

**From:** [Ada Li](#)  
**To:** [Jeff Stehm](#); [Patrick M Parkinson](#); [Pat White](#); [Jeffrey Marquardt](#)  
**Cc:** [Theodore Lubke](#); [Wendy Ng](#)  
**Subject:** Fw: Bankruptcy doc  
**Date:** 09/12/2008 09:15 AM  
**Attachments:** [Decision to file Bankruptcy 4.doc](#)

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FYI --also for the 9 AM meeting.

Thanks,  
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----- Forwarded by Ada Li/NY/FRS on 09/12/2008 09:15 AM -----

**Lily Tham/NY/FRS**

09/12/2008 01:28 AM

To Theodore Lubke/NY/FRS@FRS  
cc Michael Schussler/NY/FRS@FRS, Steven Pesek/NY/FRS@FRS, Wendy Ng/NY/FRS, Ada Li/NY/FRS, Shari Ben-Haim/NY/FRS@FRS, mcgowant@sec.gov  
Subject Bankruptcy doc

Hi, Theo,  
Attached is the latest version **Decision to File Bankruptcy** document prepared by Tom McGovan and Michael Schussler. I'll leave it to you to pass on to the broader mailing list, as appropriate.

I'll be in the office around 8:30am tomorrow. Thanks!



Decision to file Bankruptcy 4.doc

### **Decision to file Bankruptcy**

Lehman Brothers Holding Inc. (“Lehman”) would need to resolve a number of complex issues before electing to file for bankruptcy protection. The issues include (1) which entities are eligible for bankruptcy protection; (2) which entities are subject to customer claims that would be effectively stayed by a bankruptcy filing; (3) would regulatory interests be inconsistent with management’s reasons for seeking bankruptcy protection; (4) when should a filing take place.

The decision by the board to seek bankruptcy protection for the holding company does not necessarily imply that each subsidiary also will be subject to the bankruptcy proceeding. We would expect that many of Lehman’s material affiliates would not seek bankruptcy protection. The applicable authority for initiating insolvency proceedings for these affiliates is described below.

#### **Timing of Bankruptcy Filing**

One option would be to urge Lehman to file mid-afternoon (such as Sunday before 6:00 p.m.) to provide markets, clearing entities, and counterparties time to react to the filing. However, it may be less disruptive to the tri-party repo market if a filing delayed until after the morning unwind. In contrast, Lehman may have an interest to file at a different time even though filing at that time may be more disruptive to the markets. Our expectation is that the firm would work with regulators to file for bankruptcy at such a time that would minimize disruption to the markets.

#### **U.S. Depository Institutions**

With respect Lehman’s thrift and ILC, only the chartering authorities or the FDIC have authority to place the entities into receivership or into other insolvency proceedings. Neither the thrift nor the ILC can be subject of a voluntary or involuntary insolvency proceeding. Regulators can monitor the liquidation of the holding company and other entities that are in bankruptcy as well as the operations of the thrift and ILC to determine what steps may be appropriate if those firms face financial or operational difficulties.

ILC	-	Lehman Brothers Commercial Bank
Thrift	-	Lehman Brothers Bank, FSB

#### **U.S. Registered Broker-Dealers and Investment Advisors**

If Lehman filed for bankruptcy, assuming the broker-dealer remains in compliance with applicable regulatory requirements, the SEC would work towards ensuring that the broker-dealer self-liquidate and not be part of a formal insolvency proceeding. With respect to the U.S. registered brokers, a broker-dealer with “customers” would not be eligible for Chapter 11 (Reorganization). Accordingly, Lehman Brothers, Inc. and Neuberger Berman LLC. would not be eligible to be included in a Chapter 11 reorganization. Further, as a policy matter, the SEC would require that Lehman Brothers Inc. be liquidated under SIPA, if a formal liquidation was appropriate. Unless the broker-dealer was not in compliance with the financial responsibility rules, the preference would be that Lehman Brothers Inc. self-liquidate under the supervision of

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the SEC, the CFTC, and self-regulatory organizations. We note that Lehman Brothers, Inc. has two significant subsidiaries, a derivatives affiliate and a commercial paper dealer. Those entities would likely be liquidated separately from the broker-dealer.

Neuberger Berman also owns a registered investment advisor that would be eligible for Chapter 11 bankruptcy; however, a Chapter 11 filing would likely cause assignment of advisory contract and change of control regulatory issues for the advisor.

Lehman Brothers OTC Derivatives Dealer, Inc., a registered limited purpose broker-dealer, may be a “stockbroker” under the bankruptcy code and would therefore not be eligible to be reorganized under Chapter 11. The OTC derivatives dealer is not a member of SIPC and would not be liquidated under SIPA.

### **Other Derivative Dealers and Material Unregistered Affiliates**

There is a great deal of uncertainty regarding how unregistered Lehman affiliates would be liquidated. Lehman owns a number of unregistered derivatives dealers, such as Lehman Special Financing, Inc., and other material entities such as Lehman Commercial Paper, Inc. These entities are eligible for Chapter 11 and Chapter 7 bankruptcy. However, the holding company may elect not to seek bankruptcy protection for these firms, especially if these firms remain sufficiently capitalized and liquid. The derivatives dealers also may also meet the definition of a “stockbroker” under the bankruptcy code and therefore only be eligible for liquidation under Chapter 7. Unregistered affiliates include ALI, Lehman Brothers Commercial Corporation, Lehman Brothers Derivatives Products, Lehman Brothers OTC Derivatives, and LB1 Group.

### **Foreign Subsidiaries**

Lehman owns a number of foreign entities, some of which are registered as banks or securities firms in their respective foreign jurisdictions. These entities would be subject to foreign bankruptcy regimes. At the discretion of the appropriate local authorities, their proceedings could be handled separately or as part of a U.S. bankruptcy proceeding. Key foreign entities are Lehman Brothers Bankhaus, AG (German bank - BaFin), Lehman Brothers International Europe (U.K. broker-dealer – U.K. FSA), Lehman Brothers Europe LTD. (U.K. FSA), Lehman Brothers Finance SA (unregistered), Lehman Brothers Japan (broker-dealer, Japan FSA), Lehman Brothers Luxembourg SA (unregistered), and Lehman Brothers Treasury Co. BV (unregistered).

### **Actions by U.S. Regulators upon Lehman Bankruptcy Filing**

Supervisors would need to review whether to take any action in response to a bankruptcy filing by Lehman. Further, supervisors would monitor the formal and informal self-liquidations of Lehman and its affiliates to determine whether regulatory action should be taken. Particular events which may require supervisors to reconsider their decisions would include actions taken by clearing houses and clearing banks, decisions by foreign regulators, a determination that a bank or broker-dealer is no longer in compliance with applicable regulatory requirements.

**Securities Investor Protection Act of 1970 (“SIPA”)**

Generally, all U.S. registered broker-dealers are members of the Securities Investor Protection Corporation (“SIPC”). SIPC may seek to begin a SIPA proceeding if any member of SIPC has failed or is in danger of failing to meet its obligations to customers, and the broker-dealer

- (i) is insolvent;
- (ii) subject to a proceeding pending in any court or before any agency of the United States of any State in which a receiver, trustee, or liquidator has been appointed;
- (iii) is not in compliance with applicable SEC or self-regulatory organization financial responsibility rules or hypothecation of customers’ securities; or
- (iv) is unable to make such computation as may be necessary to establish compliance with those financial responsibility or hypothecation rules.

The broker-dealer has the ability to consent or object to the application to place the firm in a SIPA proceeding. If the broker-dealer objects, the application shall be heard three business days after the date the application is filed, or at such other time as the court may determine taking into consideration the urgency which the circumstances require. If the broker-dealer does not consent to the SIPA liquidation, SIPC will look to SEC or FINRA examiners to demonstrate that the firm is not in compliance, or is unable to demonstrate compliance, with the applicable financial responsibility rules. In the event of a SIPA proceeding for a large broker-dealer, the court would appoint a person specified by SIPC to serve as the trustee to administer the liquidation.

Generally, a “customer” is defined in SIPA as a person who has a claim on account of securities received, acquired, or held by the debtor in the ordinary course of its business as a broker-dealer from or for the securities accounts of such person for safekeeping, with a view to sale, to cover consummated sales, pursuant to purchases, as collateral security, or for purposes of effecting transfer. SIPC has taken the position that counterparties to repurchase transactions and securities lending are not customers under SIPA.

A SIPA liquidation would likely proceed in a similar manner as a self-liquidation. The trustee would look to complete a bulk transfer of securities accounts to a solvent broker-dealer as quickly as possible. However, even after the trustee has completed returning all customer property, a SIPC liquidation may continue as the trustee seeks to collect amounts owed to the broker-dealer or SIPC