may need to get another authorised signatory for
15 Delaware."

16 And Delaware was a reference to Lehman Brothers
17 Delaware Inc, is that right?

18 A. Yes, from memory, I think Delaware was the general
19 partner of the partnership.

20 Q. SLP2?

21 A. Yes.

22 Q. Yes, because LBDI was the sole general partner of SLP2,
23 SLP2 was the sole general partner of SLP3, and so the
24 board of LBDI, which was the Delaware company, was going
25 to be part of the approval process; that accords with

- 1 your understanding?
- 2 A. Yes, and Tony Taranto was co-head of tax at one point,
3 and I knew he had left the firm, so I didn't know who
4 the -- I knew he was the signatory for Delaware, but
5 I don't know who had replaced him.
- 6 Q. You have mentioned Tony Rush. I just want to look at,
7 if you can pick up F6/3201.
- 8 A. Yes.
- 9 Q. This is an exchange between you and Mr Rush, so I will
10 start at the bottom. 22 July, it talks about losses and
11 he says:
- 12 "Can you update me as to where things stand in
13 relation to the loss refreshment trades. Can you remind
14 me of the dollar amount re the SLP3 interest? Also,
15 where are things in relation to the Deloitte idea?"
- 16 What was the Deloitte idea?
- 17 A. Well, loss refreshment trades is nothing to do with what
18 we are discussing in court. It is another tax
19 initiative, and we were using different advisers to
20 devise new tax initiatives. Deloitte must have been one
21 of the advisers we had pulled in and got quite excited
22 about their idea.
- 23 Q. So this is a general --
- 24 A. Yes, it is a general catch-up, yes.
- 25 Q. -- catch-up request. Then what is important is your

1 response, where you say:

2 "We have put in place the deferral of the
3 [Intermediate] ... 2 interest ..."

4 I assume the "int" is Intermediate 2, is it?

5 A. Yes.

6 Q. "... which we have the flexibility of turning off in
7 2008 if required."

8 So that is you keeping him up to date on the
9 interest deferral proposal, or the interest deferral
10 that we have been discussing, is that right?

11 A. Yes, I mean, I wouldn't have been just updating him by
12 an e-mail. He sat in the office next to me, so we spoke
13 a lot, so it wasn't just this, but yes, this e-mail
14 supports the fact that I was updating him on a regular
15 basis.

16 Q. So you would go into his office sort of regularly, you
17 are saying?

18 A. Yes.

19 Q. Which makes perfect sense, he is immediately above you,
20 is that right?

21 A. Yes.

22 Q. So you go into his office and so he knows what you are
23 trying to do, yes?

24 A. Yes, because he has already signed off for me to
25 continue with it.

1 Q. So you had already explained to him that what you were
2 trying to do was to defer this interest presumably --
3 that's right, isn't it?

4 A. Yes.

5 Q. And you will have explained to him that you were doing
6 that because you could get this tax advantage, so he
7 knew exactly what it was that you were intending to do
8 with this interest deferral?

9 A. That's right.

10 Q. Is that right?

11 A. Yes, that is right.

12 Q. And just to have some idea of the two of you sort of
13 working together, and picking up on something you said
14 earlier as well. Can you just get F4, please, and have
15 a look at 2085, please. Do you see that?

16 A. Yes.

17 Q. This is the PLC board meeting, 20 April 2007. That is
18 the board meeting that approves the initial creation of
19 the sub-notes, do you see that?

20 A. Yes. Can I just have a minute just to have a quick --

21 Q. No, please do. (Pause)

22 A. Yes, that was to approve the notes, yes.

23 Q. Sorry?

24 A. Yes, that was to approve the notes.

25 Q. Absolutely. We can see that Mr Rush was present at the

1 top, and then you were in attendance with Emily Upton?

2 A. Yes, I can't remember being in attendance, but Emily
3 wouldn't have put that down unless I was in attendance,
4 that is right.

5 Q. No, absolutely. So we can see part of the working
6 relationship between you and Mr Rush, and I think you
7 have told us, you reported directly to him?

8 A. I did, yes.

9 Q. Can we then go back to F6. So we were looking at
10 F6/3201 and that was where you said you put in place the
11 deferral. Then, 3202, Mr Rush comes back and says:

12 "Thanks, Jackie. Can you remind me what the
13 interest deferral run rate is?"

14 He is there saying "Can you remind me?" because you
15 had already discussed it in the past, presumably?

16 A. Yes, we would have discussed it and, you know, he wasn't
17 just working on this. He had many other things, so he
18 probably forgot.

19 Q. No, absolutely. Over the page, 3202, you respond to
20 that and you say:

21 "Likely we will defer around 120 million of interest
22 July to November so six months at 20 million a month."

23 Can you just explain to someone as simple as me what
24 it is you are describing as a benefit there?

25 A. Yes. So let me just have a -- refresh my memory.

1 So this would have been in that period June to
2 November 2008, Lehmans was on a November year end, so
3 that is why November is relevant.

4 Q. Ah, thank you.

5 A. So for those six months, for the remaining part of the
6 2008 financial year, Intermediate 2 would have been
7 accruing interest expense at 20 million per month. So
8 six months; that is 120 million. But because we were
9 deferring it we weren't crystallising 120 million UK tax
10 loss.

11 Q. And that was the benefit of what you had been doing?

12 A. Yes.

13 MR PHILLIPS: And Mr Rush says "Thanks!" We can see that
14 just above. Sorry, forgive me a moment.

15 My Lord, I am reminded, I do apologise. If that was
16 a convenient moment and be --

17 MR JUSTICE SMITH: Yes, indeed. We will rise for five
18 minutes.

19 (2.58 pm)

20 (A short break)

21 (3.05 pm)

22 MR JUSTICE SMITH: Mr Phillips.

23 MR PHILLIPS: Ms Dolby, we had a look, if you can just look
24 back at 3201, just a couple of pages back. You see
25 22 July 2008, do you see that?

1 A. Yes.

2 Q. Just to remind you. And you will see that what you say
3 is:
4 "We have put in place the deferral of the interest."
5 Do you see the language?
6 A. Yes.

7 Q. "We have put in place..." Is that because as far as you
8 were concerned, you had put it in place?
9 A. I can't -- I can't remember.

10 Q. So at that point it was something of a fait accompli;
11 something had been done, is that right?
12 A. I am not sure. If we can just turn to when he asked for
13 the amounts June to November.
14 Q. Yes, he asked for that on 22 July.
15 A. Yes. So the suggestion would be it was implemented, so
16 that would impact the accounts in the June months.

17 Q. Right. So as far as you and he were concerned by this
18 stage it was actioned, is that fair?
19 A. I don't know where I have said we have put in place.
20 I don't know, had the board minute -- meeting happened
21 at that time? I don't know.

22 Q. We will come to that in a minute. What I am trying to
23 understand is your and his understanding because we have
24 this set of e-mails here and you start off by saying,
25 "We have put this in place" and he says, "What's our

1 saving?" And you say for the quarter up to November,
2 the June to November?

3 A. Yes. So that suggests to me that it was implemented so
4 it impacted the general ledger in June.

5 Q. Yes. So what you are saying is, as far as you were
6 concerned, it impacted the general ledger in June
7 through to November?

8 A. Yes.

9 Q. So if there were any legal formalities after that, as
10 far as you were concerned, this decision had already
11 been made, is that right?

12 A. Yes, potentially.

13 Q. Yes. And let me, just for completeness, show you
14 bundle E, tab 5. This is the written resolution -- I am
15 so sorry. This is the written resolution. So you see
16 it is a written resolution and it was signed on
17 3 September which of course is after you and Mr Rush
18 have had this exchange and Mr Rush is one of the
19 signatories?

20 A. Mmm mm.

21 Q. Yes. And the reality is as far as you and Mr Rush were
22 concerned, that this is just a legal formality that
23 needed to be signed off in order to give effect to what
24 had already been decided. That is the reality, isn't
25 it?

- 1 A. Except I don't know categorically. Although I -- if we
2 go back to the other document in file F.
- 3 Q. Which other document are you looking for?
- 4 A. So F6/3203, where I say June to November.
- 5 Q. Yes.
- 6 A. I can't categorically say that that happened in June.
7 I mean, that is what I have said in that e-mail but that
8 doesn't necessarily mean it happened in June. It could
9 have been deferred. I don't know. I can't confirm that
10 either way.
- 11 Q. So what you are saying is you don't know categorically
12 if the accounting treatment had been put in in the June
13 to November period?
- 14 A. Whether it had been executed at that time, I couldn't
15 confirm.
- 16 Q. You are talking about the accounting treatment of what
17 you were doing?
- 18 A. I am talking about the benefit that we got, I am saying
19 it is June to November. I am not sure whether it was
20 actually implemented in the general ledger in June.
- 21 Q. You don't know whether you got the benefit at that
22 point, is that what you are telling me?
- 23 A. Yes, it just seems a bit odd that the board meeting
24 happened in September and we are exchanging e-mails
25 in July saying it has happened because you would expect

- 1 the board to sign off on it at the time.
- 2 Q. Yes. But there are really two things going on here,
3 aren't there? There is a sort of what I would describe
4 as the legal formalities, this written resolution, yes?
- 5 A. Yes.
- 6 Q. You follow me? And there are the discussions between
7 you and Mr Rush that result in him and you understanding
8 that you were putting in place a structure to defer the
9 interest, yes?
- 10 A. That's right.
- 11 Q. You and he had had those discussions and then we see in
12 22 July, subject to any legal niceties, as far as you
13 two were concerned that was implemented, that was in
14 place, is that right?
- 15 A. I am saying I can't tell you whether it was implemented
16 in July. I can't confirm that either way, I wouldn't
17 know.
- 18 Q. But the two of you had had sufficient discussions that
19 you were able to say "we have put in place". Whether
20 "we have put in place" was accurate legally because that
21 formality needed to be done, as far as the two of you
22 were concerned the substantive discussions about what
23 you were doing they had taken place, hadn't they?
- 24 A. We would have been discussing it all through that first
25 six months in 2008, you know, up to -- back to June.

1 Q. Yes, and by the time you get to July, you are saying:
2 Look, we have put it in place and this is the saving.
3 Whether or not there are legal niceties to tick off,
4 that didn't make any difference to what you were telling
5 him, did it?

6 A. Well, sorry, your Honour, but my concern is if you go
7 back to the document where I quote how much per month,
8 it says "likely we will defer around" it doesn't say we
9 have deferred.

10 Q. Can we just have a look at the terms of your e-mail.
11 Have you got 3201 there? Do you see in 3201 you say --
12 well, first of all "We have put in place" and you say,
13 "We have the flexibility of turning off in 2008 if
14 required."

15 So you are describing something that has happened,
16 yes? You see that?

17 A. Yes. As I say my concern is on 3203 I have said "likely
18 we will defer."

19 Q. Yes. But that is the mechanics of whether or not you
20 are claiming the benefit that you have all been
21 discussing. But what you are telling him, I am
22 suggesting to you, in 3201, is you are telling him that
23 the ability to do what you are describing and claiming
24 that six months is all in place, the discussions that
25 you have been having have come to fruition to a point

1 where you can say "We have put this in place", do you
2 follow me?

3 A. Yes. There is inconsistent language in that -- that
4 e-mail.

5 Q. Yes, but do you follow what I am suggesting which is
6 there are two parts to this: one is the decision to put
7 this in place, okay. You make a decision that you are
8 going to put in place the deferral of interest for the
9 tax benefits that we have been discussing, do you follow
10 that? And then you have got a second question, which
11 is, as a matter of formalities, legal formalities when
12 did that happen.

13 And the point that I am just testing you on, but
14 I just want to understand, is it looks to me, and
15 I would respectfully suggest, that as far as you and
16 Mr Rush were concerned this had already been put in
17 place. Had been put in place. Not necessarily all the
18 legal formalities but as far as of the decision-making
19 process. Do you follow?

20 A. Yes. It just seems odd to me that that is a July e-mail
21 and the board minute didn't happen until September '08.
22 From my recollection, it was kind of all done at the
23 same time. That's -- that's all I can say on that
24 matter.

25 Q. No, no, I fully understand. We are looking at this

1 written resolution; that is something formal. A formal
2 piece of paper needed to be passed. And what you are
3 saying is that as far as you were concerned in July,
4 when you sent this, you would have thought that had been
5 done?

6 A. We have put -- I guess it's -- I can't remember that
7 terminology, "We have put in place", whether we are
8 taking actions in order to execute it. It would be very
9 unusual for the legal department to hold a board meeting
10 about a transaction, what, six weeks after the
11 transaction had taken place. That seems very odd to me.

12 Q. Yes. Let's move on to 3325.

13 A. 3325.

14 Q. Yes, please. In F6, I should have said; actually,
15 looking at it, you have an awful lot of files there.
16 I am very sorry, I am very bad at clearing away the
17 files when we have finished looking at them. Okay?

18 A. Yes.

19 Q. So you see, this is the minutes of a board meeting of
20 LBHI2 on 28 August, and we see Mr Rush is in the chair,
21 sitting with Mr Jameson.

22 A. I do.

23 Q. Sorry?

24 A. Yes.

25 Q. And we look at the business of the meeting, and the

1 chairman reported the purpose of the meeting was to
2 consider and approve the proposed amendments to the
3 sub-notes by the company:

4 "The purpose of the amendment was to allow the
5 company to defer cash settlement of the interest on the
6 notes at its discretion."

7 Do you see that?

8 A. Yes.

9 Q. And that is exactly what Mr Rush would have expected,
10 isn't it?

11 A. Yes, based on discussions I would have had with him into
12 the run-up to that meeting.

13 Q. Yes, exactly. And there is no reference to any other
14 purpose, do you see that?

15 A. Doesn't seem to be, no.

16 Q. No. And by the time we get to this stage, Mr Rush will
17 have shared your views about the purpose of this
18 transaction. That's right, isn't it?

19 A. Shared views with, sorry?

20 Q. With you, the two of you were discussing it. He would
21 have shared your views on what you intended to do?

22 A. He would have shared my views with whom, with me?

23 Q. Shared them with you?

24 A. Yes.

25 Q. The two of you, yes.

1 If we can just pull this together a little bit with
2 your interview, if we can go back to bundle C. Don't
3 put bundle 6 away yet, please. Just have a look at
4 bundle C and go to tab 21 and 286. Do you see that that
5 resolution, you have been looking at the resolution, and
6 Mr Lawford puts to you:

7 "Looking again at the end of the first paragraph,
8 the purpose of the amendment was to allow the company to
9 defer cash settlement of the interest on the notes at
10 its discretion."

11 He puts to you:

12 "If the purpose had been to alter the priority,
13 I think you said you would have expected the resolutions
14 to record that?"

15 And you said:

16 "Yes."

17 And that is right, isn't it?

18 A. Yes, I would have expected it.

19 Q. Mr Wilson says:

20 "Just to be clear, I think you may have answered
21 this, but you didn't discuss any alteration of ranking
22 with Mr Rush?"

23 You said:

24 "No."

25 And that is right as well, isn't it?

- 1 A. Yes, I don't recall discussing alteration of ranking
2 with Anthony Rush.
- 3 Q. Yes. And so you have confirmed that if the purpose had
4 been to alter priority, you would have expected the
5 resolution to say so, yes?
- 6 A. Yes.
- 7 Q. And you have confirmed that you would have expected
8 someone to tell you that was going on, yes?
- 9 A. Yes.
- 10 Q. And all you intended was that the interest could be
11 deferred so that you would achieve the tax benefit that
12 you have been describing to his Lordship; that's right,
13 isn't it?
- 14 A. That's correct.
- 15 Q. So going back to bundle 6, I want to go to 3338. This
16 is an e-mail sent by Ms Dave to Mr Guth, and it is
17 copied to Emily Upton and to you, and again, it is about
18 the amendments and it is sent on August 28. It is
19 addressed to Aaron. It says:
- 20 "We are looking at amending the terms of a note
21 issued by LB Holdings Intermediate 2 Limited to SLP3.
22 The change will allow LBHI2 to defer payment to SLP3
23 under the note. Interest will still accrue, however.
24 The change has been approved by London tax and legal."
25 So who was Aaron, can you help us with?

1 A. I think he was corporate counsel in the US. So he
2 was --

3 Q. Thank you very much?

4 A. -- Emily and Parul's equivalent, I guess, in the US.

5 Q. Thank you, and they explain what is -- what the changes
6 are, you see that?

7 A. Yes.

8 Q. And they say the change has been approved by London tax
9 and legal, which is -- that is the sort of process you
10 have been describing to his Lordship, isn't it?

11 A. That's correct.

12 Q. Yes, and London tax, presumably that is a reference to
13 your team?

14 A. Yes, it would be a reference to myself and Anthony Rush.

15 Q. Yes, and it attaches a draft consent to come from the
16 LBI board, and then goes on to say -- it says:

17 "We require a resolution of the Delaware board as
18 general partner of SLP2 which in turn acts as general
19 partner of SLP3."

20 We looked at that earlier.

21 "Would you be able to arrange this? I am not sure
22 who has been appointed on the board of Delaware and
23 would appreciate your help."

24 So they are asking for assistance with that
25 resolution. Then if we look at 3364, and what

1 Aaron Guth responds is:

2 "The directors are updated in WR."

3 What is WR?

4 A. World records.

5 Q. Thank you.

6 "Just e-mail the resolution to the directors, I
7 believe it's Triolo and Steinberg off the top of my
8 head, and they will approve."

9 Do you see that?

10 A. Yes.

11 Q. So that is -- Triolo, that is John Triolo, is that
12 right?

13 A. That's correct, and Daryl Steinberg.

14 Q. Thank you very much. And if we still have your
15 interview to hand, which is in tab 21, it is on page 21,
16 or 284, I just want to look at line -- picking it up
17 from line 4.

18 So you describe SLP3 and UK Holdings Delaware, and
19 then I want to pick it up on line 4, do you have that?

20 A. Yes, I do.

21 Q. So John Triolo would have known about this interest
22 deferral, because he would have been the one driving it
23 from a US tax perspective, yes?

24 A. Yes.

25 Q. That was right, wasn't it?

1 A. That's right.

2 Q. And so it kind of made sense for him to sign off. And
3 Mr Wilson says:

4 "Do you remember any discussions with anyone on the
5 LBHI2 director side?"

6 And you said:

7 "I don't know who ... the LBHI2 director that signed
8 it off, but if it was Anthony Rush, who was my boss, he
9 would have been fully aware of all the deferral, because
10 I would have taken him through it."

11 You have explained that to his Lordship.

12 But so Mr Triolo was involved in the US tax side?

13 A. He was.

14 Q. And so he would have understood the intention behind
15 deferring the interest payments from a tax perspective,
16 is that right?

17 A. Correct.

18 Q. And then if we can just go to 3503, which is the
19 Delaware consent, you can see that this is an electronic
20 consent of the board of directors -- I am so sorry?

21 A. That is all right, I have got it.

22 Q. Okay and you will see it is signed by Mr Triolo. At the
23 very top, it says:

24 "The undersigned being all the board of directors of
25 Lehman Brothers UK Holdings Delaware Inc ..."

1 And then the fourth recital, final sentence:

2 "The purpose of the amendment is to allow the issuer
3 to defer cash settlement of the interest on the notes,
4 at its discretion, the holder of the notes of SLP3."

5 Do you see that?

6 A. Yes.

7 Q. And so you can see that the drafting of this is very
8 similar to the LBHI2 minute that we looked at, yes?

9 A. He yes.

10 Q. And we can see again, there is no reference to ranking
11 alteration, yes?

12 A. No.

13 Q. And we see that Mr Triolo signed that on 3 September.
14 So let's just sort of draw that together. We can put
15 aside a lot of the paper. The 2008 amendments which we
16 have seen were authorised and approved by LBHI2 and by
17 SLP3, that's right, yes?

18 A. Yes.

19 Q. And both Mr Rush and Mr Triolo, who we have seen, were
20 tax people who were familiar with the transaction?

21 A. Correct.

22 Q. And they both understood that the intention behind the
23 transaction was to defer interest for the tax benefit
24 you have described, correct?

25 A. Correct.

1 Q. And both Mr Rush and Mr Triolo would have known that was
2 the purpose of the transaction, yes?

3 A. Yes.

4 Q. And all you intended was that the interest should be
5 deferred to achieve that tax benefit; you didn't have
6 any additional intention than that, did you?

7 A. No, not from a tax perspective, no.

8 Q. Mr Rush approved the 2008 amendments on behalf of LBHI2?

9 A. Yes.

10 Q. We have seen that. And you have explained to his
11 Lordship that you and he had a close working
12 relationship in which you discussed all of these issues
13 beforehand; that's right, isn't it?

14 A. Correct.

15 Q. And he shared the intention that you had which was to
16 defer the payment of interest for that tax benefit;
17 that's right, isn't it?

18 A. Correct.

19 Q. And you did not discuss ranking alteration with Mr Rush,
20 that's right?

21 A. Yes.

22 Q. And we have seen that the Delaware consent did not
23 mention any other purpose or intention, we have seen
24 that?

25 A. Yes.

1 Q. And Mr Triolo would have shared that same intention,
2 because he was a taxman in the US; that's right, isn't
3 it?

4 A. Correct.

5 MR PHILLIPS: Thank you, my Lord, I have no further
6 questions.

7 MR JUSTICE SMITH: Thank you very much, Mr Phillips.

8 Re-examination by MR BELTRAMI

9 MR BELTRAMI: Ms Dolby, I will be very short, you will be
10 delighted to hear. At some point this afternoon, you
11 were talking about levels of hierarchy within Lehman.
12 Mr Phillips was asking you about, I think that part of
13 your statement dealing with corporate governance, can
14 you remember that, the last few paragraphs of your
15 statement? And you said that: the initiatives, I think
16 you were talking in the plural in generality here, would
17 go through various levels of hierarchy and sign-off
18 before it was ultimately, before they were ultimately
19 signed off by the board. I think --

20 A. Yes, that's correct.

21 Q. That is what you said. I wrote it down. It is in the
22 transcript. Could you just explain what those various
23 levels of hierarchy and sign-off were that you referred
24 to?

25 A. Yes. So as this was a kind of a tax -- tax-related

1 structure, we would have had to take it through the tax
2 oversight committee to say we are looking to do this,
3 and they would have had to approve it before we could
4 have moved forward with it, and on -- on that tax
5 oversight committee, you would have had the global head
6 of tax based in the US. You would probably have had
7 some of his direct reports. You would have had
8 Anthony Rush. You potentially would have had the CFO,
9 the European CFO. And potentially a couple of the
10 senior guys in front office that also did tax
11 structuring from a front office perspective. So we
12 would have had to take it through that tax oversight
13 committee, for instance.

14 Q. That is a for instance. Any other hierarchy that you
15 were referring to when you described that?

16 A. I am not sure if this went through -- there was like
17 a new products committee that had various senior people
18 on it, from all divisions across corporate. I can't
19 remember whether this went to the new products committee
20 or not.

21 Q. Thank you. You can put away all of that apart from --
22 we are going to need that, because we are going to be
23 going in a minute -- bundle C, tab 21, which is your
24 transcript, and could you go to the last page, please,
25 on page 300. You were asked, I think at the beginning

1 of your questioning, about -- you were asked
2 specifically whether you had any issues in relation to
3 the clause 3 of the note, the amended clause 3, and you
4 said: there was no tax concern there, tiering wasn't
5 a tax issue; that is what I wrote down.

6 Can I ask you, in your transcript at page 300, about
7 line 10, you were asked by Mr Taylor:

8 "Do you recall thinking about subordination and
9 ranking at all in the context of these amendments?"

10 You say:

11 "That wasn't a tax. Tax weren't interested in that.
12 That would have been a regulatory and potentially
13 treasury, but it wasn't a thing that we were interested
14 in."

15 My only question on that is who then would be in the
16 regulatory and potentially treasury that you refer to?

17 A. So regulatory would have been Gareth Bowen, treasury
18 would have been Dave Rushton. Carlo Pellerini(?), he
19 was the head of European treasury at that time, so those
20 are the individuals I would have been referring to.

21 MR BELTRAMI: Thank you, Ms Dolby. That is all I had.

22 Does your Lordship have any further questions?

23 MR JUSTICE SMITH: Thank you, Ms Dolby. I have no

24 questions, thank you. You are released.

25 MR BELTRAMI: My Lord, I think we are all released at this

1 point because I think Mr Katz is coming tomorrow
2 morning.

3 MR JUSTICE SMITH: Mr Katz is on tomorrow.

4 MR PHILLIPS: He is, my Lord. Then Mr Geraghty, and after
5 that we have the US experts who are coming on Friday.
6 I don't think anybody thinks that a day isn't going to
7 be sufficient for that.

8 And tomorrow, of course I don't know how long my
9 learned friends will be with Mr Geraghty, but I cannot
10 imagine that Mr Katz and Mr Geraghty will take more than
11 a day, so I think the timetable is intact.

12 MR JUSTICE SMITH: I am very pleased to hear it, and
13 thank you all for your efforts in making it so. We will
14 resume in that case at 10.30 tomorrow morning.

15 (3.35 pm)

16 (The hearing was adjourned
17 until Thursday, 14 November 2019 at 10.30 am)

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