Neutral Citation Number: [2017] EWHC 2032 (Ch)

Case No: CR-2009-000052

IN THE HIGH COURT OF JUSTICE
CHANCERY DIVISION
COMPANIES COURT

Royal Courts of Justice
7 Rolls Building, Fetter Lane, London, EC4A 1NL

Date: 03/08/2017

Before:

THE HONOURABLE MR JUSTICE HILDYARD

\- -

Between:

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

AND IN THE MATTER OF LEHMAN BROTHERS LIMITED (IN ADMINISTRATION)

AND IN THE MATTER OF LEHMAN BROTHERS INTERNATIONAL (EUROPE) (IN ADMINISTRATION)

AND IN THE MATTER OF LEHMAN BROTHERS HOLDINGS PLC (IN ADMINISTRATION)

AND IN THE MATTER OF THE INSOLVENCY ACT 1986

\- -

THE HONOURABLE MR JUSTICE HILDYARD

Felicity Toube QC (instructed by **Linklaters LLP**) for the LBEL Administrators
Tony Beswetherick (instructed by **Hogan Lovells International LLP**) for the LBH Administrators
Peter Arden QC and Rosanna Foskett (instructed by **Dentons LLP**) for the LBHI2 Administrators
Philip Marshall QC and Ruth den Besten (instructed by **Dechert LL**P) for the LBL Administrators

William Trower QC and Alexander Riddiford (instructed by **Linklaters LLP**) for the LBIE Administrators

Hearing dates: 24 July 2017

- -

Approved Judgment

I direct that pursuant to CPR PD 39A para 6.1 no official shorthand note shall be taken of this Judgment and that copies of this version as handed down may be treated as authentic.

....

Mr Justice Hildyard :

Introduction

1. The joint administrators of four English companies within the former Lehman Brothers group ("the Lehman Group") seek directions in respect of a proposed settlement ("the Proposed Settlement") of numerous substantial inter-company claims including those claims at issue in the proceedings known as "Waterfall III".

2. The particular companies within the Lehman Group and their applicant joint administrators are (1) Lehman Brothers International (Europe) (in administration) ("LBIE" and "the LBIE Administrators"), (2) Lehman Brothers Limited (in administration) ("LBL" and "the LBL Administrators"), (3) LB Holdings Intermediate 2 Limited (in administration) ("LBHI2" and "the LBHI2 Administrators") and (4) Lehman Brothers Holdings plc (in administration) ("LBH" and "the LBH Administrators").

3. In addition to those companies, it is anticipated that two other members of the Lehman Group, Lehman Brothers Europe Limited (in administration) ("LBEL Administrators") and Lehman Brothers Holdings Inc. ("LBHI") will be parties to the Proposed Settlement.

4. The joint administrators of LBEL were represented by counsel at the hearing of these applications on 24 July 2017, but they did not make a similar application themselves, having received my permission earlier on 24 July to take certain steps required of LBEL and its joint administrators to facilitate the Proposed Settlement. That application is discussed in my separate judgment on it explaining my reasons for giving that permission: [[2017] EWHC 2031 (Ch)].

5. LBHI is the ultimate parent company of LBIE and its UK affiliates. It was incorporated in Delaware and has commenced proceedings under Chapter 11 of the US Bankruptcy Code. LBHI was not represented by counsel at the hearing. LBHI's direct involvement in the Proposed Settlement is relatively limited, principally to providing a capped indemnity to LBIE in the event (which the parties consider to be unlikely) of there being a shortfall in relation to LBIE's unsubordinated creditors.

The status of the administrations

6. Following the collapse of the Lehman Group in 2008, a substantial surplus, estimated at between £7 billion and £8 billion, has arisen in the administration of LBIE, which before the collapse was the Lehman Group's principal trading company in Europe.

7. LBIE, LBL and LBH have been in administration since September 2008. LBL has been in administration since January 2009. The purpose of these administrations has been to achieve a better result for the applicable companies' creditors as a whole than would be likely if the relevant company was wound up without first being placed into administration.

8. LBHI2 owns all of LBIE's shares, except for one ordinary share which is registered in the name of LBL.

9. There is a complex web of substantial claims and cross-claims between the various companies in the Lehman Group. As a result, several of the parties to the Proposed Settlement have submitted numerous claims in the administrations of other parties, each of which is typically valued in the tens or hundreds of millions of pounds. Of particular significance for the purposes of Waterfall III (described below) are two £10 billion claims submitted by LBIE, one in each of LBL's and LBHI2's administrations, in respect of those companies' respective contingent liabilities to LBIE as contributories under section 74 ("section 74") of the Insolvency Act 1986 ("the 1986 Act") which arose according to the decisions at first instance and of the Court of Appeal in the Waterfall I litigation referred to below.

10. As of the date of the present applications:

    i) The LBIE Administrators have paid dividends to LBIE's ordinary unsecured creditors, with proved claims of 100 pence in the pound (in aggregate) in respect of such claims.

    ii) The LBL Administrators have paid a dividend of 100 pence in the pound to former employees of LBL with preferential unsecured claims (comprising claims for unpaid wage and holiday pay) and a first interim dividend of 1.66 pence in the pound to ordinary unsecured creditors.

    iii) The LBHI2 Administrators obtained permission on 15 June 2017 to make interim distributions to unsecured creditors, subject to a requirement to give four weeks' notice to the LBIE Administrators before filing a notice of intended distribution. However, the LBHI2 Administrators have not made any distributions to creditors to date.

    iv) The LBEL Administrators have paid dividends to LBEL's ordinary unsecured creditors totalling 100 pence in the pound. In addition, the LBEL Administrators received permission of the Court on 24 July 2017 to appoint a director of LBEL and authorise him and LBEL's sole member, LBH, to implement (after reserving for statutory interest and other matters) a capital reduction and distribution to LBH.

    v) The LBH Administrators have paid dividends to LBH's unsecured, non-preferential (unsubordinated) creditors of 6.08 pence in the pound in respect of such claims.

11. The joint administrators of these companies are, however, unable to make further distributions pending resolution of a number of legal issues currently in dispute in the various Waterfall proceedings, to which I turn next.

Overview of the Waterfall litigation

12. In February 2013, once it had become apparent that there might be a surplus in the LBIE administration, the LBIE, LBL and LBHI2 Administrators made applications for directions in respect to that surplus in proceedings known as "Waterfall I". The issues in dispute in Waterfall I included the ranking of LBHI2's subordinated debt claim as against LBIE's obligation to pay statutory interest to unsubordinated

creditors, the existence of currency conversion claims and the scope of contribution claims and the circumstances in which they may be brought.

13. Waterfall I was heard by this Court in November 2013, by the Court of Appeal in March 2015 and by the Supreme Court in October 2016. The Supreme Court handed down judgment in Waterfall I on 17 May 2017: *Re Lehman Brothers International (Europe) (In Administration)* [2017] UKSC 38.

14. The Supreme Court, which in doing so overturned certain aspects of the decisions below, reached several conclusions which are of particular significance for present purposes, including findings that:

    i) The subordinated debt claim owed to LBHI2 by LBIE is subordinated behind statutory interest and non-provable liabilities.

    ii) Currency conversion claims do not exist as a species of non-provable liability.

    iii) Statutory interest accrued but not paid in LBIE's administration is not payable in any subsequent liquidation of LBIE.

    iv) A contributory's liability under section 74 does not extend to creating a surplus for the payment of statutory interest but it does extend to the payment of non-provable liabilities.

    v) The LBIE Administrators are not entitled to prove for a potential contribution claim that might arise in the event of LBIE going into liquidation.

    vi) The contributory rule currently applicable in liquidation proceedings extends to administration proceedings.

15. In June 2014, a further application ("Waterfall II") was brought by the LBIE Administrators with a view to clarifying a range of other issues. Given the scope and complexity of Waterfall II, the Court ordered that it be tried in three parts: Parts A, B and C. Parts A and B were heard by this Court and judgments were handed down in respect of both of them by David Richards J on 31 July 2015. An appeal was heard by the Court of Appeal in April 2017, with judgment reserved pending the Waterfall I judgment being handed down by the Supreme Court. Part C was heard by this Court in November 2015 and a judgment was handed down on 5 October 2016. Permission to appeal to the Court of Appeal was granted, and the appeal is due to be heard in July 2018.

16. In April 2016, the LBIE Administrators made the Waterfall III application seeking directions from the Court and in October 2016 the LBL Administrators made a cross-application raising similar issues. Among the issues in Waterfall III are whether the obligations of LBHI2 and LBL to contribute to the assets of LBIE under section 74 extend to a contribution to enable LBIE to pay an unsecured subordinated claim in respect of certain sums advanced to LBIE and, if so, how that would work.

17. For case management purposes, Waterfall III was split into two parts: Part A and Part B. I heard Part A at a hearing commenced on 30 January 2017. However, I indicated that I would reserve judgment pending the Supreme Court's judgment in Waterfall I

and that I might require further submissions in respect of the impact of that judgment on the issues in Waterfall III.

18. In the context of the wider Waterfall litigation, the joint administrators of the relevant Lehman Group companies may have to wait several years before Waterfall III, together with relevant aspects of Waterfall II, are finally determined. In such circumstances, it is not surprising and is salutary that efforts have been made to limit the issues in dispute by way of compromise.

19. In particular, the joint administrators have, for reasons discussed below, taken the view that the Supreme Court's decision in Waterfall I has made it considerably less likely that LBIE could bring a contribution claim against LBL or LBHI2. This has been a powerful impetus for the negotiations that have led to the Proposed Settlement.

Summary of the Proposed Settlement

20. In summary, the Proposed Settlement provides for the settlement of the intra-Lehman Group contribution and recharge claims which are the subject of Waterfall III.

21. It is intended that the Proposed Settlement will be given effect by the following documents ("the Transaction Documents"), which are exhibited in substantially final form to the fifth witness statement of Ms. Gillian Bruce, one of the joint administrators of each of LBHI2 and LBH, dated 19 July 2017 ("Ms. Bruce's fifth witness statement"):

    i) A Master Framework Agreement, which (*inter alia*) sets out a framework for the various transaction documents each of LBIE, LBL, LBHI2, LBEL, LBH (and their respective administrators) and LBHI are to enter into to give effect to the overall Proposed Settlement and provides that Waterfall III will be dismissed by consent.

    ii) A Deed of Settlement, by which (*inter alia*) LBIE and the LBIE Administrators are to release and discharge LBL, LBHI2 and LBH (and their respective administrators) from the various claims which LBIE has against them, waive the four-week notice requirement set out in my Order of 15 June 2017 and confirm that they do not object to LBHI2, LBL and LBH making distributions without any provision or reserve being made for actual or potential claims.

    iii) An Inter-Affiliate Settlement Deed, by which (*inter alia*) LBL, LBHI2, LBEL and LBH agree to pay or receive the sums agreed between the parties and to make any necessary distributions to creditors external to the Lehman Group. The agreement resolves the various inter-company claims between different Lehman Group entities. It takes into account monies that will be received into the estate as a result of the operation of the Proposed Settlement so that each Lehman estate can make one composite distribution to its creditors.

    iv) A Limited Recourse Deed, which is an agreement between LBIE and the Wentworth parties (see paragraph 38(i) below) which will limit the subordinated debt claim in the LBIE estate to the actual residual cash in that

estate, thus meaning that a contribution claim to cover the subordinated debt will not arise.

v) An Indemnity, which is a capped indemnity given by LBHI to LBIE to cover the unlikely situation of there being a shortfall in relation to LBIE's unsubordinated creditors.

22. In commercial terms, one of the important features of the Proposed Settlement is that it will enable LBHI2 and LBL (i.e. LBIE's members) to make distributions to their unsecured creditors without reserving for any future contribution claim. In particular, the Deed of Settlement provides that LBIE and the LBIE Administrators confirm: (i) that their waiver of the four-week notice period that LBHI2 is required to give them prior to issuing a notice of intended distribution is in full force and effect and continues to apply; and (ii) that they do not object to the LBHI2 Administrators, the LBL Administrators and the LBH Administrators making the payments contemplated in the Inter-Affiliate Settlement Deed without making provisions or reserves for any actual or potential claims from LBIE, the LBIE Administrators and/or any liquidator appointed to LBIE. The position of each applicant as to why they are (and as to why it is reasonable for them to be) prepared to give this confirmation, in the context of the broader Proposed Settlement, is discussed below.

The applications in outline

23. The applications were made by application notices dated 20 July 2017 in the case of the LBIE, LBL and LBHI2 Administrators and by application notice dated 23 July 2017 in the case of the LBH Administrators. The applicants each seek directions pursuant to paragraphs 63 (and/or, where applicable, paragraphs 65(3) and/or 68(2)) of Schedule B1 to the 1986 Act) that the relevant applicants be at liberty to enter into and perform (on their own behalf and on behalf of the company in respect of which they have been appointed) the Transaction Documents.

24. The applicants other than the LBIE Administrators also seek ancillary directions applicable to their role in the Proposed Settlement:

i) The LBHI2 Administrators apply for directions that (a) the four-week notice provision in my Order of 15 June 2017 is waived; and (b) following the execution of the Transaction Documents, the LBHI2 Administrators be at liberty to make a first interim distribution without reserving for any potential contribution claim by LBIE.

ii) Similarly, the LBL Administrators apply for directions that, following the execution of the Transaction Documents, they be at liberty to make any further distribution without reserving for any potential contribution claim by LBIE.

iii) The LBH Administrators apply for directions that they be at liberty to support and to take such further steps as may be considered desirable and appropriate to give effect to the mechanism for effecting a distribution by LBEL to its sole member (i.e. LBH) for which I gave permission on 24 July 2017.

25. The LBHI2 Administrators also apply pursuant to Rule 12.39(9) of the Insolvency (England and Wales) Rules 2016 that the Exhibit GEB 5(B) to Ms. Bruce's fifth

witness statement shall not be open for inspection without the permission of the Court.

The relevant legal test

26. The legal principles that I must take into account when considering applications for directions of this sort were recently summarised by Snowden J in *Re Nortel Networks UK Ltd* [2016] EWHC 2769 (Ch) at [45]-[50], gathering together the guidance provided in earlier cases as follows:

> "In re *MF Global UK Ltd (No 5) [2014] Bus LR 1156* David Richards J was asked to authorise a settlement agreement to compromise claims by the company to assets said to be held on its own account, which were also said to be held by the company on trust for its own clients. He addressed the approach to be taken by administrators when seeking to compromise the company's own claims as follows, at para 41:
>
> "In commercial matters, administrators are generally expected to exercise their own judgment rather than to rely on the approval or endorsement of the court to their proposed course of action: see *In re T & D Industries plc [2000] 1 WLR 646.* While the compromise of claims raising difficult legal issues may not be on all fours with a purely business decision, administrators commonly exercise the power of compromise without recourse to the court and in general apply to the court for directions only if there are particular reasons for doing so: see *In re Lehman Bros International Europe [2014] BCC 132*."
>
> One such "particular reason" which might justify administrators applying to the court for directions in relation to the exercise of the power of compromise can be derived by analogy from the second category of cases in which trustees can seek directions from the court. This was identified by Hart J in *Public Trustee v Cooper [2001] WTLR 901*, 922–924:
>
> "The second category is where the issue is whether the proposed course of action is a proper exercise of the trustees' powers where there is no real doubt as to the nature of the trustees' powers and the trustees have decided how they want to exercise them but, because the decision is particularly momentous, the trustees wish to obtain the blessing of the court for the action on which they have resolved and which is within their powers. Obvious examples of that, which are very familiar in the Chancery Division, are a decision by trustees to sell a family estate or to sell a controlling holding in a family company. In such circumstances there is no doubt at all as to the extent of the trustees' powers nor is there any doubt as to what the trustees want to do but they think it prudent, and the court will give them their costs of doing so, to obtain the court's blessing on a momentous decision. In a case like that, there is

no question of surrender of discretion and indeed it is most unlikely that the court will be persuaded in the absence of special circumstances to accept the surrender of discretion on a question of that sort, where the trustees are prima facie in a much better position than the court to know what is in the best interests of the beneficiaries."

The instant case is, in my judgment, just such a case. In signing the documents comprising the global settlement, the administrators and the conflict administrator have already decided that the global settlement is in the best interests of each of the EMEA Companies and their creditors. They do not propose to surrender the exercise of their discretion in that regard to the court, but they seek the approval of the court because of the great significance of the global settlement in the context of the administrations of each of the EMEA Companies. Given the size and complexity of the affairs of the Nortel group and the amounts in the Lockbox, there can, in my judgment, be no doubt that the execution of the global settlement is a truly momentous decision.

In a category two case involving trustees, the approach of the court was summarised by David Richards J in *In re MF Global UK Ltd (No 5) [2014] Bus LR 1156*, para 32, where he cited with approval the following from *Lewin on Trusts*, 18th ed (2008), para 29-299:

"The court's function where there is no surrender of discretion is a limited one. It is concerned to see that the proposed exercise of the trustees' powers is lawful and within the power and that it does not infringe the trustees' duty to act as ordinary, reasonable and prudent trustees might act, ignoring irrelevant, improper or irrational factors; but it requires only to be satisfied that the trustees can properly form the view that the proposed transaction is for the benefit of beneficiaries or the trust estate and that they have in fact formed that view. In other words, once it appears that the proposed exercise is within the terms of the power, the court is concerned with limits of rationality and honesty; it does not withhold approval merely because it would not itself have exercised the power in the way proposed. The court, however, acts with caution, because the result of giving approval is that the beneficiaries will be unable thereafter to complain that the exercise is a breach of trust or even to set it aside as flawed; they are unlikely to have the same advantages of cross-examination or disclosure of the trustees' deliberations as they would have in such proceedings. If the court is left in doubt on the evidence as to the propriety of the trustees' proposal it will withhold its approval (though doing so will not be the same thing as prohibiting the exercise proposed). Hence it seems that, as is true when they surrender their discretion,

> they must put before the court all relevant considerations supported by evidence. In our view that will include a disclosure of their reasons, though otherwise they are not obliged to make such disclosure, since the reasons will necessarily be material to the court's assessment of the proposed exercise."
>
> Similar (albeit expanded) observations appear in the current 19th ed (2014) of *Lewin on Trusts*, paras 27-079–27–081. Reference can also be made to the decision of Henderson J in *Hughes v Bourne [2012] WTLR 1333*, para 16.
>
> For my part, whilst noting that the position of an administrator seeking directions under the Insolvency Act 1986, and a trustee seeking directions under the Trustee Act 1925 are not identical, I see no obvious reason why most of the same considerations should not apply when the court considers giving directions to an administrator who wishes to enter into a compromise which is particularly momentous. In short, the court should be concerned to ensure that the proposed exercise is within the administrator's power, that the administrator genuinely holds the view that what he proposes will be for the benefit of the company and its creditors, and that he is acting rationally and without being affected by a conflict of interest in reaching that view. The court should, however, not withhold its approval merely because it would not itself have exercised the power in the way proposed.
>
> In these respects the approach of the court will mirror the attitude which the court would take to a subsequent challenge to the decision by a creditor: see e g *In re Longmeade Ltd [2016] Bus LR 506*, paras 61–65. But having regard to the fact that its approval will prevent subsequent challenge, the court will require the administrator to put all relevant material before it, including a statement of his reasons, and the court will not give its approval if it is left in any doubt as to the propriety of the proposed course of action."

27. Entry into settlement agreements and compromises is within the powers of administrators pursuant to paragraph 60 of Schedule B1 and paragraph 18 of Schedule 1 to the 1986 Act. Accordingly, it is within the applicants' powers to cause LBIE, LBH, LBHI2 and LBL to enter into the agreements comprised in the Proposed Settlement.

28. Given the size and complexity of the claims involved, the unique nature of the Lehman Group administrations and the long-running and complicated disputes that they have given rise to, I am in no doubt that the Proposed Settlement is a "momentous" decision for the applicants, the companies over which they have been

appointed and the creditors of those companies, such as to explain and justify these applications.

29. It is therefore necessary for me to consider whether the relevant evidence before me leaves me in any doubt that the applicants' view that the Proposed Settlement will be advantageous to the companies over which they have been respectively appointed and the creditors of those companies is genuinely held, rational and has been arrived at free from conflicts of interest. I must be satisfied, generally, that there is no doubt as to the propriety of what is proposed.

30. For the avoidance of doubt, and as is apparent from the authorities, the Court's function is not to determine, and could not sensibly extend to determining, whether the settlement proposed is the best available, or might be improved in some way. The decision is and remains one for the administrators; and the Court's function is not to double-guess it.

31. Unlike in the broadly analogous context of an application by trustees for directions without surrender of discretion, where it is commonplace for the Court to hear the parties individually and to be guided by opinions of Counsel as to the merits of what is proposed from the particular point of view of the beneficiaries concerned, in the context of an officeholder's application such as this the Court is not really involved in the merits of the decision and is not ordinarily furnished with partisan or confidential material of that nature. Its focus is on the rationality and propriety of what is proposed, and on being satisfied that it is not infected by some conflict of interest affecting any of its proponents.

Steps taken to mitigate conflicts of interest

32. A number of the joint administrators of the companies participating in the Proposed Settlement are also joint administrators of other companies in the Lehman Group, raising the possibility of conflicts of interest should a single administrator be asked to assess, negotiate and decide whether to accept the Proposed Settlement from the perspective of more than one administration.

33. To mitigate these potential conflicts, each of the parties to the Proposed Settlement (other than LBH which has authorised another independent person as explained in the next paragraph) has authorised a single administrator to take primary responsibility for negotiations of the Proposed Settlement on its behalf and to determine whether it benefits the creditors of that party separately. In so doing, they have also been able to consider the global benefits of the Proposed Settlement.

34. In the case of LBIE, the person so designated is Mr. Russell Downs who has given an eleventh witness statement dated 19 July 2017 for the purposes of LBIE's application. For LBL, it is Mr. Michael Jervis, who has given an eighth witness statement dated 19 July 2017, although the issue does not in fact arise in the case of LBL whose two joint administrators are not appointed in respect of any other Lehman Group company in administration. For LBH and LBHI2, the person designated was Ms. Bruce, although in relation to LBH the Proposed Settlement has also been the subject of independent consideration by Mr. Robert Lewis ("Mr Lewis"): although not an administrator of LBH, Mr Lewis has been authorised to represent its interests, specifically with regard

to potential conflicts of interests in relation to Waterfall III and has given a witness statement in support of the Proposed Settlement dated 23 July 2017.

35. In their witness statements, each of Mr. Downs, Mr. Jervis, Ms. Bruce and Mr. Lewis explain that the LBIE, LBL, LBHI2, and LBH Administrators have, respectively, formed an independent view, with the benefit of independent legal advice on, and have been able to reach a view as to the appropriateness of, the Proposed Settlement free of any conflict of interest.

36. In these circumstances, I am satisfied that the applicants have each been able to reach a view as to whether the Proposed Settlement will benefit the estate in respect of which they have been appointed, and its creditors as a whole, without being infected by any conflicts of interest.

Rationality of entering into the Proposed Settlement

37. In their witness statements, each of Messrs. Downs, Jervis and Lewis and Ms. Bruce set out their several assessments of the advantages and disadvantages of the Proposed Settlement as regards LBIE, LBL, LBH and LBHI2 (and their respective creditors), respectively.

38. In his eleventh witness statement, Mr. Downs explains the principal advantages of the Proposed Settlement to LBIE and its creditors as follows:

    i) A joint venture entered into by the LBHI2 Administrators, Elliot Management Corporation and King Street Capital Management ("Wentworth") will waive any right to be paid the subordinated-debt advanced to LBIE pursuant to three subordinated loan agreements entered into on 1 November 2006 ("the Sub-Debt"), out of anything other than LBIE's existing assets. This will effectively cap LBIE's liability in respect of the Sub-Debt.

    ii) For the same reasons, the Proposed Settlement will effectively remove the possibility of a contribution claim in respect of the Sub-Debt. This will give LBIE certainty in relation to this issue much sooner than it would otherwise have obtained it (i.e. after the determination of the relevant issues in Waterfall III and any appeals against that determination) and means that many of the issues in Waterfall III will not require the Court's determination, with the inevitable potential for uncertainty, delay and cost which this would entail.

    iii) LBIE and LBL will agree a nil balance in respect of their mutual claims. This will avoid the need for further costs to be incurred in the LBIE administration in dealing with LBL's claims (including costs in relation to disputed proofs) and the possibility of any balance in favour of LBL being determined.

    iv) Waterfall III will be settled. This will remove the possibility of LBL establishing (and the LBIE Administrators' need to reserve for) its recharge claims. It will also provide legal certainty much sooner than would otherwise be the case and will avoid the need for LBIE to incur further substantial costs (both in respect of the determination of the Waterfall III Part B issues at first instance, and in respect of any appeals in respect of any of the Waterfall III issues).

v) LBHI will grant LBIE a capped indemnity to cover any shortfall in LBIE's ability to pay what are described as Senior Creditor Entitlements (i.e. statutory interest accrued in LBIE's administration and certain potential non-provable claims).

vi) Finally, one effect of the Proposed Settlement will be to expedite the distribution by the LBH Administrators to LBH's unsecured creditors. LBIE has a substantial admitted unsecured claim in LBH's estate, and so this aspect of the Proposed Settlement will be to LBIE's advantage.

39. Mr. Downs also identifies two potential disadvantages to LBIE and its creditors:

i) The principal potential disadvantage is that the Proposed Settlement will require the LBIE Administrators to give up any right they might otherwise have to object to LBIE's members making certain distributions without reserving for any future contribution claim. However, as discussed below, the LBIE Administrators consider that this potential disadvantage does not, in reality, amount to a material concession. To the extent that it is a disadvantage at all, it is one which the LBIE Administrators consider is in any case outweighed by the various advantages set out above.

ii) LBIE will be required to acquiesce in the transfer by LBL of its share in LBIE to LBHI2. However, the LBIE Administrators consider that there is no sensible basis on which they could object to such a transfer (and indeed they note that LBHI2 and LBL can, in any event, effectively take the relevant steps without any involvement from LBIE or the LBIE Administrators). Accordingly, the LBIE Administrators do not consider this feature of the Proposed Settlement to be a material disadvantage.

40. In his eighth witness statement, Mr. Jervis explains the principal advantages of the Proposed Settlement to LBL and its creditors as follows:

i) It will facilitate a substantial amount becoming available for distribution to LBL's affiliates and creditors. This amount, together with the existing assets in LBL's estate, will enable the LBL Administrators to pay a dividend of 100 pence in the pound to unsecured creditors, together with accrued statutory interest.

ii) LBL's creditors will imminently make a recovery on their outstanding debts.

iii) The Proposed Settlement will resolve the outstanding disputes between the parties to Waterfall III.

iv) The Proposed Settlement will eliminate the risk that further, potentially protracted, legal hearings will take place, together with associated litigation risks on the issues in Waterfall III.

v) The Proposed Settlement will avoid the incurring of further legal and professional costs in preparing for the hearing scheduled in Waterfall III.

vi) The Proposed Settlement will enable the distribution and finalisation of LBL's estate within a reasonable timeframe.

41. Mr. Jervis identifies the following potential disadvantages:

i) The Proposed Settlement does not include any undertaking by LBIE or the LBIE Administrators to avoid liquidation, or release LBL from any contribution claim that a future liquidator of LBIE might make. However, for reasons discussed below, the risk of a contribution claim going forward is now considered unlikely or highly unlikely.

ii) The Proposed Settlement compromises the LBL Administrators' outstanding claims to recharge certain liabilities asserted in Waterfall III (see above).

iii) There remains a risk of a potential future objection by LBIE to a distribution in its estate. However, the LBL Administrators have taken the view that this risk is highly unlikely given that, following the Proposed Settlement, LBIE will no longer be a creditor in LBL's estate, and a year after LBL's transfer of its share to LBHI2, it will not be liable for any contribution claim.

42. For Ms. Bruce's part, she describes in her fifth witness statement the principal advantages of the Proposed Settlement to LBHI2 and its creditors as follows:

i) It settles the Waterfall III litigation.

ii) It allows progress to be made in the LBHI2 administration, in circumstances where creditors have received no distributions since the commencement of the administration in early 2009.

iii) By virtue of the Inter-Affiliate Settlement Deed, it enables the other affiliates to make distributions to their stakeholders.

iv) It will result in the payment of a substantial sum owed to LBHI2 by LBL.

v) It enables LBHI2 to make a substantial first interim distribution to its creditors.

vi) By virtue of making an interim distribution, it reduces the ongoing accrual of statutory interest on the claims in LBHI2's estate, thus optimising the potential return to LBHI2's subordinated creditors who are otherwise prejudiced by the delay.

vii) It limits the Sub-Debt claim currently owed by LBIE to Wentworth Sons Sub-Debt S.à r.l. (one of the Wentworth parties) to those assets ultimately available in LBIE for distribution to it without recourse to LBIE's contributories.

43. Although not a disadvantage for the creditors of LBHI2, Ms Bruce has identified that the Proposed Settlement will not require any reserve by LBHI2 in respect of a future contribution claim. Like the other applicants, however, the LBHI2 Administrators believe that the likelihood of a contribution claim is slight.

44. Finally, Mr Lewis identifies in his witness statement, the following advantages of the Proposed Settlement for LBH and its creditors:

i) LBL will withdraw and release the claims pursued against LBH in Waterfall III, by which LBL seeks to pass on any liability for a contribution claim to LBH or to rectify LBIE's share register so as to substitute LBH as a member of LBIE in its place.

ii) In addition to removing the threat of that liability, such release will remove the need for LBH to reserve for that claim (and no other party has asserted any claim of that sort), thereby removing the present block upon any distributions being made by LBH to its creditors (which might otherwise remain for several years to come while Waterfall III runs its course).

iii) The dismissal of Waterfall III will lead to substantial savings in legal costs and expenses.

iv) LBHI2 will not be obliged to continue to reserve for a contingent contribution liability as a member of LBIE, meaning that its administrators would be able to pay dividends to its admitted unsecured creditors. LBH has a substantial unsecured claim in LBHI2 which is to be admitted and form the basis of distributions to LBH, together with statutory interest, as part of the Proposed Settlement. There is also a possibility that LBH might in due course receive a return from LBHI2 in respect of LBHI2's subordinated debt liability to LBH and any such return will be increased to the extent that LBHI2 makes distributions to its unsecured creditors more quickly and thereby limits the accrual of statutory interest in that estate.

v) It is anticipated that as a consequence of the Proposed Settlement, LBEL will make a substantial distribution to LBH as its sole member.

vi) There will be an agreed resolution of intercompany positions as between LBH and the other affiliate entities, which reduces the scope for further litigation between those entities.

45. The only potential downside of the Proposed Settlement, or *quid quo pro*, that Mr. Lewis identifies is the mutual releases granted by LBH and the LBH Administrators to LBL and LBHI2 (and their respective joint administrators). However, the LBH Administrators consider that this does not affect any claims which are agreed or acknowledged as part of the Proposed Settlement, does not involve LBH withdrawing or conceding any known or asserted claims against LBL or LBHI2 and is rather a way of seeking to ensure finality in all parties' interests.

46. A common feature of the reasoning of all applicants as to the merits of the Proposed Settlement, and indeed a central driver for the negotiations which have led to the Proposed Settlement, is the view that a contribution claim by LBIE against either of its members is now unlikely or highly unlikely. In brief summary, the reasons are as follows.

47. First, as matters currently stand, the LBIE Administrators have no standing to object to LBIE's members making distributions to their creditors, since LBIE is not in liquidation. This position is confirmed by the decision of Lord Neuberger in the Waterfall I appeal at [165]. Further:

i) It is clear that the making of a contribution claim under section 74 is exclusively a liquidator's remedy and not one which is available to an administrator even as a contingent claim in the member's insolvency (see Lord Neuberger's judgment on Waterfall I at [164]).

ii) Moreover, whilst the Supreme Court's extension of the contributory rule to administrations (see ibid. at paragraph [186]) provides LBIE with some theoretical protection (specifically, by enabling the LBIE Administrators to retain funds reflecting the "*reasonable maximum potential liability as a contributory*" of each of its members out of any distributions which would otherwise be made to those members as LBIE creditors), this will be to no avail to the LBIE Administrators insofar as objecting to LBHI2 and LBL making distributions to their own respective creditors is concerned.

48. Secondly, and as a result, the only circumstance in which there might be any standing to object to the making of distributions by LBIE's members would be where LBIE moved into liquidation. However, it is most unlikely that LBIE will go into liquidation in the foreseeable future. In particular:

i) In light of the Supreme Court's decision in the Waterfall I appeal, any entitlement to statutory interest during the period of LBIE's administration would come to an end upon LBIE moving into liquidation. For that reason alone, it would be very difficult to justify moving LBIE into liquidation until such statutory interest (the precise quantum of which will not be known until the Waterfall II proceedings are finally determined) is paid in full.

ii) Secondly, LBIE's entry into liquidation would in any event attract various negative tax consequences.

49. Thirdly, even if LBIE were to move into liquidation (which is unlikely to be justifiable and is not intended, particularly in the foreseeable future, for the reasons given above), then any contribution claim which LBIE's liquidators might make against LBIE's members would only have any value at all in certain circumstances which are possible but prima facie unlikely. As to this:

i) In light of the Supreme Court's decision in Waterfall I, LBIE's liquidators could not make a contribution claim in respect of statutory interest.

ii) Accordingly, the contribution claim would only have any value in the event that: (a) in the pending appeal in Waterfall II, it were established (contrary to David Richards J's decision at first instance) that a non-provable claim to damages on the *Sempra Metals* basis exists; and (b) LBIE's surplus were insufficient to pay such non-provable claims.

iii) The LBIE Administrators' financial modelling shows that scenario (b) is likely only to arise if LBIE's creditors' entitlement to Statutory Interest were to be inflated as a result of either: (i) the Senior Creditor Group ("the SCG") succeeding on the *Bower v Marris* issue in Waterfall IIA (contrary to David Richards J's decision at first instance); or (ii) the SCG succeeding on the cost of funding issues in Waterfall IIC (contrary to my own decision at first instance in that case).

50. The applicants have also considered that they are under a duty to progress their administrations and, at least in some cases, are under pressure to do so from creditors.

51. While, on their evidence, the applicants have taken an independent view as to the merits of the Proposed Settlement, they have also sought to keep creditors informed and to provide them with the opportunity to express their views (save in respect of LBH where over 95% of its unsecured, unsubordinated creditors are either parties to the Proposed Settlement or under the control or influence of such parties). In particular, the applicants have:

    i) on their respective websites, announced the Proposed Settlement, summarised its key terms, made documents available to creditors and provided contact details for creditors to send any questions or comments in respect of the Proposed Settlement; and

    ii) made direct contact with major creditors regarding the Proposed Settlement and sought their views.

52. I am informed, and take into account, that no creditors have expressed any objection to the Proposed Settlement to date.

Conclusion

53. I have heeded the injunction that the Court should be cautious in giving approval which will prevent subsequent challenge.

54. However, it is apparent that considerable thought has been put into developing the Proposed Settlement over a period of several months by professional administrators with the benefit of professional legal advice. The presentation of the matter left me in no doubt as to the care with which the proposals have been developed. The evidence submitted in support is clearly expressed; and I have had the benefit of clear and helpful skeleton arguments and oral submissions from Counsel for each applicant.

55. I am satisfied that in each case what is proposed is within the administrators' powers; that each administrator (and Mr. Lewis in relation to LBH) genuinely holds the view that the Proposed Settlement will be for the benefit of the relevant company and its creditors; that the view each has reached has not been infected by any conflict of interest; and that the Proposed Settlement to be implemented by the documentation to which I have been taken is rational and not improper. I am further comforted by the fact that after being kept informed of the proposals no creditor has pursued any objection.

56. I therefore grant the applications for directions in respect of the Proposed Settlement.

57. Lastly, the LBHI2 Administrators sought an order pursuant to Rule 12.39(9) of the Insolvency (England and Wales) Rules 2016 that exhibit GEB5(B) should not be open for inspection without the permission of the Court. The other parties supported that application since all had agreed to confidentiality in respect of at least a substantial part of the exhibit. After oral argument, I acceded to that application, for reasons given in a separate ruling on 28 July 2017.