

The David Doble Solicitors Publication for Institutional Investors

Holdings of Lehman repackaged and structured Notes – Dante Multi Issuer Secured Obligation Programme

In this edition of Legal Issues, we examine how **the small print in the documents could mean the difference between a loss and the recovery of 100% of the investment.**

Institutional investors that hold repackaged or other structured Notes from Lehman Brothers have no doubt been busy trying to assess the value of such instruments and what actions they should take to protect the value (if any) of their positions.

This newsletter focuses specifically on Notes issued under the Multi Issuer Secured Obligation Programme arranged by Lehman Brothers International (Europe). Many series of Notes under this

Programme were sold in bespoke transactions to institutional investors around the globe. In particular, we look at the provisions found in many of those transactions relating to the rights of Noteholders in circumstances where the Notes become subject to early redemption as a result of the insolvency of the Swap Counterparty (one or other Lehman entities).

The Programme enabled a range of special purpose vehicles (SPVs) to issue repackaged notes¹. Some series of Notes were secured on the SPV's rights under a swap agreement with one or more Lehman entities. In the event that the Notes were to be redeemed prior to their Maturity

Date, there may not have been sufficient value in the Collateral for those transactions to ensure that Noteholders would be repaid principal in full. Typically, any amount due to the Swap Counterparty as a result of the early termination of the Swap Agreement would rank above the claims of Noteholders. **However, there is a notable and crucial exception in many of these transactions in the event that the Notes become repayable prior to the Maturity Date as a result of the termination of the Swap Agreement caused by an Event of Default of the Swap Counterparty (or the Swap Counterparty Guarantor).**

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Many transactions under the Lehman Secured Obligation Programme contain a provision of key importance – in the following terms (or similar) in relation to the so-called “Order of Priorities”:

“[If] an Event of Default (as defined in the Swap Agreement) occurs and the Swap Counterparty is the Defaulting Party (as defined in the Swap Agreement).... Noteholder Priority shall apply”.

This means that Noteholders of each relevant series may well be entitled, in the present circumstances of an Event of Default under the Swap Agreement by the one or other Lehman entities, to recover amounts due to them under the Notes before any amount is payable to the Lehman entity (or its administrator) under the Swap Agreement. Clearly, the difference in the recovery amount for Noteholders could be extremely significant.

Noteholders should be aware that the position would be very different if the Notes were to be redeemed

by relying on the Event of Default provisions in the Notes – which are likely to have become capable of being triggered by a non-payment of interest on the Notes. In such a case, the Order of Priorities would almost certain relegate the rights of Noteholders below those of the Swap Counterparty – despite the fact that the Notes have become repayable as a result of the Swap Counterparty’s default under the Swap Agreement!

Accordingly, it is very important for investors in any series of Notes issued under the Lehman Secured Obligation Programme to examine the legal documentation very closely. Failure to understand these fine distinctions in their rights may well incur significant and unnecessary losses for investors. Ongoing developments in the chapter 11 proceedings with regard to Lehman Bros. in the U.S. make it important that Noteholders address this issue sooner rather than later.

(1) the SPV issuers under the Programme include: ANGIOLIERI FINANCE PLC, AQUAMARINE FINANCE PLC, BERYL FINANCE LTD, BOCCACCIO FINANCE PLC, CITRINE FINANCE PLC, DIADEM CITY CDO LIMITED, DIAMOND FINANCE PLC, GMG FINANCE LIMITED, JUPITER QUARTZ FINANCE PLC, LION CITY CDO LIMITED, MERLIN FINANCE S.A., ONYX FUNDING LIMITED, PEARL FINANCE PLC, PETRARCA FINANCE PLC, QUARTZ FINANCE PLC, RUBY FINANCE PLC, SAPHIR FINANCE PLC, TOPAZ FINANCE LIMITED AND ZIRCON FINANCE LIMITED.

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Legal advisory to institutional investors...

David Doble Solicitors was established in London in 2005 to provide legal advice to institutions, within Europe and beyond, investing in complex structured financial instruments.

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