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# Lehman Brothers Insolvency Proceedings in the US, UK and Japan

#### The Bankruptcy Filing

Holdings"), the holding company for the fourth-largest United States investment bank, filed for protection under Chapter 11 of the United States Bankruptcy Code on September 15, 2008, marking the largest US bankruptcy filing in history. Following the filing in the Southern District of New York, the directors of Lehman Brothers International (Europe) and three of its UK subsidiaries, Lehman Brothers Holdings Plc, Lehman Brothers Limited and LB UK RE, applied for administration (a process similar to Chapter 11) in the UK. Four partners of PricewaterhouseCoopers have been appointed to act as the administrators. In addition, Bloomberg News reported this morning that Lehman Brothers Japan Inc. and Lehman Brothers Holdings Japan Inc. filed for bankruptcy protection today in Tokyo District Court. Nine of the thirty largest unsecured creditors in the US case are Japanese banks, reported to collectively hold in excess of US \$1.6 Billion in bank loan claims against Lehman Brothers Holding, Inc. According to Bloomberg reports, Lehman units in both Seoul, Korea and Hong Kong also suspended trading

Lehman Brothers Holdings Inc. ("Lehman

Of significance, the only Lehman entity to have entered bankruptcy in the US is Lehman Brothers Holdings Inc., the parent and holding company of numerous broker-dealer and other subsidiaries, including Lehman Brothers, Inc. and Neuberger Berman Holdings, LLC, among others. Lehman Holdings has stated publicly that it is exploring the sale of its broker-dealer operations, and is reportedly in discussion with a number of potential purchasers to sell its investment management division. The stockbroker subsidiaries of Lehman Holdings are not eligible for reorganization under Chapter 11 of the U.S.

Bankruptcy Code, under which the debtor's management and directors may remain in possession and control of operations under court supervision absent overriding circumstances. The only available option for broker-dealers under US bankruptcy law is immediate replacement of the debtor's management and directors by a bankruptcy trustee and liquidation under Chapter 7 of the Bankruptcy Code.

The US, UK and Japanese proceedings may have implications for counter-parties to financial contracts including swaps of all kinds, loan participations and guaranteed investment contracts involving Lehman, parties with accounts at Lehman, those settling trades with Lehman and those insuring or providing cover for Lehman debt, among others. The Federal Reserve has announced that it will assist in the orderly unwinding of positions involving Lehman in order to reduce the potential for dislocations and to maintain the smooth functioning of the financial markets, although the direction and extent of that assistance is unclear.

#### **Impact on Financial Contracts**

The filing of a US bankruptcy petition under Chapter 11 triggers an automatic stay which, when applicable, prevents creditors from exercising remedies against the debtor, including collection efforts and termination of contracts. At this time, the stay only applies to contracts to which Lehman Holdings is a party.

Importantly, the U.S. Bankruptcy Code excepts certain categories of investments from the usual restraint on remedial action. For example, the termination and setoff of mutual debts and claims arising under securities contracts, forward contracts, commodity contracts and repurchase agreements, as well as swap and forward foreign exchange agreements are excepted

The US, UK and Japanese proceedings may have implications for counterparties to financial contracts including swaps of all kinds, loan participations and *quaranteed investment* contracts involving Lehman, parties with accounts at Lehman, those settling trades with Lehman and those insuring or providing cover for Lehman debt, among others.

from the automatic stay. Although traditional swap contracts are typically covered by this exception to the automatic stay, it is unclear whether more complex contracts will be covered. Where not restrained by the automatic stay, such agreements with Lehman Holdings may be unwound at the option of the counterparty.

In the UK, an administration order similarly creates a stay preventing the exercise of any enforcement rights of creditors without the consent of the administrators or order of the court. However, similarly, under UK law there are exceptions to the stay in the case of financial collateral arrangements. "Financial collateral" is widely defined to include shares, bonds and other instruments giving rise to or acknowledging indebtedness if they are tradeable on the capital market as well as other securities giving rise to the right to acquire such shares, bonds and securities by subscription, purchase

or exchange giving rise to cash settlements. Furthermore, close-out and netting arrangements continue to take effect notwithstanding that the collateral provider or collateral taker is in administration. In the case of swaps, counterparties will refer in most cases to the provisions of the International Swaps and Derivatives Association Rules which provide for the event of one counterparty becoming insolvent.

#### **Accounts Held at Lehman**

Of additional concern is the status of cash and securities held by customers at Lehman. Securities laws provide that accounts held at Lehman are protected by insurance provided by the Securities Investor Protection Corp. (SIPC) which protects customers of a failed brokerage firm to the extent of a maximum of \$500,000 per customer, including a maximum of \$100,000 of cash claims. Certain investments, however, including com-

modity futures contracts and currency, and investment contracts which are not registered with the U.S. Securities and Exchange Commission under the Securities Act of 1933, are ineligible for SIPC protection.

#### **Our Capabilities**

Edwards Angell Palmer & Dodge LLP has established a task force to address the numerous and varied issues raised by the Lehman Holdings bankruptcy filing and the related Japanese filing and UK administration proceedings. Our team has broad experience in a wide range of restructuring and insolvency matters, including cross-border insolvencies, and we have insolvency, re/insurance, equity securities and debt and public finance professionals engaged on these issues, including lawvers on-site in both our New York and London offices. For more information, please contact one of the members of our team listed below.

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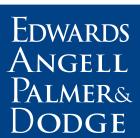
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