



Fellow of INSOL International

International Association of Restructuring, Insolvency & Bankruptcy Professionals

Global Insolvency Practice Course

The 2010-2011 Global Insolvency Practice Course is underway, drawing together a new cohort of some of the world's leading young professionals as participants. The course officially commences on 1st August when participants will have access to the course literature in preparation for Module A and start work on the first of three written papers. Module A will start with a Welcome Dinner on Sunday 3rd October. The programme commences in earnest on Monday 4th October and is being held at University of London. There are still some last minute places available on the course. The brochure is

available on our website or from Penny Robertson at pennyr@insol.ision.co.uk

One of the many benefits is the strong professional and personal relationships that are built up over the course of the programme. These have developed into the INSOL Fellowship Alumni. Fellows contact details can be found on the INSOL Fellow page at our website www.insol.org. One benefit of the Alumni is the opportunity for Fellows to showcase cross-border cases they have been working on in INSOL World. The first of these articles focuses on Lehman by INSOL Fellow Edward Middleton, KPMG China. 🌐

The Life and Times of a Lehman Liquidator



By Eddie Middleton
KPMG China
Fellow, INSOL International

INSOL Fellow Eddie Middleton is the Head of Restructuring Services at KPMG China. He was attending the Module B of the INSOL Fellowship course prior to the INSOL Shanghai Conference in 2008, the weekend that Lehman Brothers became the world's largest bankruptcy. Eddie hurried to the airport and by the Wednesday of that week he and partners of his firm in Hong Kong (Paul Brough and Patrick Cowley) and Singapore (Peter Chay, Bob Yap and Roger Tay) had been appointed to the first three of what became a succession of liquidation appointments over the Lehman entities in those jurisdictions. Between them, these companies comprise the major bulk of Lehman's presence in Asia ex-Japan. In this article, Eddie recalls the excitement of those early days, and shares some of the – occasionally hair-raising – experiences that can attend on the life of an insolvency practitioner in Asia.

Even in the best of economic times the life of an insolvency practitioner is rarely dull. At times, however, the Lehman liquidation in Asia has seemed more akin to the script of an Indiana Jones movie! We've had lifts in borrowed Indonesian police helicopters over the dense forests of Borneo to view a toll road, speedboat rides

across crocodile-infested waters (baboons watching from the banks) to view a coal mining facility in Kalimantan, spent time analysing the impact of the 'red shirt' protests in Bangkok on real estate values in Thailand and dotted the last 'I's and crossed the last 'T's on settlements in late-night Singapore bars, after days of negotiations. And, in parts of emerging market Asia, there is still (unfortunately) a degree of personal risk attached to asset recovery efforts, and we've had unwelcome trials and tribulations along that road as well. So, while we have trading books full of repos, reverse repos, derivatives and other exotic trades (the use of which has been widely examined and debated at length in the world's media), for our teams in Asia it is the realization of assets that will provide us with the most stories to bore the grandchildren with.

Part of the reason for this is the age-old problem of Recognition. Since the explosion of international trade a couple of hundred years ago, and the development of insolvency legislation that went with it, office holders have always had a nervous wait to see what reception they would receive when they left their home jurisdiction in hopes of bringing back whatever juicy fruits remained of the intrepid entrepreneur's failed enterprise. Whilst one or two countries in the Asia-Pacific, notably Australia and Japan, have brought in versions of the UNCITRAL Model Law on Cross-Border Insolvency, the Lehman liquidation is taking us into jurisdictions where the bright sun of that particular legislation is yet to shine. This shouldn't be too surprising since it was only the Asian financial crisis of 1997 – just 13 years ago – that prompted many of these countries to modernise existing insolvency legislation and in some cases, introduce it for the first time. With memories fading of such glorious restructurings as

Thai Petrochemical Industries and Asia Pulp & Paper, since that time, Asia has generally been a massive growth story. This perhaps explains the lack of political and commercial pressure being brought to bear on insolvency legislation, to ensure that it is embedded, modernized, and relevant, if always unwanted, by market enterprise economies.

So, what have been some of the more interesting examples? Japan is one. Here, the Lehman Hong Kong unit that acted as the group's regional funding hub, is owed several billion US dollars by Lehman's Japanese subsidiaries, which are being wound down under Japan's Civil Rehabilitation Law. Many of the relevant reorganization plans have been approved by creditors but some have now become the subject of challenge by certain creditor groups arguing that Lehman's inter-company debt should be subordinated to all other debt, even though Japanese insolvency law states that all creditors should be treated on a *pari passu* basis. Thus far, at least, such arguments have not found favour with the Japanese courts.

We face a similar situation in Germany, where we are involved in a very complex and intellectual debate about whether significant commercial deposits placed by the Lehman Hong Kong estates with Lehman Brothers Bankhaus, a German bank, on the normal commercial terms (the interest rate on offer was much more attractive than that available in Hong Kong), are caught by those provisions of German insolvency law that do provide for subordination of inter-company debt. If they are so caught, the implications for our creditors are very significant indeed since not only would our claims be subordinated but, also, we are told, there is a risk that such deposits would not be protected under the German deposit protection scheme.

And while we're talking legislative hurdles, I should also mention Australia where Deeds of Company Arrangement, although achieving the voting majorities necessary for support were successfully challenged in the Australian High Court on the basis that third party releases (in our case, releases to Lehman Brothers entities outside of Australia) were found to be beyond the scope of what such a Deed could encompass. I am told that this case has at least served to clarify certain important aspects of insolvency law in Australia, so there has been benefit from that point of view.

In terms of the proprietary investment book, we've had (and are continuing to have) fun and games realizing our book of real estate investments. Around 17% of Lehman's global real estate investment assets were in Asia, with heavy concentrations in Japan, Thailand and China. In Thailand we've run up against the full menu of issues, from the most aggressive of challenges to the liquidators' authority all the way through to having to deal with the political turmoil that has afflicted the country this year. Most of the assets that we are dealing with in Thailand are either tourism assets on the more popular islands or are

located in the heart of Bangkok itself. Even before the 'red shirt' protests took hold, the valuation and realization of these assets was problematic, but it has been made even more difficult as a result of those protests. How long will it take for the Thai tourist market to pick up again and, thus, make valuation of those assets possible again? How are the owners/borrowers impacted as a result of what has happened? Progress has been and is being made and recoveries to date have been very encouraging.

China meanwhile, has been a sweet spot for asset realisations. Assets in China accounted for about 40 percent of the real estate portfolio that we are dealing with. At the time of writing, we have realized all but two of our positions and look set to recover 95% of the total principle outstanding at the time of our appointment as Liquidators. We've had a number of cases where, despite Lehman's own collapse, the realizations achieved have been at or near the rates of return that Lehman expected when the original investment was made. Most of the transactions have so far involved the sale of assets back to the issuers or borrowers. This is our preferred strategy because it enables the borrower to self finance along with our assistance in a manner that does not erode value for our creditors unnecessarily. I think it is also reflective of the property boom that has been taking place in China in the last few years, which the government is now actively seeking to curtail.

Most recently we have sold US\$620m of Lehman's portfolio of loans, bonds and equity positions in the region. The transactions, which achieved an average recovery rate of 100%, represented the first major disposals from the US\$2.6 billion "principal investments and loans" portfolio built up by Lehman in Hong Kong. The team is now realizing a further US\$300 million of the portfolio, which is mostly comprised of investments in China and India.

Just a few weeks into the Lehman engagement, I had to complete the final stage of the INSOL Fellowship course; the dreaded, week-long virtual restructuring case. For the three of us doing the course from Hong Kong the timing could not have been worse – we had to do it from 4:00 a.m. Hong Kong time. The Fellowship course didn't seem like such a great idea at that time, I can secretly reveal, until I hatched a cunning plan of Machiavellian conceit; playing the role of a financial institution creditor; I did what so many of them do in real life; I found a greater fool (one of my fellow candidates in Hong Kong) – and traded out of the position as quickly as I could! My hitherto undiscovered negotiation and valuation skills saw that my virtual institution got out at a virtual 100, so I promptly awarded myself a virtual bonus of several million dollars, went home to bed for all of about 18 minutes and hurried back to the office to play the game again – but this time for real! 🙄

We are working closely with the teams from PPB, led by Neil Singleton, Tony Sims, Steve Parberry and Marcus Ayres in Australia; with Nobutaka Tanaka of Ohehashi in Japan and Dr Michael Frege and Felix Schaefer of CMS Hasche Sigle in Germany.