IN THE COURT OF APPEAL **A3/2020/1787**

ON APPEAL FROM THE HIGH COURT OF JUSTICE

IN THE MATTER OF LB HOLDINGS INTERMEDIATE 2 LIMITED (IN ADMINISTRATION)

AND IN THE MATTER OF THE INSOLVENCY ACT 1986

BETWEEN:

LEHMAN BROTHERS HOLDINGS SCOTTISH LP3

Appellant

and

(1) LEHMAN BROTHERS HOLDINGS PLC (IN ADMINISTRATION)
(2) DEUTSCHE BANK AG (LONDON BRANCH)
(3) THE JOINT ADMINISTRATORS OF LB HOLDINGS INTERMEDIATE 2 LIMITED (IN ADMINISTRATION)

Respondents

REPLACEMENT SKELETON ARGUMENT OF

THE JOINT ADMINISTRATORS OF LEHMAN BROTHERS HOLDINGS PLC ("PLC")

in the LBHI2 proceedings

INTRODUCTION

1. This is the skeleton argument of PLC as respondents to the appeal of SLP3 against paragraph 1 of the Order of Marcus Smith J dated 24 July 2020 (the **Order**[1]), by which it was declared that the claims of PLC under the LBHI2 Sub-Debt (**Claim A**)[2] ranked for distribution ahead of the claims of SLP3 under the LBHI2 Sub-Notes, as amended on 3 September 2008 (**Claim B**)[3]. PLC adopts the abbreviations employed by the Judge in the **Judgment**[4] dated 3 July 2020.

2. The issues to be addressed on the SLP3 appeal comprise:

   a. The **ranking issue** as between Claim A and Claim B. This is an issue of contractual interpretation and was considered at Judgment [125]-[253]. Issues relevant to the background are discussed below at Section A. The SLP3 Grounds of Appeal[5] identify the separate consideration given by the Judge to the ranking issue by reference to (a) the original, unamended form of the LBHI2 Sub-Notes (at Judgment [125]-[198], **historic ranking**); and (b) the current, amended form of the LBHI2 Sub-Notes (at Judgment [199]-[253], **present ranking**). The same course is followed in this skeleton: see Sections B, C and D.

   b. The **rectification claim**, made by SLP3 in the event that (as the Judge found) the ranking issue was determined against it. At Judgment [254]-[269], the Judge rejected the rectification claim. This is addressed at Section E.

3. Respondent's Notices have been served by PLC in respect of the ranking issue and the rectification claim. PLC's position in summary is that:

   a. PLC agrees with SLP3 that the Judge erred in concluding that Claim B historically ranked in priority to Claim A. PLC submits that Claim A historically ranked in priority to Claim B.

   b. So far as concerns present ranking, the Judge was right to conclude that Claim A ranked in priority to Claim B.

   c. The Judge was also right to reject the rectification claim, which has no foundation on the evidence.

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[1] [CB2/23].

[2] [CB3/38; CB3/39; CB3/40].

[3] [CB3/41; CB3/42].

[4] [CB2/22].

[5] [CB1/3].

A. BACKGROUND TO THE RANKING ISSUE

A1. Contractual interpretation

4. At Judgment [60], the Judge quoted from *The Ocean Neptune*[6] as a sufficient summary of the well-known principles of contractual interpretation, which were not in dispute[7]. Further specific aspects for emphasis are:

   a. The unitary exercise of interpretation may involve giving greater or lesser weight to any of the particular words used, the contractual context, the wider factual matrix and the commercial sense of rival interpretations. In the case of formal and sophisticated contracts, especially ones drafted by lawyers, correspondingly greater weight is accorded to the words used and the contractual context[8]. In such cases, interpretation should accordingly be "*principally by textual analysis*"[9].

   b. The approach to contractual interpretation is objective, whether or not the parties had any pertinent subjective intention as to meaning[10]. This means that references to the contractual "*purpose*" of a document are also objective[11]. Accordingly, an enquiry into what the actual parties might or might not have subjectively intended or believed (even if such an enquiry could at this remove have yielded any safe conclusions) is futile and irrelevant.

   c. Effect is to be given to every word used in the contract so far as possible and words should not be added which are not there unless sense cannot otherwise be made of the language[12].

5. As regards the interpretation of an amended contract, the same rules of interpretation apply. The general principle is that each amendment falls to be interpreted as at its date, against the circumstances then prevailing. The meaning must be ascertained as at the date of the amendment[13]. The consequence is that it

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[6] [2008] EWHC (Comm) 163 at [8].

[7] To the extent necessary, reference may also be made generally to *Investors Compensation Scheme Ltd v West Bromwich Building Society (No. 1)* [1998] 1 WLR 896 at 912-3; *Arnold v Britton* [2015] UKSC 36, [2015] AC 1619, at [14]-[23]; and *Wood v Capita Insurance Services Ltd* [2017] UKSC 24, [2017] AC 1173, at [9]-[14].

[8] *Lukoil Asia Pacific v Ocean Tankers* [2018] EWHC 163 (Comm), [2018] 1 Lloyd's Rep 654.

[9] *Wood v Capita*, at [13].

[10] *Tartsinis v Navona Management Co* [2015] EWHC 57 (Comm) at [9] per Leggatt J.

[11] *Reardon Smith Line v Hansen Tangen* [1976] 1 WLR 989 at 995-996.

[12] *Multi-Link Leisure Developments Ltd v North Lanarkshire Council* [2010] UKSC 47, [2011] All ER 175, at [11].

[13] *Stena Line Ltd v Merchant Navy Ratings Pension Fund Trustees Ltd* [2011] EWCA Civ 543, [2011] Pens LR 223, at [30] and [32].

is an erroneous exercise to interpret the contract in a pre-amended state and then ask whether there was any intention to change that interpretation (although that question may be relevant to rectification claims).

6. At Judgment [61], the Judge explained why the admissible factual matrix in this case was narrow. SLP3 continues to argue for a broader factual matrix but the Judge properly rejected that submission, for the reasons he gave. The relevant context for this conclusion was as follows:

   a. The LBHI2 Sub-Debt agreements compulsorily replicated an FSA standard form under the then applicable regulatory regime, IPRU(INV). The scope for admissible factual matrix for their interpretation was therefore inherently attenuated[14].

   b. The Terms and Conditions of the LBHI2 Sub-Notes were contained in the Offering Circular dated 26 April 2007, as amended pursuant to a resolution dated 3 September 2008. Under the regulatory regime by then in place, GENPRU, there was no compulsory standard form[15] and so the wording used in the Offering Circular was the choice of the drafters, albeit that it had to be compliant with GENPRU. In fact, the LBHI2 Sub-Notes did not replicate any standard form in evidence and the source of the relevant wording used was unidentified[16].

   c. The Offering Circular was a formal, complex and sophisticated document, in respect of a debt obligation of over $6 billion and it (and its amendments) were drafted by A&O and considered by senior professionals within Lehman. It was at the most sophisticated end of the scale of contractual documents, such that a textual analysis was likely to carry overwhelming weight in the interpretation exercise.

   d. The LBHI2 Sub-Notes were created as negotiable notes listed on the Channel Islands Stock Exchange (**CISX**) which were transferable according to their terms. As such, only a very narrow factual matrix

[14] See generally *AIB Group (UK) Ltd v Martin* [2001] UKHL 63, [2002] 1 WLR 94, at [7].

[15] See [GENPRU 2.2.164].

[16] Although it seems that the LBHI2 Sub-Notes began with a prior form of PLC Sub-Note as a base document [Day 2/156.15-157.15)] [SB2/53/554-555], substantial changes were then made, including a full re-writing of clause 3 on "Status and Subordination". Mr Miller of A&O believed that there were other transactions which used the same wording but was unable to say where the new clause 3 came from [Day 2/158.4-160.25] [SB2/53/555], although was "*pretty sure*" that he did not look at the forms for IPRU(INV) Ch 5 or 10 [Day 2/161.5-6] [SB2/53/556].

was in principle admissible on their construction[17]. Further, in the case of a tradeable instrument, the commercial intention is to be derived from the terms of the contract itself[18].

e. As the lending was used for the purpose of regulatory capital, the regulatory regimes provided potentially relevant context and factual matrix (subject to the limitations described below).

f. More broadly, the position before the Judge presented profound difficulties in any resort to evidence of extra-contractual intent. The instruments were drafted and produced in the context of a complex multinational corporate structure, which was responding to regulatory requirements and taxation determinants in different jurisdictions, over a decade ago. Each step that was taken was the subject of detailed advice by lawyers and accountants. It was impossible to recreate all the factors in play at any one time or all the considerations leading to the decisions taken. Those difficulties are even greater on appeal.

7. The Judge discussed at Judgment [65]-[70] the regulatory background.[19] This is relevant, though principally because it is neutral as to the outcome of the ranking issue. LBIE was a regulated investment firm and the UK Lehman Group was subject to consolidated supervision by the FSA. Both the LBHI2 Sub-Debt and the LBHI2 Sub-Notes qualified, and were intended to qualify, as lower tier 2 regulatory capital.

8. However, the most important element of the regulatory background, as noted at Judgment [61(3)(c)] and [262(2)] and never disputed, was that, whilst for the subordinated debt to qualify as tier 2 regulatory capital, it had to be subordinated to all unsubordinated debt (Judgment [57]), the regulators were indifferent to the relative priority of regulatory capital debt. Neither IPRU(INV) nor GENPRU said anything about priority between subordinated debts: they did not require (nor even suggest or prefer) relative *pari passu*. This meant that, whilst the regulatory background was in principle admissible factual matrix evidence, the significance of that evidence to the matters for determination was slight. The question asked of the Court, as to the relative ranking of subordinated instruments, was not a matter which formed part of the regulatory scheme

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[17] *Chitty on Contracts* (33rd edn, 2018) at [13-051]; *Cherry Tree Investments v Landmain* [2012] EWCA Civ 736, [2013] Ch 305, at [124], [125] and [130]. See also *BNY Mellon Corporate Trustee Services Ltd v LBG Capital No. 1 plc* [2016] UKSC 29, [2017] 1 All ER 497, at [30] per Lord Neuberger.

[18] *Napier Park European Credit Opportunities Fund Ltd v Harbourmaster Pro-rata CLO 2 BV* [2014] EWCA Civ 984 at [33]. *Street v Mountford* [1985] AC 809 at 826 per Lord Templeman, "… *the only intention which is relevant is the intention demonstrated by the agreement…".*

[19] See also *Waterfall1* (HC): Re *Lehman Brothers International (Europe) (in administration)* [2014] EWHC 704 (Ch), [2015] Ch 1, at [35-47].

and responded to no part of the regulatory purpose. Ultimately, relevant ranking under the various instruments was a matter of close construction of the terms of the instruments in question.

9. As part of its case on factual matrix, SLP3 also seeks to place reliance on supposed evidence of market practice. At SLP3 skeleton [16], [48(4)] and [67] ([CB1/7/61, 73, 81]), it is alleged that a relative *pari passu* ranking of subordinated debt at the same tier was the "*market expectation*" or the "*custom*". The Judge indicated no support for this submission, which must be rejected. In its original Position Paper[20], SLP3 had hinted at the possibility of running a "*market practice*" argument but it did not seek or obtain permission to call the necessary expert evidence to support it.[21] In its Opening, SLP3 claimed to rely on certain specific "*open source materials*" to advance this point[22] although the materials did not evidence such market practice and no reliance is now placed on them. In its Closing, and now on appeal, SLP3 sought to rely on some observations of Mr Miller, a partner at A&O, given in the witness box[23] (although nowhere in his witness statement). However, those observations were inadmissible as evidence of any market practice, as Mr Miller was a witness of fact only and cannot convert into an expert witness, for which no permission had been sought and therefore as to which PLC had no opportunity to lead its own evidence. Further and in any event, what Mr Miller actually said was, sensibly enough, that he "*would expect instruments within lower tier 2 and 3 to rank pari passu between themselves*" as a default because often there would be no commercial reason not to do so, but there was flexibility to layer even between debt of the same tier, and it all depends upon the terms of the agreements. That does not take the question of what these particular instruments did on their proper construction any further.[24]

A2. Subordination

10. At Judgment [71]-[124], the Judge discussed the nature of subordination, concluding (correctly) in particular that: (a) Consensual subordination may be by way of simple contractual subordination, contingent debt subordination and (not relevant here) trust subordination; (b) Instruments may deploy a combination of methods of consensual subordination; (c) Simple contractual and contingent debt subordination can only serve to demote the creditor's interest in relation to other creditors. They cannot improve the creditor's

[20] SLP3 Position Paper [24(6)(ii)] [CB2/32/525].

[21] See SLP3's letter to all parties dated 14 May 2019 confirming it would not be seeking permission for such evidence: [SB2/62/642-655].

[22] SLP3 Written Opening at fn 119 to [105] [SB1/8/138-9], and Oral Opening [Day 1/20.8-13] [SB2/49/531].

[23] Day 6/1.12 to 2.3 [SB2/56/578]. The evidence, described by SLP3 as "*key*", was nothing of the sort.

[24] And SLP3's claim in SLP3 skeleton [53(1)] [CB1/7/75] that Mr Miller said that 'clear and unequivocal language' is needed to displace a pari passu ranking is invention on SLP3's part.

interest; and (d) Simple contractual and contingent debt subordination may subordinate not merely within a category of obligation but between categories of obligation.

11. At Judgment [111] and [122], the Judge went on to address the provability of subordinated debts, concluding that the creditor whose claims are subordinated by a contingency must prove in the ordinary way, whereas an effective provision for simple contractual subordination renders the creditor unable to prove until senior obligations have been satisfied in full.

12. The manner in which SLP3 seeks to formulate the ranking issue suggests that its case is that there is significance in identifying the order in which creditors are entitled to prove for their debts[25] but this is to turn the relevant question upside down. The ranking issue is determined as a matter of contractual interpretation (it is understood that all parties agree that this is so). The outcome of that determination may or may not have a consequential impact on whether and if so when, as a matter of insolvency process, a particular creditor is entitled to prove for its debt, if that matters in any case. No such issue arises in the present case, where the question is purely one of ranking.

13. It is correct that, in *Waterfall I*, the Court was required to give consideration to the question of provability. This was because of the operation of (the then-applicable) IR2.88(7) which (as set out in *Waterfall I* (HC) at [43]) provided that statutory interest should be paid out of "*any surplus remaining after payment of the debts proved.*" One of the arguments of the subordinated creditor (LBHI2) was that, because its subordinated debt was provable, IR2.88(7) meant that such debt had to rank ahead of statutory interest. Although each of the Courts rejected this argument of legislative priority, there was a difference of view as to why. David Richards J held at [69] that LBHI2 was precluded from lodging a proof because of a separate prohibition at clause 7(d)(e) of the relevant agreement. Lewison LJ at [39]-[41] disagreed as to the effect of clause 7(d)(e) but concluded that this did not matter because the proof would be valued at nil. Lord Neuberger at [69] thought that David Richards J's view was to be preferred. But this was to deal with the nuance of IR2.88((7) and had no broader effect on the contractual ranking issue. This can be seen for example in Lord Neuberger's speech. The analysis of the ranking issue starts at [37]. At [64]-[66], he reaches "*Conclusions on priority*". Only after that, at [68]-[72] does he consider the point about proofs.

14. Similarly, or perhaps as part of the same argument, SLP3 sets much store by the existence of IR14.12[26] (elevated by SLP3 to "The Pari Passu Principle"[27]). Its main theory is that the exercise of contractual interpretation necessary to determine the ranking issue is itself skewed by the existence of the default rule of *pari passu* ranking. Before the Judge, it was contended (without authority) that the effect of IR14.12 was

[25] Described as "*the critical issue*" at SLP3 skeleton [23] [CB1/7/63].

[26] Numbering under the 2016 Rules.

[27] SLP3 skeleton [21] [CB1/7/62-63].

a "*strong default position"*, whatever that means, and that *pari passu* ranking could be displaced only by "*something clear and unequivocal to the contrary"*[28]. The same argument is advanced on appeal (see below).

15. The Judge's careful explication of the insolvency "waterfalls" and of the efficacy of subordination provisions undermines SLP3's contention. As noted at Judgment [101], the prevailing wisdom prior to 1993 had been that the predecessor to IR14.12 was more than even a strong default: it was thought to be a rule by which all unsecured creditors were paid *pari passu*. However, it was confirmed first in *Re Maxwell Communications Corp plc (No 2)*[29] and then in *Re SSSL Realisations (2002) Ltd*[30], that creditors could agree to subordinate their debts, such that *pari passu* was not overriding or mandatory. The same was confirmed in the context of regulatory subordinated debt materially identical to the LBHI2 Sub-Debt in *Kaupthing Singer & Friedlander Ltd*[31] (contrary to SLP3's suggestion that the debt being regulatory capital alters the position in some way[32]). Whether a creditor has in fact done so is a question of contractual interpretation. As Arden LJ noted in *Lehman Brothers International (Europe) v CRC Credit Fund Ltd,*[33] the *pari passu* maxim is not of universal applicability: "*It always yields to a contrary intention, express or inferred…"* And in *Waterfall I* (SC),[34] per Lord Neuberger: "*I can see no objection to giving effect to a contractual agreement that, in the event of an insolvency, a contracting creditor's claim will rank lower than it would otherwise do in the 'waterfall'".* Accordingly, the relevance of IR14.12 is that it is engaged in a gap-filling role, if the contract runs out[35]. It does not assist in the determination of what the contract actually says.

16. At SLP3 skeleton [36] ([CB1/7/68-69]), SLP3 puts its case on historic ranking on two bases. The first is that the Judge's own approach ought to have led to the conclusion that the subordination provisions were ineffective as between each other. As to that, PLC accepts that, if the correct conclusion were indeed that the provisions were ineffective, then *pari passu* would be the result, by operation of law as the contract would have run out. The second is that Claim A and Claim B ranked *pari passu* as a matter of construction. If, again, this were the correct conclusion, then *pari passu* would again be the right result, this time by operation of contract. In both cases, however, (and hence on the entirety of SLP3's case), *pari passu* would be the conclusion from the process of construction. The mere existence of IR14.12 would not be a driver in that

[28] Day 6/2.23 to 3.1 [SB2/56/578].

[29] [1993] 1 WLR 1402.

[30] [2006] EWCA Civ 7.

[31] [2010] EWHC 316 (Ch) per Blair J at para 10.

[32] SLP3 Written Opening para 44 [SB1/8/122].

[33] [2010] EWCA Civ 917, [2011] Bus LR 277 at [76], quoting from *Cox v Bankside Members Agency Ltd* [1995] 2 Lloyd's Rep 437, at 463 per Peter Gibson LJ.

[34] *Re Lehman Brothers International (Europe) (No. 4)* [2017] UKSC 38, [2018] AC 465 at [66].

[35] See generally *Re Golden Key Ltd* [2009] EWCA Civ 636 [3]-[6].

process, whether by purported "*factual matrix*" or otherwise. This is why SLP3's persistent reliance on IR14.12 as if it assisted in the exercise is misplaced.[36]

A3. Analysis of the subordination provisions in the LBHI2 Sub-Debt

17. At Judgment [126]-[149], the Judge analysed the LBHI2 Sub-Debt agreements. Although there are three agreements, variations are not material. As noted at Judgment [131] and [134], the Front Page records the purpose that the loan qualify as regulatory capital. No other purpose is specified.

18. The Standard Terms contain a series of definitions of the liabilities of LBHI2. The effect of the definitions is to place all of LBHI2's liabilities into 3 categories, for the purpose of the LBHI2 Sub-Debt agreements: Excluded, Subordinated and Senior. Subordinated Liabilities are, on the apparent face of the wording used, limited to the debt arising under that particular agreement. Excluded Liabilities are debts which are expressed to be junior to the Subordinated Liabilities and so require a cross-referral to the terms of LBHI2's other obligations. And Senior Liabilities is the default category for everything else. There is no express reference to the possibility of debts ranking *pari passu* with the LBHI2 Sub-Debt in question.

19. At Judgment [140]-[146], the Judge found that the first part of paragraph 5(1) is a form of simple contractual subordination, the effect of which is to subordinate the liabilities under the LBHI2 Sub-Debt agreement to Senior Liabilities and that the second part of paragraph 5(1) is a form of contingent debt subordination, of which the operative part is the solvency condition at paragraph 5(1)(b), coupled with the solvency definition at paragraph 5(2).

20. The two subordination provisions identified by the Judge are linked by the word "*accordingly*". At Judgment [147]-[149], the Judge interpreted this word as a conjunction (meaning in effect '*and also*'), giving separate and cumulative effect to each clause. At Judgment [149], he said that the simple contractual subordination was "*reinforced*" by the solvency condition.

21. It does not ultimately matter for the determination of the ranking issue whether the LBHI2 Sub-Debt agreements each contain two separate (and hence potentially competing) subordination provisions or a single subordination provision, because the end result is likely to be the same. Nevertheless, PLC does see potential difficulties with the former and submits that the better analysis is that the LBHI2 Sub-Debt agreements (and, as below, the LBHI2 Sub-Notes) should each be construed as containing a single

[36] And PLC agrees with SLP3 that all depends upon the parties' agreement as to whether the debts prove at the same time (SLP3 skeleton [8(2)] incl fn 10, [21(2)], [22], [23(1)], [24]) ([CB1/7/59, 62-64]).

composite subordination provision, given that (for reasons of certainty and commercial sense) paragraph 5 is intended to achieve a single operative outcome. SLP3 agrees, as understood[37].

22. Reading it in this way, whilst the first element (namely the statement that the rights of the Lender are subordinated to Senior Liabilities) if alone might well operate to effect subordination, when it is coupled with the detailed subordination mechanism comprising the solvency condition in paragraph 5(1), that first element may properly be regarded as a statement of introductory or general intent[38]. The second element is the critical and implementing provision, which creates and defines the subordination of the debt and it is through the mechanism of the solvency condition that the subordination is given effect.

23. A solvency condition such as this enables the contracting parties to specify the precise level at which the subordination is cast. If no payment can be made unless a solvency condition is satisfied, then the components of the solvency test will determine the corresponding level of subordination. In simple terms, the more debts that have to be capable of being paid within the solvency test, the deeper the subordination. And this is exactly how the same provision has been analysed in *Waterfall I*, with the solvency condition identified and analysed as the operative condition that determined the ranking of the debt, with no consideration of the effect of the introductory words of paragraph 5(1) as if this provided a distinct and additional subordination clause in its own right.[39] To the same effect is the approach of Henderson J in *Lehman Brothers Luxembourg Sarl v Lehman Brothers UK Holdings Ltd*[40], who described paragraph 5(1) in the following terms: "*In order to give effect to the principle of subordination, payment of any amount… in respect of the loan is then made conditional upon the matters set out in sub-paragraphs 5(1)(a) and (b).*" So, the initial words of the paragraph set out the principle of subordination but it is the solvency condition which gives effect to it.

24. On this analysis, the ranking issue falls to be tested against the operation of the solvency condition. In effect, the synonym for "*accordingly*" in the introductory words is not "*and also*" but "*therefore*" and the solvency condition does not "*reinforce*" the subordination but implements it. The same applies to the LBHI2 Sub-Notes. As submitted above, this does not affect the outcome, but PLC considers that it provides a more coherent and principled approach.

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[37] SLP3 Skeleton [26] advocating construing the provision "*as a whole… in a unified manner*" ([CB1/7/64-65]).

[38] As to these elements, the labels used by the Judge ("*simple contractual subordination*" and "*contingent debt subordination*") are just that (i.e. labels) and it is possible that they may serve to confuse rather than elucidate.

[39] See Lewison LJ in the CA identifying only the solvency condition and making no reference to the introductory words: [2015] EWCA Civ 485, [2016] Ch 50 at [38] (the second method). In the SC no reference was made to CA [38] but the focus was again on the solvency condition.

[40] [2016] EWHC 617 (Ch) at [17].

25. At SLP3 skeleton [26] ([CB1/7/64]), SLP3 submits that the Judge erred in identifying separate subordination provisions in each instrument. As above, PLC agrees that the better analysis is a single provision. However, SLP3 goes on to submit that the Supreme Court in *Waterfall I* "*expressly rejected*" the Court of Appeal's "*contingent debt subordination analysis in favour of a simple contractual subordination analysis."* As to this:

a. If this is a point about labels (such as whether the label 'contingent debt subordination' is best avoided), or when a debt has to prove, then it is a rather arid debate, when what matters is what the instruments actually say and where in the ranking the instrument sits.

b. If, as appeared to be suggested before the Judge, the submission is that the Supreme Court in some way disagreed with Lewison LJ's description of methods of subordination, either generally or with regard to paragraph 5(1), then PLC disagrees. The Supreme Court said nothing about the relevant paragraph in Lewison LJ's judgment, none of which was controversial.

c. The Supreme Court did disagree with Lewison LJ's subsequent views (expressed, *"In addition*…") at [41] as to when a subordinated creditor can prove for its debt but, as explained above, that was in connection with an issue on which no point turns in the present case.

A4. Analysis of the subordination provisions in the LBHI2 Sub-Notes as unamended

26. This was considered at Judgment [157]-[172]. At Judgment [161], the Judge dismissed the relevance of the evidence of the witnesses to the interpretation of the unamended LBHI2 Sub-Notes. He was correct to do so for the reasons he gave. In particular: (a) such evidence fell outside the admissible factual matrix; (b) it was at best inadmissible evidence of subjective intent (or indeed hypothetical subjective intent); and (c) the highest it went, in any event, was evidence of an intention to subordinate the LBHI2 Sub-Notes in accordance with the regulatory regime, which was neutral as to the relative ranking of subordinated debt. It is not understood that SLP3 challenges the Judge's approach.

27. The Judge concluded that, like the LBHI2 Sub-Debt, the unamended LBHI2 Sub-Notes contain both a form of simple contractual subordination and a form of contingent debt subordination. By what he termed simple contractual subordination, the rights of the noteholders are "*subordinated in right of payment to the Senior Creditors (as defined below)…"*. Senior Creditors are defined as: "*creditors of the Issuer (i) who are unsubordinated creditors of the Issuer or (ii) who are subordinated creditors of the Issuer other than those with whose claims the claims of the Noteholders are expressed to rank pari passu and those whose claims rank, or are expressed to rank, pari passu with, or junior to, the claims of the Noteholders."* As the Judge noted at Judgment [166(2)], the relevant provision for present purposes is clause (ii). Further, as per Judgment [166](2)(a)], the starting point on its face is the acknowledgment that even subordinated creditors will constitute Senior Creditors under the LBHI2 Sub-Notes, unless they fall within the defined proviso within clause (ii).

28. As for the proviso within clause(ii), the Judge noted at Judgment [166](2)(e)] that the operative part, so far as relevant, is the second clause. This requires that the claims of the subordinated creditor "*rank, or are expressed to rank" pari passu* with or junior to the claims of the Noteholders. The Judge concluded that the first word "*rank*" was a reference to legal subordination but that the critical words in a situation involving consensual subordination were "*expressed to rank"*, which must be right, given that consensual subordination affects the legal position. There is no relevance, in the present case at least, to an enquiry into where an instrument ranks in the abstract beyond the crucial enquiry into where it is expressed to rank.

29. As with the LBHI2 Sub-Debt agreements, the operative subordination provision lies in the solvency condition, which the Judge referred to as contingent debt subordination. Clause 3(a) goes on to provide that "*no amount which would otherwise fall due for payment shall be payable except to the extent that the Issuer could make such payment and still be solvent immediately thereafter"*. By clause 3(b), the Issuer is solvent if "*(i) it is able to pay its debts as they fall due and (ii) its Assets exceed its Liabilities (each as defined below) (other than its Liabilities to persons who are not Senior Creditors)."* The Judge addressed these contingencies at Judgment [171]. There are two contingences, separated by the conjunction "*and*". As the Judge said, the contingencies are therefore cumulative and not alternative (i.e. both must be satisfied).

30. The Judge erred in his treatment of this first contingency in the solvency condition. The Judge's conclusion that the solvency test fell to be applied "*from time to time as and when LBHI2 seeks to make a payment"* must be correct, though this point had never been in issue.[41] This means that, on each occasion on which the condition falls to be tested, the question is whether LBHI2 is able to pay its debts which are then presently due. But the Judge failed to apply that condition when considering the ranking issue as against the unamended LBHI2 Sub-Notes, and effectively ignored it.

31. The correct approach, which PLC submitted to the Judge and repeats on Appeal, is that, at each point at which a payment would otherwise be made by way of distribution, one applies the condition as against debts remaining due. The words "*its debts*" mean what they say, namely all of LBHI2's due and unpaid debts, which must therefore include both unsubordinated and subordinated debts; and debts, once due and remaining unpaid, are not thereafter excluded for the purpose of the condition. The LBHI2 Sub-Debt agreements and the LBHI2 Sub-Notes differ in this because the LBHI2 Sub-Debt agreements contain no such equivalent provision in their solvency condition. The effect of this condition is, accordingly, to achieve the

[41] There was no need for the Judge to raise or discuss (Judgment [171]) the question of whether the condition created a one-off trigger—i.e. that if the Issuer was once unable to pay its debts as they fell due, it was always unable to pay its debts as they fell due. No party had argued in favour of such a construction.

subordination of Claim B below all other due debts of LBHI2[42], as the condition can never be satisfied unless and until all those debts are capable of being paid in full.

B. HISTORIC RANKING

32. The Judge addressed at Judgment [173]-[198] the relative ranking of Claim A and Claim B, by reference to the unamended LBHI2 Sub-Notes. In so doing, he considered separately the effect on ranking of simple contractual subordination and contingent debt subordination provisions in the LBHI2 Sub-Debt agreements and thereafter the provisions in the LBHI2 Sub-Notes. His conclusion, at Judgment [198], was that (a) under the LBHI2 Sub-Debt agreements, Claim A subordinated itself to Claim B but that (b) under the LBHI2 Sub-Notes, Claim B said nothing about relative priority to Claim A. He then determined that Claim A was (on the historic position) subordinated to Claim B. Neither SLP3 nor PLC had argued for that outcome at trial or seeks to support it on appeal.

33. The Judge arrived at this outcome by the following process:

    a. In considering the simple contractual subordination provision in the LBHI2 Sub-Debt agreements, there was a need to determine whether the competing claim under the LBHI2 Sub-Notes, Claim B, was an Excluded Liability under the LBHI2 Sub-Debt agreements.

    b. In order to determine whether Claim B was an Excluded Liability under the LBHI2 Sub-Debt agreements, it was therefore necessary to see whether, under the LBHI2 Sub-Notes, Claim B was expressed to rank junior to (or pari passu with) Claim A.

    c. The terms of the LBHI2 Sub-Notes placed Claim B as junior to Senior Creditors, hence it was necessary to revert to the LBHI2 Sub-Debt agreements to see whether Claim A was under those agreements expressed to rank junior to Claim B (absent which Claim A would be a Senior Creditor under the LBHI2 Sub-Notes, and so Claim B would be an Excluded Liability under the LBHI2 Sub-Debt agreements).

    d. However, the LBHI2 Sub-Debt agreements said nothing about the ranking of Claim A against Claim B (Judgment [183]): "*There is no meaningful expression of ranking at all.*" The Judge continued "*That being the case, PLC's claims under Claim A do not constitute PLC a Senior Creditor* [under the LBHI2 Sub-Notes]." Therefore, under the LBHI2 Sub-Debt agreements, Claim B was not expressed to be junior to Claim A (Judgment [184]). Hence, under the LBHI2 Sub-Debt agreements, Claim B was an Excluded Liability and Claim A was accordingly subordinated to it.

[42] Theoretically, if another LBHI2 debt carried the same provision then this could create an issue of circularity, of the sort which arises in respect of Claims A(i), (ii) and (iii), but no such issue arises on these instruments.

e. At Judgment [191], the Judge considered the question from the perspective of the LBHI2 Sub-Notes. His view, as above, that PLC's claims under Claim A did not constitute PLC as a Senior Creditor under the LBHI2 Sub-Notes, led him to conclude that, under the LBHI2 Sub-Notes, "*there is no applicable subordination provision at all.*"

34. In reaching these conclusions on historic ranking, the Judge misapplied his own findings. SLP3 agrees with PLC that the Judge made a "*clear error*" in this respect[43]. Having determined that there was no "*meaningful expression of ranking*" in the LBHI2 Sub-Debt agreements, he concluded that this meant that Claim A was not a Senior Creditor under the LBHI2 Sub-Notes. However, on those findings, the opposite conclusion followed. Under the LBHI2 Sub-Notes all subordinated creditors were Senior Creditors unless they were expressed to rank junior or pari passu to Claim B. Accordingly, if there was no meaningful expression of ranking in the LBHI2 Sub-Debt agreements, then Claim A must on the Judge's findings have been a Senior Creditor under the LBHI2 Sub-Notes.

35. The Judge's error is apparent on the Table at Judgment [185] (at 4(d)). He correctly noted that, under the LBHI2 Sub-Notes, Senior Creditors included subordinated creditors other than those whose claims were expressed to rank *pari passu* or junior (Judge's emphasis). He then said, with respect to Claim A, "*PLC's claims do not fall within this definition* [i.e. the 'other than…' carve out]. *They are (on their own terms) subordinated and are not expressed to rank either pari passu or junior to SLP3's rights.*" This is, so far, consistent with the Judge's findings. However, he then said, "*PLC is not, therefore, a Senior Creditor, SLP3's rights are not subordinated.*" This conclusion cannot follow from the premise: if, as per the premise, all subordinated creditors are Senior Creditors unless there is a contrary expression of *pari passu* or juniority, and if the LBHI2 Sub-Debt agreements contain no such contrary expression, then Claim A must be a Senior Creditor under the LBHI2 Sub-Notes. The same error can be seen in the Table at Judgment [191].

36. Further, having reached the conclusion that Claim A subordinated itself to Claim B under the LBHI2 Sub-Debt agreements and that Claim B said nothing about its relative priority to Claim A under the LBHI2 Sub-Notes, the Judge went on to resolve the apparent conflict within the two agreements by applying the terms of the LBHI2 Sub-Debt agreements, which he said (Judgment [198]) "*must be given effect to.*" The reason for privileging the LBHI2 Sub-Debt agreements over the LBHI2 Sub-Notes was not given and is not apparent. If, on the Judge's approach, there is consensual subordination under the LBHI2 Sub-Debt agreements but *pari passu* ranking as a matter of law under the LBHI2 Sub-Notes, there is no obvious reason to favour one outcome over the other. A contractual provision will displace default *pari passu* ranking. But, on the Judge's reasoning, the LBHI2 Sub-Notes contain no such contractual displacement provision. Had that point arisen

[43] See SLP3 skeleton [42(2)] fn 59 ([CB1/7/70]).

for determination, it would have been necessary to find a principled reason to arrive at a conclusion which reconciled the terms of two conflicting agreements.

37. Hence, the Judge's finding that Claim B historically ranked senior to Claim A was erroneous on its own terms. More broadly, however, the Judge's approach to this question was itself flawed. The correct answer, which the Judge ought to have reached, is that Claim A ranked senior to Claim B by reference to the unamended LBHI2 Sub-Notes. This is for the following reasons:

38. First, it is the result which is mandated by the operation of the solvency condition in the unamended LBHI2 Sub-Notes. As indicated above (paragraphs 21 to 25), two independent conditions must be satisfied before payment of Claim B is possible. The first is the "*cash flow*" condition requiring that LBHI2 be able to pay its debts as they fall due. There is no exclusion from this condition of other subordinated debts such as Claim A. The consequence is that Claim B is in practice subordinated to the lowest level of due debts (i.e. lower than any other debt which did not have an equivalent condition to payment). That is what the words say and is the only conclusion available if the words are to be given their plain meaning. The absence of a similar condition in the LBHI2 Sub-Debt Agreements means that the LBHI2 Sub-Debt must be paid first. This is not in any way inconsistent with the regulatory scheme or otherwise uncommercial. The Judge's error was that, having decided that the cash flow condition did not operate as a once and for all trigger (with which PLC agrees) the Judge then failed to give any meaning or effect to the condition.

39. Further, the same result is reached whether the LBHI2 Sub-Debt agreements and the LBHI2 Sub-Notes each contain two separate subordination provisions (as the Judge found) or a single operative provision derived from the solvency condition. The cash flow condition in the LBHI2 Sub-Notes is, on its terms, an expression of juniority over all other due debts. Although Claim A is not expressly referred to in the LBHI2 Sub-Notes, it falls within the description of "*its debts*". Accordingly, Claim B is, under the LBHI2 Sub-Notes, expressed to rank junior to Claim A. For that reason, under the LBHI2 Sub-Debt agreements, Claim B is an Excluded Liability and so not a Senior Liability to which Claim A is subordinated, and Claim A ranks ahead of Claim B. And Claim A is a Senior Creditor to which Claim B is subordinated and so ranks behind under the LBHI2 Sub-Notes. In other words, the distinct and operational cash flow condition in the LBHI2 Sub-Notes, as an expression of juniority, enables both agreements to reach the same outcome under both simple contractual subordination and contingent debt subordination, if that is the right analysis.

40. Second, and even leaving aside the operation of the cash flow condition, the remainder of the terms of the instruments point to Claim A ranking ahead of Claim B. The LBHI2 Sub-Notes expressly envisage the subordination of Claim B to other subordinated debt, whereas there is no similar provision in the LBHI2 Sub-Debt agreements, which contain no clear or express reference to their relative ranking position vis-a-vis any other subordinated debt. When applying two cross-referential structures, this is a notable difference between the LBHI2 Sub-Debt agreements and the LBHI2 Sub-Notes. The LBHI2 Sub-Notes overtly

provide for their subordination to other subordinated debt, unless this position is expressly reversed in the referred instrument. The LBHI2 Sub-Debt agreements make no express provision for their position as against other subordinated debt and so do not expressly reverse the subordination created in the LBHI2 Sub-Notes. Claim A is under the LBHI2 Sub-Notes a subordinated creditor which is also a Senior Creditor, which means that Claim B is an Excluded Liability under the LBHI2 Sub-Debt agreements.

41. Third, the timeline favours this construction. As at the date of the LBHI2 Sub-Debt agreements, the LBHI2 Sub-Notes did not exist. The wording in those agreements ("*expressed to*") was therefore a reference to possible future debt. By the time of the LBHI2 Sub-Notes, in contrast, the LBHI2 Sub-Debt was already in existence. Hence, the subordination provisions in the LBHI2 Sub-Notes were directed to the existing subordinated debt as well as to any future debts. The drafting technique in the LBHI2 Sub-Notes creates default subordination to other subordinated debt, unless it falls within the proviso specified. The LBHI2 Sub-Notes make no reference to the extant subordinated debt owed under the LBHI2 Sub-Debt agreements as falling within the proviso.

42. SLP3 argues for *pari passu* ranking. Even before addressing its points, it should be noted that SLP3 has said nothing about the cash flow condition in the LBHI2 Sub-Notes. It is not easy to see how SLP3 can advance a case on ranking without addressing this point. Recognising that it needed to deal with that condition, SLP3's submission at trial was that the words, "*its debts*", meant "*the debts of the Senior Creditors"*,[44] but there is no basis for reading those words in that way. Furthermore there is a clear contrast between the cash flow condition at 3(b)(i) and the balance sheet condition at 3(b)(ii). In the latter sub-clause, there are expressly excluded *'Liabilities to persons who are not Senior Creditors'*. Where the wording draws a specific contrast between the composition of two conditions in the same paragraph, there is no warrant for concluding that they were intended to mean the same thing. Perhaps recognising the weakness of this implication case, SLP3 simply ignores the cash flow condition in its appeal skeleton.

43. As for the points which SLP3 does advance, it first contends (SLP3 skeleton [37]-[44] ([CB1/7/69-71])) that, if the Judge had correctly applied what he stated to be his own approach, then he would have concluded that the subordination provisions in the LBHI2 Sub-Debt agreements and the LBHI2 Sub-Notes were ineffective *inter se* and that therefore the default rule of *pari passu* should apply by operation of law. This was not an argument advanced by SLP3 at trial and is not consistent with any of its stated reasoning. The criticism levelled at the Judge is that he adopted what SLP3 describes as a "Conjunctive Construction"[45]. This is unfair. At Judgment [175], the Judge (correctly) stated that he should not construe the LBHI2 Sub-Debt agreements and the LBHI2 Sub-Notes together, in the absence of any "network" agreement involving multiple creditors. However, he went on to note at Judgment [176] that, whilst he would examine each

[44] Day 6/90.2-4 [SB2/56/591].

[45] SLP3 skeleton [32] ([CB1/7/67]).

agreement separately, this might require looking to the provisions of other agreements, given their cross-referral nature. That is exactly what he then did.

44. This criticism is developed at SLP3 skeleton [37]-[44] ([CB1/7/69-71]). As understood, it is said that, when determining, for example, whether Claim B was an Excluded Liability under the LBHI2 Sub-Debt agreements, the Judge should not have asked (as he did) whether Claim A was a Senior Liability under the LBHI2 Sub-Notes. However, the Judge did not thereby fall into the alleged error of construing the agreements together. This was simply a product of the cross-referral provisions. The Judge did not use the LBHI2 Sub-Notes to determine the meaning of the LBHI2 Sub-Debt agreements. He only looked to the LBHI2 Sub-Notes to determine whether Claim B was a Subordinated, Excluded or Senior Liability under the LBHI2 Sub-Debt agreements, because that is what the LBHI2 Sub-Debt agreements required.

45. At SLP3 skeleton [42] ([CB1/7/70]), it is baldly asserted that the Judge should have found that, under the LBHI2 Sub-Debt agreements, Claim B was not an Excluded Liability "*because the terms of Claim B do not expressly rank it junior to Claim A, having regard to those terms but without construing Claim A within Claim B.*" But, because the LBHI2 Sub-Notes also adopt a cross-referral drafting technique, it is necessary to follow that technique through before any conclusion can be reached as to whether the terms of the LBHI2 Sub-Notes do or do not rank Claim B junior to Claim A. SLP3's approach seems simply to be to stop the exercise at an arbitrary and early point, and therefore to disapply the cross-referral terms. Applying those terms on their face (as the Judge did and was required to do) is not the same as construing the two agreements as if they were one.

46. In any event, in the absence of an articulated case by SLP3 in respect of the effect of the cash flow condition in the LBHI2 Sub-Notes, it is difficult to see where this argument is thought to go. For the reasons explained above, the cash flow condition was a clear expression in the LBHI2 Sub-Notes of the juniority of Claim B to Claim A. Even on the rather narrow approach to construction advanced by SLP3, effect would have to be given to that expression.

47. By way of second submission, SLP3 advances its own case on the ranking issue (SLP3 skeleton [45]-[49] ([CB1/7/71-74])), largely on the same basis advanced before the Judge. This may be taken in stages. At SLP3 skeleton [46] ([CB1/7/71]), and apparently as an overriding point, SLP3 contends that the Judge ought to have asked "*after which senior liabilities has the subordinated debt agreed to prove?*" But this question encapsulates underlying flaws in the SLP3 approach. As explained above, the question for the Court is about ranking between competing debts; SLP3's focus on proving as a matter of insolvency process is unnecessary and potentially misleading. More fundamentally, and as explained further below, it is not enough simply to rely on the fact of common senior creditors without engaging with the contractual position *inter se*. In seeking some sort of short cut to the answer, SLP3 persistently fails to undertake (or seeks to circumvent) the necessary process of construction.

48. At SLP3 skeleton [47] ([CB1/7/71-72]), it is said that the "*default*" of *pari passu* should pertain "*in the absence of clear and unequivocal language*". This is a recapitulation of the argument before the Judge, which is unsupported by any authority, or indeed principle. For the reasons explained above, *pari passu* may or may not be the conclusion (PLC submits that it is not). But the existence of a default is not the same as a presumption.

49. At SLP3 skeleton [48] ([CB1/7/72-73]), certain arguments are advanced in support of *pari passu* ranking. The premise of this paragraph is the assertion that the Judge "*apparently*" construed the LBHI2 Sub-Debt agreements and the LBHI2 Sub-Notes as precluding Claim A and Claim B from ranking *pari passu* with other subordinated creditors. It is correct that the Judge concluded that the terms of the LBHI2 Sub-Debt agreements did not allow for *pari passu* ranking (see further below). But he made no such finding in respect of the LBHI2 Sub-Notes. Hence, the premise of this paragraph is misplaced (and its relevance not understood in any event). Thereafter, SLP3 devotes its efforts to a submission that, for one reason or another, *pari passu* ranking should be at least possible. For the avoidance of doubt, PLC does not disagree with this contention at a level of abstraction. PLC does not need to contend that LBHI2 could not have agreed to a *pari* passu outcome. Its contention is that it did not do so.

50. SLP3's positive case on construction is at SLP3 skeleton [49] ([CB1/7/73-74]). The principal submission, as before the Judge, is the assertion that Claim A and Claim B are subordinated behind "*the same*" senior creditors, that the provisions are structured in "*materially the same way*" and that the subordination categories are "*entirely symmetrical*". Accordingly, so it is submitted, they must be ranked at the same level. As at trial, this is not a substitute for analysis:

    a. If the word "*same*" is intended to mean "*common*", then the statement is true in an irrelevant sense, in that both instruments are subordinated debt and hence have common senior creditors. The word "*symmetrical*" is to the same effect. That both Claim A and Claim B are subordinated to the same population of unsubordinated creditors could be said to create a "*symmetry*" of sorts. But none of this touches on the only relevant question, as to their relative ranking *inter se*.

    b. If, on the other hand, the word "*same*" is intended to mean more than "*common*", namely that under each instrument the population of senior creditors (falling within the defined terms 'Senior Liabilities'/ 'Senior Creditors') is identical, then the statement simply assumes what it seeks to prove. The population of senior creditors is identical only if, pursuant to the process of construction, it is concluded that the instruments rank *pari passu inter se*. Hence, this is not a premise but a conclusion. That conclusion can be reached only by construing the words of the agreements in order to determine the agreed ranking position. If that exercise is undertaken, then the purported premise is unnecessary. If it is not undertaken then it is unjustified.

c. The gap in SLP3's reasoning can be seen in the false syllogism at SLP3 skeleton [21(1)] ([CB1/7/62]). It is said that, "*if A subordinates its debt to C, and B subordinates its debt to C, A and B will prove at the same time and will rank pari passu.*" But this ignores the necessary enquiry whether A or B subordinates its debts to the other. That is determined as a matter of construction of the agreements. It is not concluded merely because both A and B have common senior creditors.

51. Third, at SLP3 skeleton [50]-[54] ([CB1/7/74-75]), SLP3 seeks to pray in aid supposed assistance from the factual matrix. This is misguided. As submitted above, the Judge was right to restrict relevant evidence of factual matrix (although none of this ultimately makes any difference to the construction of the terms actually agreed). SLP3's first case is that the "*relevant audience*" was the "*centralised decision makers*" within Lehman. It is alleged that the Judge failed to give weight to the supposed facts that there was "*never any intention*" to transfer the LBHI2 Sub-Notes out of the Lehman Group and that the terms of the LBHI2 Sub-Notes were not public. Such assertions cannot broaden out the admissible factual matrix.

a. The determination of the applicable factual matrix must itself be an objective question, based on the nature of the instruments themselves. The LBHI2 Sub-Notes were created as negotiable instruments listed on the CISX. Hence they must be construed on their terms for the reasons explained above.

b. SLP3's submission at SLP3 skeleton [51] ([CB1/7/74]) that "*there was never any intention*" to transfer the LBHI2 Sub-Notes out of Lehman itself betrays the flaw in its case. That is a reference to subjective intent. The proper ambit of the factual matrix cannot be influenced by subjective intent. The ambit of available material for the construction exercise, and indeed the correct interpretation of the LBHI2 Sub-Notes, cannot be dependent on an internal view as to whether and if so how they intended to deploy the negotiability of the instruments.

c. In any event, and even if such material were admissible or relevant, the evidence given at trial undermined SLP3's case. Ms Hutcherson expressly confirmed that there was never any commitment that intentions would not change, i.e. the listed and negotiable status of the LBHI2 Sub-Notes could be utilised at a later date[46].

52. On the premise of this first case, it is then alleged (SLP3 skeleton [52] ([CB1/7/74-75])) that the "*purpose*" of the transaction was to refinance existing LBHI2 Sub-Debt "*on materially the same commercial terms*", which debt had itself been *pari passu*. However, the purpose of the LBHI2 Sub-Notes was as stated on the face of the instrument, under the heading "Use of Proceeds". Whilst that includes the paying off of existing loans, it says nothing about the terms on which the refinancing was to be effected. If there were any purpose beyond that, this could be derived only from the terms of the instrument, as properly construed. Hence

[46] Day 2/36.23-37.1 [SB2/50/540-541].

SLP3's assertion again assumes what it seeks to prove. In fact, the LBHI2 Sub-Notes were a different instrument, drafted on different terms, in respect of a different debt. SLP3's submission is really that the construction exercise carries some sort of presumption that the two instruments were intended to have the same order of ranking but there is no objective reason why that is so. The Judge was right to proceed on the basis that the answer lies in the construction of the words actually used.

53. SLP3's alternative submission (SLP3 skeleton [53] ([CB1/7/75])) is that other matters would have been generally known to the market, namely, (a) that the "*custom*" of the market was for *pari passu* ranking. But, as explained above, this carries no evidential weight at all; and (b) that the subordination provisions were based either on the standard form or language "*very similar*" to it. This is another bootstraps argument (which is also factually wrong as the LBHI2 Sub-Notes had their own language which was not replicated in the standard forms). The proper construction of the words used will determine the ranking issue, rather than a misplaced assertion that the words used are similar. For the reasons explained above, it is the material differences in the wording which results in the priority of Claim A over Claim B.

C. PRESENT RANKING

54. This was addressed at Judgment [199]-[253]. The Judge concluded that Claim A ranked ahead of Claim B, by reference to the amended LBHI2 Sub-Notes. The Judge reached the right conclusion for the reasons which he gave.

55. In terms of his overall approach, the Judge undertook to construe the amended LBHI2 Sub-Notes in accordance with their terms. He was correct to do so. Echoing its argument on historic ranking, SLP3 had sought to contend that the question for the Court, having reached its conclusions on historic ranking (which SLP3 contended was *pari passu*), was whether the amended form of LBHI2 Sub-Notes should be construed as effecting a change from the historic position. This was a faulty and ultimately futile submission:

    a. The task for the Court is to construe the contract as it stands, by reference to its current and therefore amended wording. Provided the construction exercise is properly directed to the amended contract, there is no scope for injecting into the exercise the different question of whether the current amended wording was intended to make a change to original and historic wording. Further, the danger is that, by asking whether there was an intention to change, the focus slips into a consideration of subjective intent.

    b. If and insofar as it is a legitimate question, an objective analysis does not assist SLP3. The amendments substantially revised the terms of Clause 3 of the LBHI2 Sub-Notes and (as explained below) entirely replaced a major element of the contingent debt subordination provision. Objectively, the broad nature of the amendments plainly signalled an intended change to "Status and Subordination" under Clause 3. There is certainly no basis for a presumption that there was no intent to change the "*status quo*" whatever

that was. Ultimately, the answer is derived by an objective interpretation of the words actually used, as the Judge said.

56. At Judgment [201]-[215], the Judge recorded the process that led to the amendments. This was by way of background and could not otherwise have formed part of the factual matrix. Insofar as such material was admissible for this purpose, it has no material bearing on the ranking issue. Further, the fact that the Judge went on to find (in the context of the rectification claim) that there was no evidence of a mistaken common subjective intent, and indeed no manifestation of outward accord, renders either impossible or inherently unlikely the prospect of factual matrix evidence displacing the objective meaning of the words used.

57. As for the operation of the amended LBHI2 Sub-Notes, the Judge's conclusions were clear and correct:

a. Judgment [216]: the effect of the amendments was to insert a new subordination provision which interposed a different contingency. The new provision provides an alternative and hence mutually exclusive regime. Outside a formal insolvency process, the existing (and unamended) solvency condition still applies. However, within an insolvency process, that solvency condition no longer applies. Instead, the new regime articulated in the amendments applies.

b. Judgment [218]-[220]: The "*Explanatory Note"* is equivalent to a recital, such that the Court should construe the operative terms of clause 3(a), in the light of the Explanatory Note. As confirmed in the passage from *Chitty*, cited at Judgment [219], clear words in the operative part of an instrument cannot be controlled by recitals.

c. Judgment [226]-[231]: the new regime[47] makes the entitlement to payment on Claim B determined by reference to new terms. By those terms, Claim B is to be paid as if, and hence at the level for ranking purposes of, the holder of a class of preference shares with certain characteristics. Those characteristics are:

i. Payment above all other classes of issued shares.

ii. Payment above Notional Holders, which are creditors whose rights of payment are themselves subordinated to a notional preference share level. (There were not in fact any Notional Holders and so this category is purely hypothetical).

iii. Otherwise, payment below all debt (save for any debt with a similar subordination provision) because, by definition, payment at a notional preference share level must fall below payment at debt level.

[47] At Judgment [221]-[225], the Judge held that the new regime potentially applies in administration as much as winding up. The contrary had been argued by SLP3 but the point is not pursued on appeal.

d. Whether or not (as the Judge observed at Judgment [231]) an alteration of ranking (on his analysis of the unamended LBHI2 Sub-Notes) might with the benefit of hindsight be regarded as surprising, this was ultimately of no consequence. The terms of the amended LBHI2 Sub-Notes were "*unequivocal*", once the process of construction had been followed through.

58. SLP3 cannot contend that the drafting technique of subordination by relegating a debt payment to a preference share level was unusual or inoperative or ineffective. It was a technique specifically used by Lehman for ranking purposes in respect of the PLC guarantees[48] which, it was common ground, subordinated those guarantees below other subordinated debt. There was also contemporaneous evidence as to the use of such a technique[49]. At all events, the Judge considered that the meaning of the provision was "*very clear*" (Judgment [231]). PLC submits that the terms are indeed clear and that there is no other available alternative, in circumstances in which:

a. The new ranking regime is overtly directed to the ranking of the LBHI2 Sub-Notes. Clause 3 is headed "Status and Subordination". Further, this is clear from its function as a partial replacement of the solvency condition, which is itself a means of subordination.

b. Furthermore, the operative provision states that the metric for payment is that of the holder of a class of preference shares having a right of return *"over*" the holders of issued shares and Notional Holders. Accordingly the provision is aimed directly at ranking and priority in a winding up.

c. The ranking placement is clear and, as the Judge said, unequivocal. It is a deeming provision, to the effect that, on the application of the waterfall, the claims of Noteholders are to be treated, not at the priority level of debt claims, but at the priority level of claims by preference shareholders imbued with certain characteristics.

d. Of necessity, this provision affects priorities because creditors and shareholders stand in a different place in the waterfall. By deeming the Noteholder claims to be equivalent to those of notional preference shareholders, and making payable only such amount as "*would have been payable*" if they held preference shares within the definition, the amendment relegates Noteholder claims behind all other creditors (other than Notional Holders, if there are any, [which there were not), including all other subordinated creditors.

[48] [CB3/50/892].

[49] In an email dated 17 February 2005 [SB2/20/408-409]], Mr Miller had referred to the technique as providing a "*benchmark*" on liquidation, which would lead to a debt being "*ultra-subordinated*".

e. The overriding characteristic of a preference share is that it ranks below debt. This was expressly accepted at the trial by SLP3[50]. By ranking the LBHI2 Sub-Notes at the level of described preference shares, the amendments were setting both a floor and a ceiling to the ranking of the LBHI2 Sub-Notes in a winding up: they would be above shareholders and Notional Holders but otherwise below debt.

f. This is confirmed also by the final assumption at the end of the paragraph that such preference share "*was entitled to receive, on a return of assets in such winding up"* amounts of principal plus interest. All other debt payments, including under the LBHI2 Sub-Debt agreements, fall due before, and hence in priority to, any "*return of assets*" to shareholders or creditors entitled to payment at shareholder level.

g. Of course, this does not transform the LBHI2 Sub-Notes into actual preference shares, but it deems them to lie at a preference share level for the purpose of a distribution in a winding up or other insolvency process. It was not disputed, at least between the parties, that, all other things being equal, preference share level comes after debt level in any insolvency waterfall. SLP3 itself cited in its Written Opening[51] both the classic description of the waterfall by Lord Neuberger in *Re Nortel GmbH*[52] (where shareholders are at the bottom) and the similar statement to that effect by Lewison LJ in *Waterfall I* (CA)[53]. And at [256(4)] [SB1/8/173] (referring to the agreed position in respect of the PLC Guarantees), SLP3 correctly described that claim as "*so deeply subordinated in an insolvency of PLC that their claims rank pari passu with the non-cumulative preference shares."*

h. This outcome is also consistent with the Explanatory Note, declaratory in its effect, namely that the Noteholders are to have a right to a return of assets in the winding up in priority over (and, so no more than just over) shareholders for regulatory capital purposes qualifying as upper Tier 2 or Tier 1. As dated instruments, Claim A could only qualify either as lower tier 2 capital or as tier 3 capital[54]. Had there been any intention to rank Claim B *pari passu* with Claim A, this could easily and may be expected to have been made clear in this paragraph.

59. Further, there is nothing uncommercial about ranking subordinated debt such as the LBHI2 Sub-Notes at preference share level (and thereby changing the ranking status of that debt). This is clear from the willingness of LBIE to convert large amounts of subordinated debt into actual preference shares. As

[50] SLP3 oral closing [Day 6/119.21-2] "*On no view would an actual preference share ever have a right of return over a creditor in a winding up."* [SB2/56/592].

[51] At [386(2)] [SB1/8/201-202].

[52] [2013] UKSC 52, [2014] AC 209, at [39].

[53] [2015] EWCA Civ 485, [2016] Ch 50, at [60].

[54] GENPRU 2.2.11G, 2.2.12G, 2.2.157G, 2.2.159R, 2.2.177R, 2.2.194R.

recorded in *Waterfall I* (HC) at [29] and [30], LBIE replaced a total of $7.1 bn of subordinated debt with preference shares in 2006 and 2007.

60. The Judge was accordingly right to reach the conclusions which he did as regards the ranking issue on the amended LBHI2 Sub-Notes. On PLC's preferred analysis of a single subordination provision, the answer is found exclusively in the new regime specified in the amendments. As the Judge found, however, the same answer arises on the dual subordination provision analysis:

    a. Judgment [233]-[240]: simple contractual subordination under the LBHI2 Sub-Debt agreements. As before, this requires a consideration of the terms of the LBHI2 Sub-Notes. Under those terms, as amended, the new regime means that Claim B is expressed to be junior to Claim A in a winding up. That means that, under the LBHI2 Sub-Debt agreements, Claim B is an Excluded Liability and so Claim A ranks senior to it.

    b. Judgment [241]-[242], as Claim B is an Excluded Liability under the LBHI2 Sub-Debt agreements, there is no difficulty with the operation of the contingent debt subordination in the LBHI2 Sub-Debt. This will enable Claim A to be paid ahead of Claim B.

    c. Judgment [243]: the new regime under the LBHI2 Sub-Notes pushes Claim B in a winding up below all other debt save for Notional Holders. The LBHI2 Sub-Debt contains no such deeming provision and PLC is not a Notional Holder. Accordingly, under the LBHI2 Sub-Notes, Claim B ranks junior to Claim A.

61. Accordingly, under both the LBHI2 Sub-Debt agreements and the amended LBHI2 Sub-Notes, Claim A ranks ahead of Claim B. There is no inconsistency and no circuity, hence no need to reach for an implied term or some other solution because there is no deadlock to break. The contracts determine the relative ranking of the instruments and so the default *pari passu* regime is not engaged. The administrators of LBHI2 should distribute in accordance with the contractually agreed position.

62. At SLP3 skeleton [56]-[57] ([CB1/7/76]), it is suggested that the Judge would have reached a conclusion of *pari passu* ranking had he properly applied his own approach. To the extent that this advances a separate argument, PLC disagrees with it. But the Judge correctly applied the right approach for the reasons given above.

63. At SLP3 skeleton [58]-[64] ([CB1/7/76-80]), SLP3 advances its own case on the ranking issue. It contends that the Judge's determination of the present ranking issue was wrong as a matter of construction. The broad case advanced is that (a) Claim A and Claim B were historically ranked *pari passu*; and (b) this did not change as a result of the amendments to the LBHI2 Sub-Notes, largely because the wording of the definition of "*Senior Creditors*" did not change. The detail of this argument is addressed below but, as understood, the entirety of SLP3's case is premised on the historic ranking being *pari passu*. SLP3 has no case (and its appeal

must necessarily fail) in the event that, as submitted above, Claim A historically ranked ahead of Claim B. The remainder of this section of the skeleton accordingly assumes, as a hypothesis for the purpose of the argument only, that Claim A did not historically rank ahead of Claim B.

64. The core submission, at SLP3 skeleton [58] ([CB1/7/76]), is that the amended LBHI2 Sub-Notes "*remained subordinated to the same Senior Creditors"* and therefore relative ranking "*was unchanged*". However, SLP3's approach in this regard is erroneous principally for two reasons:

    a. As submitted above, the task of the Court is to construe the wording as it stands, in this case by reference to the amended LBHI2 Sub-Notes. Whether the ranking has "*changed*" (in the course of the rewriting of the ranking provisions) is a conclusion reached after the exercise has been properly conducted. It is not a question which drives the construction exercise.

    b. In any event, SLP3's approach is self-servingly narrow. If the question is, has the wording of the section changed, the answer is yes, it has very substantially changed. In such circumstances, it is not helpful to focus on the fact that the words comprising the definition of Senior Creditors have not changed. In neither unamended nor amended form is there a fixed identity of the population of Senior Creditors. It is an umbrella term for those creditors which, upon the proper construction of the substantive provisions of the LBHI2 Sub-Notes, rank ahead of Claim B. If the substantive provisions have changed, the fact that the words making up the definition of the term "Senior Creditors" remain unchanged is of very little significance on the construction question. It is perfectly possible for there to be a different population of Senior Creditors both before and after amendment. As Lord Neuberger observed in *Waterfall I* (SC) at [50], "*The fact that an expression has a single meaning self-evidently does not prevent it from producing different outcomes in different circumstances."* The answer lies in the construction of the substantive provisions, not in the definitions.

    c. Nor does PLC accept the claim made by SLP3 that the "*key subordination wordin*g" remains unchanged. This is just forensic assertion. The relevant section of the LBHI2 Sub-Notes falls to be construed as a whole without *a priori* assumptions as to which bits are "*key*". However, if there is to be some form of hierarchy, the specific implementing provision dealing expressly and precisely with the ranking of payments on a winding up (or administration) is more deserving of the epithet "*key*". This provision has very substantially changed.

65. As for the detailed criticism of the Judge's findings:

    a. At SLP3 skeleton [60] ([CB1/7/77-78]), there is a long paragraph which appears to criticise the Judge for applying the new subordination provision at all. Instead, so it is said, he ought just to have given effect to the unchanged definition of "*Senior Creditors*". But, other than resting on the fact that the wording of the definition has not changed, SLP3 offers no explanation of how the new subordination

provision could on its case be given meaning. On the basis of no or no obvious rationale it seeks to downgrade the new condition by describing it as a "*payability condition*". What this is supposed to mean is not clear (especially when determining when something is 'payable' is the means of determining its ranking). But, ultimately, SLP3's case can only be that it should be ignored. The principal difficulty facing SLP3 at trial and on appeal is that it cannot find a credible meaning to the amendments which helps its case.

b. At SLP3 skeleton [61] ([CB1/7/78-79]), it is said that the Judge ought to have concluded that the new subordination provision worked only from the "*bottom up*" rather than the "*top down*". But this is an impossible interpretation as it is not what the amendment says. The deemed status for payment purposes as a species of preference shareholders carries both a floor and a ceiling. It is this conscious and overt deeming provision which confirms the subordination of Claim B to Claim A.

c. SLP3 skeleton [62] ([CB1/7/79-80]) criticises the Judge's approach to the Confirmatory Note but there was no error in this, for the reasons explained above.

d. At SLP3 skeleton [63] ([CB1/7/80]), it is said that the Judge failed to check his conclusion against the provisions of the contract and their commercial consequences. The main point which is made is the submission that different ranking conclusions might on the Judge's approach follow depending on whether LBHI2 was in a winding up or not. It is not accepted that the Judge failed to check the rival constructions. However, where, as in this case, the wording is clear, then so is the answer, especially when the only rival constructions were that the wording should be either ignored or contorted for no obvious purpose other than to achieve an outcome favourable to SLP3. Further where, as in this case, the instruments were drafted and amended within a complex regulatory and corporate environment, responding also to tax demands in multiple jurisdictions, it is dangerous and unsatisfactory to try to influence conclusions on construction by reference to a single supposed anomaly when it is impossible to recreate the full consequences of any particular construction. In any event, the supposed anomaly is largely illusory. Issues of ranking between species of subordinated debt would only in practice arise in a winding up or other insolvency process or other financially constrained scenario (this being, of course, the whole reason and context for the scheme of regulatory capital[55]) and so there is no true comparison to be made.

66. At SLP3 skeleton [65]-[68] ([CB1/7/80-81]), SLP3 advances some further arguments based on factual matrix. As with the earlier arguments, the primary arguments are unfounded as a matter of principle because

[55] See e.g. the references in *Waterfall I* (HC) at [37] and [40] to the Council Directives implementing the Basel I and Basel II, which defined the requirement for regulatory capital as the subordination of debt "in the event of the bankruptcy or liquidation of the credit institution."

the scope for factual matrix in respect of the construction of the amended LBHI2 Sub-Notes is as narrow as for the construction of the unamended LBHI2 Sub-Notes. Even putting that to one side, the points raised are themselves erroneous or insignificant:

a. It is said that the "*purpose*" of the amendments was to defer the cash settlement of interest on the LBHI2 Sub-Notes. This was not stated on the face of the amended LBHI2 Sub-Notes. On the contrary, it is plain on the face of the amendments that their purpose was not limited to the deferral of interest. Further if (as seems to be SLP3's premise) it is permissible to take account of internal Lehman documents to discern the "*purpose*" (which it is not), it is again absolutely plain that the purpose of the amendments was not limited to the deferral of interest. This is apparent from the examination of the rectification claim, below. SLP3 consistently fails to distinguish between the genesis of the amendment process (which was the deferral of interest) and the purpose of the amendments as drafted (which was much wider).

b. SLP3 then contends that the Judge gave no weight to the (alleged) historic *pari passu* ranking. It is technically correct that he did give no weight to prior *pari passu* ranking because he had concluded that Claim B ranked ahead of Claim A. It is clear that he gave that (erroneous) finding full consideration (see Judgment [231]) but nevertheless "*could not abandon the very clear meaning*" of the amended LBHI2 Sub-Notes.

D. THE RANKING OF CLAIMS A(i), A(ii) AND A(iii) *INTER SE*

67. At Judgment [245]-[250], the Judge returned to the ranking of Claims A(i), A(ii) and (iii) *inter se*. The factual background here is that: (a) Judgment [11]: there were 3 LBHI2 Sub-Debt agreements, each dated 1 November 2006, between the same parties (LBHI2 and PLC); (b) Judgment [133]: each was drafted on FSA standard forms and on exactly the same terms as regards subordination; and (c) whilst the overall balance on the LBHI2 Sub-Debt was identifiable, there was no evidence before the Court as to whether and if so how that balance was broken down between the agreements. Indeed, the indication from the administrators of LBHI2 and PLC after the draft Judgment had been circulated was that this had not been established on the Lehman records and might never be capable of being established: Judgment [188(1)].

68. Under the terms of each LBHI2 Sub-Debt agreement, Liabilities can be only one of Senior, Subordinated or Excluded. The Judge concluded that Subordinated Liabilities were confined to the Liabilities (if established) under the particular LBHI2 Sub-Debt agreement in question. For example, for the purpose of the LBHI2 Sub-Debt agreement for Claim A(i), Claims A(ii) and A(iii) could not be Subordinated Liabilities. That meant that Claims A(ii) and A(iii) would have to be either Senior Liabilities or Excluded Liabilities. The Judge concluded (Judgment [151]) that they must be Senior Liabilities. The same would apply, *mutatis mutandis*, under the LBHI2 Sub-Debt agreements for Claims A(ii) and A(iii). It was this analysis which led to what the Judge described as a "*race to the bottom*" (Judgment [152]) and which he then resolved (Judgment

[248]-[250]) by determining that these were, *inter se*, ineffective subordination provisions and that the default ranking of *pari passu* should apply in that case.

69. The Judge concluded at Judgment [252] that this analysis had no bearing on the ranking issue as between Claim A and Claim B, where there was no similar "*endless loop*". That was plainly correct. If, as the Judge found, there is no similar issue of circularity as between Claim A and Claim B, then the specific and unusual problem raised by the interaction of Claims A(i), (ii) and (iii) does not arise. Nevertheless, and as became apparent in the further hearing after the draft Judgment was circulated, the Judge's finding that Claims A(ii) and A(iii) were Senior Liabilities under Claim A(i) (and vice versa) required consideration to be given to the operation of the solvency condition in the LBHI2 Sub-Debt agreements. If balances under Claim A(ii) and A(iii) were Senior Liabilities under the LBHI2 Sub-Debt agreement for Claim A(i), did that mean that they would not be disregarded for the purpose of the solvency condition at paragraph 5(2)? If they were not to be disregarded, then that might, depending on how the numbers fell, impede distributions.

70. No party suggested that the administrators of LBHI2 should be precluded from making payment to PLC under, for example, Claim A(i) because and only because of the existence of balances on Claims A(ii) and A(iii). All recognised that that would be an absurd outcome, not least because it would tie up funds in the estate, potentially for ever. The Judge amended the draft Judgment after receiving further submissions on the point by finding (at Judgment [186]-[189], [241] and [253]) that, for the purpose of the operation of the solvency condition in the LBHI2 Sub-Debt agreements, debts which are as a matter of law *pari passu inter se* (namely, in this case, Claims A(i), (ii) and (iii)), should be treated as the same claim.

71. The result of all of this is that the Judge's analysis of Claims A(i), (ii) and (iii) has no bearing on any aspect of the ranking issue between Claim A and Claim B. PLC is accordingly content for that analysis to stand. However, it does consider, to the extent helpful, that the better analysis is that each of Claims A(i), (ii) and (iii) are Subordinated Liabilities under the other LBHI2 Sub-Debt agreements, either by way of construction or implied term. Each agreement purports to provide an exclusive categorisation of all other debts into one of Senior, Subordinated or Excluded. It is plain (and, it seems, all parties and the Judge agree) that these debts could only possibly rank *pari passu inter se*, as under loan agreements between the same parties on the same date for the same regulatory purpose and, so far as material, on the same terms (all of which is admissible factual matrix when construing each). The Judge's approach, which involved construing the agreements in a way which arrived at an impossible conclusion (namely that the debt under each LBHI2 Sub-Debt Agreement was a Senior Liability under each other LBHI2 Sub-Debt Agreement) and then disapplying that conclusion because it was impossible, hints at an error of approach. This is a case where the construction of the agreements must yield to business common sense[56]. Alternatively, an implication

[56] *Antaios Cia Naviera SA v Salen Rederierna AB* [1985] AC 191, at 201.

would satisfy the stringent test for the implication of terms[57]. The solution proposed by PLC involves minimal disruption to the words actually used and produces a result where (unlike the Judge's) the contractual position is at one with the legal outcome.

72. Further, even if the Judge was right to conclude that, as between Claims A(i), A(ii) and A(iii), the contractual subordination provisions were ineffective and that those debts revert to *pari passu* as a matter of law, there is a simpler and more principled solution to the operation of the solvency condition in the LBHI2 Sub-Debt agreements. Again, by way of either construction or implied term, there should be disregarded Liabilities which do in fact rank *pari passu*, or alternatively all such Liabilities should be treated as a single debt. At Judgment [253(5)], the Judge acknowledged that an implied term was "*an alternative potential solution"* but considered that the solution instead arose "*by operation of law*". However, given that, at this stage of the argument, the question is how to apply the solvency condition in the LBHI2 Sub-Debt agreements, a solution under the agreements themselves is more natural.

E. RECTIFICATION

E1. Introduction

73. SLP3's rectification appeal is a weak challenge to factual findings, in circumstances in which the decision-makers did not give evidence, the Judge found no mistake after oral evidence of the one relevant actor who did give such evidence (Ms Dolby), and there was no evidence that at the time a change to ranking (which is the necessary hypothesis of the rectification claim) (i) was of any importance, (ii) was a mistake, or (iii) would not have been made had it been fully understood. This was a claim for rectification based on subjective intention where no witness said there was a mistake and the state of mind of the decision-makers was unknown.

74. The chronology in relation to the 2008 Amendments was introduced in Judgment [203]-[215]. This was a $6bn instrument, the amendments to which were drafted by an expert firm of solicitors and reviewed by a number of senior tax, legal, and regulatory personnel at Lehman. The origin of the amendment process was the deferral of interest so as to achieve tax benefits. The first draft amendments sent by Mr Grant of A&O on 5 June 2008, noting that he had yet to run them past Mr Dehal of A&O, were limited and principally introduced a new clause 4(f), allowing for the deferral of interest.[58] On 12 June 2008, Mr Grant sent a second draft with wider amendments including substantial additions to clause 3(a) that removed the solvency condition and specified the subordination level of the LBHI2 Sub-Notes under the heading 'Status and

[57] *Marks & Spencer plc v BNP Paribas Securities Services Trust Co (Jersey) Ltd* [2015] UKSC 72, [2016] AC 742.

[58] [SB2/24/417-430].

Subordination'.[59] The amendments were effected on 3 September 2008, in substantially the form of the second draft, through various formal resolutions, minutes, certificates and consents, approved by Ms Upton and Mr Triolo of SLP3 and Mr Rush and Mr Jameson of LBHI2.[60]

E2. The legal requirement of a mistaken intention

75. Rectification requires a mistake such that the relevant document does not reflect the common intention.[61] There must be "*convincing proof*"[62] that the document is "*not what [the parties] meant*" to "*counteract the cogent evidence of the parties' intention displayed by the instrument itself*" and the inherent probability that the parties meant what they said[63]. The jurisdiction is one which must be "*cautiously watched and jealously exercised*".[64]

76. Leggatt LJ explained in *FSHC* (CA) at [147] that "*It is fundamental to the doctrine… that an actual mistake was made by one or more real people in believing that the written contract gave effect to what either was or was understood by one party to be the parties' actual common intention*". Hence (at [146]) rectification is justified where relying on the contract is against conscience "*because it is inconsistent with what both parties in fact intended (and mutually understood each other to intend) those terms to be when the document was executed.*" There must therefore be a positive belief or intention of the parties as to what the terms of the document were or did, or as to what they did not contain or do.

77. It is important to avoid elision between two possibilities. The first is a positive intention to effect change X, coupled with either a positive intention not to effect change Y or a positive intention not to effect any other changes (which category must include Y). This is required for rectification. The second possibility, of only having a positive intention to change X and having no intention either way as to Y (i.e. being unaware or indifferent or both), was not the position in this case but is in any event insufficient for rectification. Not intending to change Y is not the same as intending not to change Y.

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[59] [SB2/31/448-486].

[60] [CB3/42], [SB2/44/522-523; SB2/45/524; SB2/46/525; SB2/47/528].

[61] *FSHC Group Holdings Ltd v Glas Trust Corporation Ltd* [2019] EWCA Civ 1361, [2020] Ch 365 at [46], quoted by the Judge at Judgment [258(1)].

[62] *Swainland Builders Ltd v Freehold Properties Ltd* [2002] EWCA Civ 560 at [34]; *T&N Ltd v RSA plc* [2003] EWHC 1016 at [135]; *Chitty* [3-089]. See also *Etablissements Georges et Paul Levy v Adderley Navigation Co Panama SA (The Olympic Pride)* [1980] 2 Lloyd's Rep 67 per Mustill J at 72 emphasising that the court must be "*sure*".

[63] *Thomas Bates and Son Ltd v Wyndham's (Lingerie) Ltd* [1981] 1 WLR 505 at 521; *Tartsinis v Navona Management Co* [2015] EWHC 57 at [85]; *FSHC* at [186].

[64] *Whiteside v Whiteside* [1950] Ch 65 at 71 per Evershed MR.

78. If parties meant to include something in the document but forgot to do so, that is not sufficient mistake for rectification because there was no positive belief or intention that the document included the matter.[65] The same is true where the parties overlooked—did not appreciate—something in the document, i.e. had no intention either way as to the point. So, for example, in *Lloyd v Stanbury*, there was no rectification of a contract for the sale of land because the purchaser had not been interested in the precise boundaries, was content to leave their exact definition to his legal advisers and so had "*no positive intention*" that a disputed parcel of land (plot 1428) should be excluded from the sale[66]. Leggatt LJ in *FSHC* (CA) at [74] approved *Lloyd* as an illustration of how a claim for rectification can fail at the first hurdle "*for want of proof that the written contract was contrary to the actual intentions of the parties*".[67]

79. It remains unclear whether SLP3 agrees with or seeks to challenge the above propositions. This is because its case rests, as at trial, on linguistic ambiguity. At SLP3 skeleton [93(1)] ([CB1/7/89]), it is submitted that, if it can be shown that the relevant decision makers had a subjective intention *only* to make change X, then it "*necessarily follows*" that they did not intend to make change Y. But this only begs the question as to what is meant by "*only*". If the intention was to make change X and not to make change Y, then it is a correct statement of the law, if circular. If it was to make change X with no thought about change Y, then it is not.

80. As understood, the parties do, however, agree that there is no special rule for rectification of amendments, it is simply that in the case of some amendments the evidence may demonstrate a positive intention not to make change Y.[68] The feature of this being an amendment case was (i) plainly at the forefront of the Judge's mind (the terms 'amendment' and 'modification' are used dozens of times by the Judge), and (ii) not, contrary to SLP3's characterisation, a "*critical legal issue*" that the Judge erroneously failed to address (SLP3 skeleton [107] and [111(1)] ([CB1/7/92-93])).

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[65] *Chitty* [3-058]. Thus in *Olympia Sauna Shipping Co v Shinwa Kaiun Kaisha Ltd (The "Ypatia Halcoussi")* [1985] 2 Lloyd's Rep 364 at 370, a settlement agreement was not rectified so as to include the deduction of an overlooked balance in favour of the defendants because "*The defendants themselves, having unhappily forgotten all about the $74,000 balance, had no intention in regard to it at any relevant time before the compromise agreement.*"

[66] [1971] 1 WLR 535 at 544. A further example of clients knowing lawyers have made some provisions, and thus intending them without considering or discussing, or even reading, them, which SLP3 accepts is not enough for rectification [Day 6/147.8-14, 157.17-25], is found in *Lansing Linde Ltd v Alber* [2000] Pens LR 15.

[67] He went on at [84] to distinguish this requirement from the test for implied terms, citing from a decision of the High Court of Australia: "*The difference is that with rectification the term which has been omitted and should have been included was actually agreed upon; with implication the term is one which it is presumed the parties would have agreed upon had they turned their minds to it – it is not a term that they have actually agreed upon.*"

[68] SLP3 Rectification Closing p1 point labelled 'First' [SB1/14/330].

81. The absence of discussion about a change may be evidence to support the inference of a positive objective intention not to make the change, which is what Henry Carr J was considering in *FSHC* (HC)[69], and the same is probably true for subjective intention, although the inference is less clear.[70] Everything depends upon the circumstances but there is no dispute about this proposition of law, which the Judge correctly quoted at Judgment [259].

82. But what cannot be contended, and has no basis in law, is the suggestion[71] that when amending a contract any alteration or addition must be specifically read, considered and positively desired by the client, or ancillary to a change that was[72], otherwise it is necessarily a mistake such as could justify rectification, i.e. every amendment includes an intention not to implement any changes other than those expressly discussed. This may be what is contended in SLP3 Skeleton [93(1)] ([CB1/7/89]), although that remains unclear.[73] If it is contended, it is wrong as a matter of law and fact,[74] although in the present case the particular amendment was adverted to sufficiently that this proposition would not apply to this case anyway.

83. Thus in *FSHC* there was a positive subjective intention to do no more than grant the limited security over the shareholder loan. See e.g. (CA) at [4] per Leggatt LJ[75]: "*The judge also concluded that it was both objectively and*

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[69] *FSHC Group Holdings Ltd v Barclays Bank* [2018] EWHC 1558 (Ch).

[70] Henry Carr J's comments on this inference at (HC) [44-7] and Leggatt LJ's at (CA) [191] were made in relation to findings of objective intention, as SLP3 seems to accept at SLP3 Skeleton [98] ([CB1/7/90-91]).

[71] First made by SLP3 in Closing: [Day 6/147, 151, 154, 157-8] [SB2/56/593-596].

[72] SLP3 said that anything falling within a "*general instructions to make sure the [primary instructed change] works*" would also not be susceptible to rectification: [Day 6/149.2-10] [SB2/56/594].

[73] See also [Day 6/157-8] [SB2/56/596].

[74] The case law relied upon by SLP3 does not formulate any special rule of law for amendments. In *AMP (UK) plc v Barker*, as SLP3 says, Lawrence Collins J did not require AMP to show any actual consideration of change Y. But there is no unpacking by the learned Judge of the distinction set out above (only intending X, and intending only X), merely the finding quoted by SLP3 at [96] ([CB1/7/90]), which is best read as recording a positive intention not to make any other changes other than the one identified: [2001] Pens LR 77 at [67]. The *Univar UK Ltd v Smith* decision, also relied on by SLP3 at [96] ([CB1/7/90]), merely reaffirms that "*the intention not to make a specific change can be inferred from the absence of any evidence that there was an intention to make it"* [2020] EWHC 1596 (Ch) at [213], correctly emphasising the need for an intention not to Y although that can be inferred from lack of evidence of an intention to Y, and finding at [239] "*a positive subjective intent… to make no changes to the member benefits described on the face of the 1996 DDR other than changes required by the law* [i.e. X]" i.e. (at [240]) "*each of the Trustees proceeded on the basis that there were to be no changes of substance unless they were included in the schedule of changes (or were otherwise expressly authorised)*".

[75] See also at [42], [44] and [177].

subjectively the common intention of the parties to execute a document which satisfied the Parent's obligations to grant security over the shareholder loan and which did no more than this", or [42] "*their subjective intention was to do no more than provide third party security*". This satisfied the legal requirement referred to above. The emphasis throughout the judgment was on "*actual intentions*" [160], [164-6]. Thus, *Lloyd v Stanbury* was explicitly approved at [74] on the basis that rectification was refused there because there was "*no positive intention*".

84. Thus SLP3 needed to show, to the necessary standard of "*convincing proof*", that the decision makers positively intended to make no changes other than to defer interest. This did not, as contended at SLP3 Skeleton [108] ([CB1/7/93]), require SLP3 to prove a negative. And it is different from merely showing that the origin of the amendment process was the deferral of interest and/or that this was the only change to which the Lehman decision makers devoted their specific attention (although, to be clear, even that could not be shown on the evidence). The rectification claim failed not because the Judge applied the wrong test, but because he refused to draw the necessary inferences from the evidence, such as it was, which he heard.

E3. The factual findings

85. SLP3's case at trial was that the Judge should infer from the evidence an intention that all of the 2008 Amendments had a single purpose, namely to defer interest and *no more* (by which language SLP3 sought to equate the present case with the, as the Judge observed (Judgment [259], "*very different*" facts in *FSHC*). The Judge refused to draw such an inference and instead made the following findings of fact:

a. Relative subordination was a matter of indifference and was perceived as unimportant within Lehman. This was because it did not affect the regulatory capital position[76], was not relevant to tax,[77] insolvency was "*unthinkable*" (Ms Dolby's word[78]), and in any event in an insolvency subordinated creditors would not expect to be paid anyway: Judgment [262(3)-(4)]. Lehman had no reason to think about or seek advice about it.[79]

b. There was no subjective intention as to relative subordination, which did not cross anyone's minds: Judgment [262-(1)], [262(4)(d)], [264-5].

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[76] See paragraph 8 above.

[77] Dolby [Day 3/66.8-20 and 92.3-5] [SB2/54/561-562], Dolby interview 37.10-12 [SB1/4/72].

[78] Dolby WS at [68] [SB1/5/80-81], quoted at Judgment [262(4)(a)]. Also Hutcherson [Day 2/37.24-38.22] [SB2/50/541] and Hutcherson WS at [56]-[57] [SB1/6/96]; Dolby WS at [52]-[53] and [67] [SB1/5/77-78, 80] and [Day 3/67.10-15, 90.22-91.6] [SB2/54/561-562].

[79] Dolby WS at [52]-[53] and [67]-[68] [SB1/5/77-78, 80-81], Dolby interview 14.6-7 and 15.18-23 [SB1/4/49-50]. See also Hutcherson WS at [31], [56]-[57], [90] [SB1/6/90, 96, 103]; [Day 2/37.24-39.6] [SB2/50/541]; Hutcherson interview 22.21-28 and 19.33-4 [SB2/3/31, 34].

c. The Judge described the suggestion of a positive intention that relative subordination not change as "*fanciful*" [266]. Thus the Judge explicitly rejected such a case.

d. The only subjective intention was that reflected by the objective construction of the terms of the LBHI2 Sub-Notes as issued "*whatever that construction may have been*" (emphasis in original) [263] and [266-7] (also [264]). Thus the Judge found a positive intention to agree the amended terms as drafted.

86. It is not apparent from SLP3's skeleton that it challenges any of these findings of fact. Any such challenge would itself be fanciful. Yet, on the basis of such findings, the appeal must necessarily fail. The Judge was both entitled and right to reject SLP3's case. Indeed, the Judge went on to make the further finding (not necessary to reject the rectification claim but on its own fatal to it) that the relative ranking of subordinated debt would have been "a *matter of indifference*" if raised and would have been met with a "*resounding* '*So what?*'" from the Lehman Group [262(4)(d)]. This is stark. Contrast all the cases relied upon by SLP3 in which rectification was granted.

87. Because it has to, SLP3 challenges this '*So what'* finding, but without any serious basis for doing so[80]. This was a finding of fact by the Judge on the evidence before him. SLP3 relies on Ms Dolby's low key indications that she would likely have wanted to discuss the matter with the legal and regulatory departments. But the Judge was well aware of that evidence (he quoted it in the same paragraph). And that evidence stood in a broader context (explored more fully below). Even Mr Grant, called by SLP3 and re-examined on exactly this point, refused to say that, if the amendments changed the ranking, this was a mistake.[81] SLP3 does not get close to demonstrating a reason to interfere with the Judge's assessment of the evidence.

88. SLP3's case on appeal, as understood, is that there was other evidence which the Judge did not refer to and which, so it is suggested, ought to have caused him to arrive at the opposite conclusion from that which he found. But this is, with respect, hopeless.

89. First, the Judge's conclusions involved an evaluation of all of the evidence presented to him at trial. The circumstances in which such conclusions will be overturned on appeal are necessarily attenuated: see e.g. *Fage UK Ltd v Chobani UK Ltd*[82], *Biogen Inc v Medeva plc*[83].

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[80] Merely asserting groundlessly and wrongly that a change to ranking inter se of subordinated debt was a "*fundamental change*": SLP3 Skeleton [111(4)] ([CB1/7/94]), echoing the use of the same words in *FSHC* accurately to describe the mistaken change there.

[81] [Day 2/139.8-11] [SB2/52/552].

[82] [2014] EWCA Civ 5, [2014] FSR 29 at [114].

[83] [1997] RPC 1, at 45.

90. Second, the approach of the Judge is unassailable. If an issue is unimportant, the value of the absence of evidence of a discussion about it is likely to be slim. Especially after 11 years and with a limited number of witnesses, this was not even evidence of the absence of a discussion (and parties cannot be expected to remember discussing unimportant matters, although likely there were discussions here that the witnesses cannot remember[84]). But, even if it could be said to constitute such evidence, absence of a discussion of an unimportant issue is much weaker evidence from which to draw an inference, because it is much less obvious that parties will positively intend not to make unimportant changes without discussing them. SLP3's suggestion that some legal error was made here or that absence of discussion is universally or in this case material evidence of an actual intention (SLP3 skeleton [109[, [110], [111(4)] ([CB1/7/93-94])) is wrong. The Judge correctly considered the circumstances of this case after rightly distinguishing *FSHC* as factually very different[85].

91. Third, any suggestions (SLP3 Skeleton [80-2], [103-6], [113] and [117(1)] ([CB1/7/85, 91-92, 94, 95])) that the Judge did not take all the relevant evidence into account when making his decision on rectification is unfounded. There were a mere ten or twenty relevant communications to which Lehman were party relating to the amendment[86] and a single oral witness from Lehman (Ms Dolby). The Rectification Chronology handed up on Day 6 by SLP3 was not referred to in the Judgment (nor would a chronology usually be referred to) but the key matters within it were addressed exhaustively in the written submissions[87] and cross-examination.

92. Fourth, the Judge's findings pointed instead to the entirely commonplace situation where commercial parties are content to agree changes proposed by their lawyers, on the understanding that the amendments carry

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[84] Ms Dolby says she probably would have had conversations but cannot now remember any: [Day 3/92 and 106] [SB2/54/562, 566]. Mr Grant cannot recall whether he sought instructions from Ms McMorrow: Grant WS at [57] [SB1/1/20-21]; the documents refer to discussions taking place [SB2/28/444; SB2/31/448; SB2/32/498; SB2/33/499; SB2/36/513]. Hence Judgment [211].

[85] In *FSHC* (i) incurring the Additional Obligations represented a "*fundamental change*" to the existing arrangements (*FSHC* Carr J at [158]). It would have been "*commercially absurd*" and "*inconceivable*" (Carr J at [172-3], CA at [35 and 190]. (ii) The *FSHC* parties would never have acceded to the change had they been aware of it (Carr J at [166]). (iii) The amendment had in *FSHC* not been read by anyone (CA at [40]). (iv) All the relevant individuals gave evidence such that the matter was "*thrashed out*" in the witness box (Carr J at [82] and [133], CA [38]).

[86] SLP3's Rectification Chronology identifies 76 items but many merely note points of witness evidence or communications internal to A&O or are immaterial [SB1/12/291-313].

[87] E.g. SLP3 Written Opening [446] [SB1/8/215-218], PLC Written Opening [163] and [175] [SB1/10/255-257, 261-263], PLC Closing [143-155] and [168-9] [SB1/13/316-324, 327].

the meaning which the law attributes to them, without undertaking the intellectual process of reviewing or considering what that meaning was. But that could never support a case in rectification.

93. Fifth, the necessary premise of SLP3's case (which would not be sufficient even if established), namely that the parties did not appreciate that amendments were being made which went beyond the original purpose of the deferral of interest, was entirely unfounded. Indeed, such evidence as there was pointed firmly in the opposite direction.

    a. The terms of the LBHI2 Sub-Notes were only 10 pages long. The amended draft sent on 12 June 2008 showed the amendments in blue[88] and it would have been clear to all readers that they comprised (i) a complete rewrite of section 3 'Status and Subordination', disapplying the solvency condition in an insolvency situation and implementation of a deemed ranking as a preference share, (ii) changes to section 4 'Interest', (iii) minor changes to sections 5 and 8. Further, attention was drawn to the amendments with an explanation for the further amendments that "*a comparison showing the changes since the last draft you saw. Deferral provisions introduce tax sensitivities. The amendments are designed to ensure these sensitivities are met.*"[89]

    b. The draft amendments were sent to and seen by Ms Dolby (tax), Ms McMorrow (legal), Ms Dave (legal), Ms Upton (legal and one of the two ultimate decision-makers for SLP3), and also by subsequent forwarding to Ms Edwards and Mr Bowen (both regulatory/compliance),[90] and Mr Wiener and Ms Homer (both accounting)[91] at Lehman. As was apparent on their face, the amendments to clause 3 concerned the subordination and ranking of the LBHI2 Sub-Notes. Further, Mr Grant's explanation made clear that such amendments addressed a tax issue going beyond interest deferral.

    c. Ms Homer explicitly considered the ranking of the LBHI2 Sub-Notes pursuant to the proposed amendments in the context of the regulatory position, noting in her email of 28 August 2008: "*The Notes are intended to have a right to a return of assets in the winding up or dissolution of the Issuer in priority to the rights of the holders of any securities of the Issuer which qualify as Upper Tier 2 Capital or Tier 1 Capital. The Notes are only junior to Senior Creditors.*"[92]

94. Against this background, it mattered not that the amendments were summarised in the Board resolutions as being for the purpose of achieving interest deferral (which self-evidently, and as Mr Grant confirmed,

[88] [SB2/31/448-486].

[89] [SB2/31/448-486].

[90] [SB2/34/500], [SB2/36/513]; [SB2/37/514].

[91] [SB2/40/517], [SB2/41/518], [SB2/42/519].

[92] [SB2/41/518].

was a summary of the core commercial change not an exhaustive identification of all changes[93]). Hence also SLP3's case that there was a mistake because the parties '*only*' intended to defer interest is both (i) inadequate and ambiguous (as it does not entail an intention not to do more) and (ii) inapt to the present case where Ms Dolby (and assuming, for the moment, that as the only Lehman witness called on the point her intention is relevant) intended to make the changes proposed by the lawyers and read and considered by the parties. There was no challenge to Ms Dolby's evidence that:

> *"I relied on A&O and my legal colleagues to prepare the necessary documentation. So long as they were content that the amendments were necessary and appropriate, and did not impact the lower tier 2 status of the LBHI2 Sub-Notes, I had no particular reason to second guess their drafting. Sarah McMorrow or one of her legal department colleagues would similarly have been reviewing the documentation, and would have had to be happy with it as part of the process by which it was finalised for execution."*[94]

95. Sixth, Ms Dolby was asked in cross-examination whether all she intended was to defer interest with no other intention,[95] but she was deliberately not asked whether she intended not to make changes to the ranking section, or whether she saw the tax sensitivities as part of the interest deferral.

96. Seventh, the Judge was aware of the nature of the single rectification claim which SLP3 advanced at trial (and now on appeal). Strikingly, that was a claim to remove, virtually wholesale, the entirety of the detailed amendment to clause 3 proposed in the second draft on 12 June 2008, restoring the position to the original draft on 5 June 2008.[96] This perceived need for SLP3 to put its case at such an extreme level underscored its departure from reality, because (at the very least) the parties knew and intended that such detailed and extensive amendments had some legal effect. The law of rectification does not permit a party to seek to remove such amendments simply because it does not now like one of the consequences of them.

97. Eighth, the nature of the mistake contended for by SLP3 (albeit with hindsight) is in truth not as to the meaning or legal effect of the amendment but rather as to their effect as a matter of fact, i.e. the effect they have *given the existence of the LBHI2 Sub-Debt with its subordination provision* (which the parties did not have in mind: Judgment [262(3)(c)]) *and given the insolvency but with sufficient assets to pay subordinated lenders* that ultimately occurred. Hence its real case was as SLP3 contended in opening: "*It was not part of the common intention of the parties that SLP3 should be demoted or relegated below [PLC] in the event of an insolvency*".[97] Even if justified on the

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[93] [Day 2/123.9-124.21] [SB2/51/549].

[94] Dolby WS at [65] [SB1/5/80].

[95] [Day3/110.13-18, 131.10-14, 135.4-7] [SB2/54/567, 570-571].

[96] SLP3 Oral Closing [Day 6/154] [SB2/56/595]: "*the rectification sought only simply puts condition 3 in the same form as the first draft that was approved by Ms Dolby and others and that would have had the intended effect of deferring interest, no more no less*".

[97] SLP3 Oral Opening [Day 1/88.4-9] [SB2/49/535].

evidence, this would at most be a mistake as to the effect of the amendment, which is not sufficient to give rise to rectification. PLC adopts the submissions of Deutsche on this point.

E4. Relevant decision makers

98. All of the above discussion is in fact unnecessary, because the further gaping hole in SLP3's case is that there was no evidence of the intentions of the actual decisions makers, namely those who sanctioned the amendments, Ms Upton and Mr Triolo on behalf of SLP3 and Mr Rush and Mr Jameson on behalf of LBHI2. None of them was called by SLP3 and their actual intentions and understanding were simply incapable of being explored. Absent such evidence, the rectification claim was always inchoate. SLP3 sought to plug the gap by contending that the decision makers were in fact persons other than those who sanctioned the amendments. But this turned out to be a mutating case, which was evidentially unsupported in any of its formulations.

99. In its Opening, SLP3's case[98] was that Ms Dolby and Ms McMorrow were "*in reality*" the decision makers (for both SLP3 and LBHI2) or that their intentions were "*adopted by*" the actual decision makers. An immediate problem with this case was that SLP3 did not call Ms McMorrow either, and so her intentions could not be explored. Ms McMorrow was a senior lawyer within the Lehman Group. So the case which was opened had to be abandoned by the time of Closing, at which point the new case was that it was Ms Dolby, alone, who was the decision maker or whose intentions were adopted by the decision makers. SLP3 offered no explanation of why it changed its case on such an important issue. The irresistible inference is that Ms Dolby ended up as the candidate for decision maker for no reason other than that she was the only one who gave evidence. But that was not a principled or sustainable basis upon which to advance a new case in Closing[99].

[98] SLP3 Written Opening [436]-[437] [SB1/8/213].

[99] Of the two, Ms McMorrow was probably the more important. As the relevant senior lawyer, she instructed A&O and was the main point of contact for them. Judgment [205] and [208]; Dolby WS at [39] and [61] [SB1/5/75, 79], Dolby interview 12.8-18 [SB1/4/47], Dolby [Day 3/96.22-3] [SB2/54/563], Grant WS at [20] [SB1/1/13], [SB2/21/410]. The original draft of the amendments was sent only to her [SB2/24/417], [SB2/25/431]. Mr Grant confirmed that if he had been aware that the amendment was altering ranking, he would have sought instructions from Ms McMorrow but now cannot recall whether he did [Day 2/139.8-11] [SB2/52/552], Grant WS at [57] [SB1/1/20-21], Judgment [262(4)(b)]. Ms Dolby confirmed that she gave no instructions in relation to ranking but would not confirm that Ms McMorrow gave none: Day 3/95-6.

100. Given his findings on the evidence, the Judge did not need to address this question: Judgment [269]. It was considered in detail by PLC at trial[100] and the point is relied upon by Respondent's Notice[101]. The relevant principles were set out by Mann J in *Murray Holdings Ltd v Oscatello Investments Ltd*[102]. SLP3 has set out no detailed case, and for present purposes PLC confines itself to the following points:

101. First, the starting point is that the decision maker will usually be the person with authority to bind the company. It is not disputed that these were Ms Upton, Mr Triolo, Mr Rush and Mr Jameson. No one suggested that Ms Dolby could or ever would have purported to bind either (let alone both) LBHI2 or SLP3.

102. Second, and as per *Oscatello*, the burden of showing that Ms Dolby (alone) was nevertheless the decision maker fell on SLP3. That question is heavily fact-sensitive. *Oscatello* shows that the appropriate delegation will be found where the formal decision-maker had a mere "*compliance*" role but the test is necessarily high.[103] It is not satisfied even where it is "*always likely that* [the negotiator's] *recommendations would be accepted*".[104]

103. SLP3 adduced no evidence that could possibly justify a case of delegation (indeed abdication) of responsibility by *both* PLC (Mr Rush and Mr Jameson) and SLP3 (Mr Triolo and Ms Upton). On the contrary, and strikingly, Ms Dolby gave unambiguous evidence (adduced by SLP3 itself[105] and so not open to challenge) that she was <u>not</u> the decision maker[106]. SLP3 never explained how it could pursue a case directly inconsistent with its own evidence.

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[100] PLC Written Opening [144-154] [SB1/10/248-252].

[101] PLC Supplementary Respondent's Notice [2-3] [CB1/5/40].

[102] [2018] EWHC 162 (Ch).

[103] [67], [190], [202(d)], [203]. The trustee in *Hawksford Trustees Jersey Ltd v Stella Global UK Ltd* [2012] EWCA Civ 55 at [41]-[43] was similar.

[104] [216]. See similarly *Mayor and Burgesses of Barnet v Barnet Football Club Holdings Ltd* [2004] EWCA Civ 1191 and *George Wimpey UK Ltd v VI Construction Ltd* [2005] EWCA Civ 77 at [49]-[50].

[105] This evidence from an interview was adduced by SLP3 pursuant to a hearsay notice.

[106] Dolby interview 24.11-25 and 26.3-7 [SB1/4/59, 61], also [Day 3/116.5-8] [SB1/54/568]. Ms Dolby also explained in clear terms the role of Mr Rush as her superior in the tax department who was therefore himself fully aware of the issues from a tax perspective, had a "*number of discussions*" with Ms Dolby "*briefing him on a regular basis"* and "*daily basis"* and approved everything as it occurred: Dolby WS at [71]-[72] [SB1/5/81-82], [Day 3/113.2-10] [SB2/54/568], Dolby interview 21.9-11, 24.30-34 and 26.11-15 [SB1/4/56, 59, 61]. He had enough of his own understanding to answer questions from the Board: Dolby [Day 3/113.14-16] [SB2/54/568]. His decision was active, not just a sign-off: Dolby interview 25.4-8 [SB1/4/60]. Ms Dolby did not know what process Mr Triolo's

104. There was no evidence from any other source even to explain the decision making and approval processes of any of Mr Rush, Mr Jameson, Mr Triolo or Ms Upton, let alone to give any support to the contention (which not a single witness supported) that they merely rubber-stamped the decisions that were made[107]. If, and to the extent necessary, PLC invites the Court to conclude that the only relevant intentions for the purposes of this claim to rectification are of those authorised decision makers. There was no evidence before the Judge that any of those persons operated under a mistake or, indeed, that they did not understand and intend that the amendments would have the effect in law found by the Judge. Absent proper evidence to establish the contrary, it followed that the decision-makers intended to approve the contract as presented to them and with the meaning the reasonable person would understand it to have.[108]

E5. Outward expression of accord

105. It is clear law that an outward expression of accord is an independent legal requirement for rectification of a contract, as the Judge recorded at Judgment [258(3) and (5)-(6)] citing Leggatt LJ in *FSHC*[109]. Common but unshared private subjective intentions are insufficient—it is necessary that "*the parties understood each other to share that intention*" (Leggatt LJ at [176]). The Judge found, after considering the position of SLP3 and LBHI2 separately, that even if there had been a mistake, there was no outward expression of accord between SLP3 and LBHI2: Judgment [268]. SLP3 challenges this at SLP3 Skeleton [118]-[120] ([CB1/7/96]) but this was a finding of fact which the Judge was entitled (and right) to make. Dealing with the points with similar brevity:

106. First, an outward expression is required here. The pension cases (which SLP3 says are an "*analogy*": SLP3 Skeleton [119] ([CB1/7/96])) do not require outward expression because the document being rectified is not a bilateral contract that itself required mutual agreement, rather the exercise of a trustee's unilateral

approval comprised but did know that he was involved from start to finish: Dolby interview 20.23-31 and 36.13-18 [SB1/4/55, 71].

[107] SLP3's contention involved, at least implicitly, criticism of the conduct of directors of these companies, which criticism was unwarranted and unfounded. They were not rubber-stamping off-shore directors with no understanding of the underlying substance of the matters. They were not given the opportunity to respond to these allegations.

[108] *Barnet* at [48]; *Wimpey* at [49]-[50], also [82]-[84].

[109] See *FHSC* (CA) at [72-4], [76-7], [81], [102], [159], [176].

power of amendment that was simply approved/consented to by the employer, and which have long been characterised alongside unilateral transactions such as wills or voluntary settlements: *FSHC* CA [78-9][110].

107. The instruments in this case constitute commercial contracts between the issuer LBHI2 and the noteholder SLP3. The terms of the LBHI2 Sub-Notes do not grant either party a unilateral power to amend subject merely to the consent of the other.[111] And so an outward expression of accord between LBHI2 and SLP3 is required.

108. Second, there was no outward expression here. SLP3 relies (SLP3 Skeleton [120] ([CB1/7/96])) on the general run of communications within Lehman (e.g. those between Ms Dolby, Ms McMorrow and A&O). It is correct that communication can be tacit but this is set at a higher test even than implied terms—the relevant matter must be actually mutually agreed.[112] Such a test can be satisfied where, as in *FSHC*, the unintended amendment would be "*absurd*" and "*inconceivable*".[113] In the present case, there would need to be more than merely the fact that the formal corporate resolution documentation only referred to the core commercial purpose of interest deferral, remembering that the amendments themselves provide the clearest expression of what was intended.

1 March 2021 (replacement skeleton 29 March 2021)

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[110] Also *AMP (UK) v Barker* [2001] Pens LR 77 at [59], [62] and [65], and *Re IBM Pension Plan* [2012] EWHC 1766 (Ch) [2012] Pens LR 469 (Warren J) at [19]-[24] explaining that a pension amendment is a "different animal" from a contract.

[111] Condition 12(b) reserves to the Registrar the power unilaterally (and without consent of the Noteholders) to make minor non-prejudicial amendments to the LBHI2 Sub-Notes, but no one contends that that power is relevant to the amendments made in autumn 2008.

[112] *FSHC* (CA) [81-7].

[113] See footnote 85 above.