



What's this about Lehman Derivative contracts being unenforceable?

The Metavante/Lehman case has been getting a lot of press lately. An Asian financial news source ran an article last week that got picked up by a number of blogs, perhaps due to its catchy headline. The headline mentioned a court decision that Lehman derivative contracts are "Unenforceable." We thought it could be helpful to restate a few of the facts and highlight the issues, since this case clearly has implications for other non-defaulting counterparties.

Metavante was a non-defaulting party that did not attempt to terminate its Lehman swap following the bankruptcy but did begin withholding its periodic swap payments to Lehman based on ISDA provision 2(a)(iii). In an oral decision on September 15, 2009, the bankruptcy court ruled that Metavante must pay the withheld payments, with interest. Additionally the judge categorized the Metavante swap as an executory contract, which could result in the swap not falling under the umbrella of the Safe Harbor Provisions. The largest benefit of Safe Harbor is the non-defaulting party's ability to terminate, accelerate, or liquidate a swap agreement in response to a counterparty's Chapter 11 filing.

Does this mean the ISDA is therefore unenforceable? ISDA doesn't think so. In fact, ISDA sent out a letter that included the following:

- 1) An ISDA reassurance that this decision was not a surprise.
- 2) A clarification that the Metavante ISDA Master Agreement is "alive and well".
- 3) An acknowledgment that the court decided Metavante delayed too long before exercising a termination.

The court ruling seems to indicate that a non-defaulting party should either terminate its trades promptly or keep making its swap payments until it terminates. What could this mean for other non-defaulting parties?

- 1) Non-defaulting parties that withheld payments but did not terminate will likely need to make those payments plus default interest.
- 2) Non-defaulting parties that waited longer than 11 months to terminate have probably waived the right to terminate at this point.

The big question still running in the background remains whether the court will declare the ISDA to be unenforceable, but we think it's too early to conclude that decision has been made. We echo what Mark Twain might have said:

"The reports of ISDA's unenforceability are greatly exaggerated."

As a reminder, the bankruptcy court did approve the Alternative Dispute Resolution

(ADR) process. If you have been contacted by Lehman about settling your position, please don't hesitate to get Chatham involved along with your legal team. We expect Lehman to start working through their "in the money" derivatives contracts in the near future and delivering Derivatives ADR Notices. We have helped almost 50 clients assign or terminate over 100 derivative contracts and would welcome the opportunity to talk about your situation.

Contact us to discuss your Lehman termination:

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ADR Procedures are a "GO"

Bloomberg.com reported yesterday afternoon that the bankruptcy court authorized Lehman to proceed with the proposed Alternative Dispute Resolution (ADR) Procedures. Judge Peck was quoted by Bloomberg as saying, "I think these procedures are quite appropriate."

The ADR Procedures were initially proposed this July and have been reviewed and modified in recent weeks. While both Lehman and the non-defaulting party are expected to be required to participate in the process, the process is not expected to require a resolution-- parties can always continue the dispute in court. In general, the mediation procedure is expected to follow the process outlined below:

1. **ADR Notice.** Lehman sends the non-defaulting party a Derivatives ADR Notice containing the payment demand and a brief explanation describing why the amount is being demanded.
2. **Statement of Position/Response.** The non-defaulting party has 20 calendar days to respond to Lehman's ADR Notice with a Statement of Position including a Response (either Agree to Settle or Deny Demand). Failure to respond could send the process directly to mediation.
3. **Lehman Reply.** Lehman must reply to the non-defaulting party's Response within 15 days, either modifying the Demand, providing additional info, making a counteroffer or rejecting the Response entirely. Denying the non-defaulting party's Response would send the process directly to mediation.
4. **1-hr Call.** At any point after delivery of the initial Derivatives ADR Notice, either party may request a 1-hour conference call that must occur within 5 days of the request. Both parties' counsels and advisors may participate in this call.
5. **Mediation.** Once Lehman has provided their Reply, if the dispute isn't resolved then the process moves to mediation. The business principal from the non-defaulting party will likely be able to participate via video-teleconference.
6. Ultimately, if resolution isn't achieved through the mediation process and both parties are deemed to have cooperated in good faith, the dispute process continues either informally or in court.

If you are considering terminating a Lehman derivative contract or have already been contacted by Lehman with an ADR Notice, please don't hesitate to get Chatham involved along with your legal team. We have helped almost 50 clients assign or terminate over 100 derivative contracts and would welcome the opportunity to talk about your situation.

Reminder: just 6 days until the September 22 Bar Date!

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Refusing to "Pay to Play"

Several non-Debtor counterparties have received attention on the Lehman bankruptcy docket in recent weeks for derivatives-related issues, including Metavante, Chicago Board of Education and MEG Energy Corp ("MEG"). While other forums have discussed Metavante and the Board in detail, we have heard less discussion about the MEG Energy case, in which Lehman Brothers Special Financing Inc ("LBSF") requested authorization to assume a set of derivative contracts. If this request is authorized by the bankruptcy court, Lehman will have another play in its playbook, which would be useful for capturing withheld swap payments in certain situations.

The Background. MEG is a counterparty to LBSF in four separate interest rate swap contracts and began withholding net payments to Lehman under those swaps. Their basis for not making the payments was Section 2(a)(iii) of the ISDA which requires payment to be made subject to "the condition precedent that no Event of Default...with respect to the other party has occurred and is continuing". The swaps total \$350mm in notional and mature at the end of December 2010. Due to the path 3-month LIBOR has taken over the past year, MEG has been a net payer for quarterly swap payments to Lehman, which total almost \$10mm.

Perusing the documentation on the docket, we modeled the swaps in question to determine the next payment that would be due and the current mark-to-market value. Based on recent 3-month LIBOR rates and current expectations for 3-month LIBOR through 2010, the swaps are in a net liability position to MEG on the order of \$20mm, not including the net payment of roughly \$4mm that will be due at the end of this month.

The Motion. According to the motion filed on the docket, the bankruptcy court could allow LBSF to assume these swaps, provided LBSF cures any Event of Default prior to assuming the contracts. Once cured, these swaps would be active again, immediately putting MEG on the hook for withheld payments and interest. Failure by MEG to make these payments would result in a "Failure to Pay" default under the ISDA.

The Problem. While we are not lawyers, it logically appears that whether LBSF can cure the Event of Default or not is the big issue. MEG cites the LBHI bankruptcy filing as the Event of Default that allowed MEG to withhold payments. Therefore, to cure the LBHI bankruptcy, LBSF either needs to travel back in time and somehow prevent the September 15, 2008 bankruptcy event, or the court needs to rule that the Event of Default is no longer enforceable.

The hearing is scheduled for next week to see what the bankruptcy court will do. Lehman's position is that MEG needs to "Pay to play". Reading into that statement a bit, if MEG does not "pay" the Unpaid Amounts, they may not be allowed to "play" in the ADR Procedure process later this year. Drawing a broader conclusion, if LBSF is allowed to assume the contracts, we could see this play used more often in situations

where the non-defaulting party cited LBHI's bankruptcy filing as the sole reason for withholding payments.

The cases to date have focused more on counterparties with extreme positions or very large disputed amounts. While the ISDA gives the non-defaulting party certain rights; a bankruptcy event does not allow the non-defaulting party to carte blanche walk away from financial obligations. Chatham is monitoring these on-going cases to extract the pertinent precedents being set that will affect the masses. We continue to work with many clients seeking to resolve Market Quotation and Loss settlements that were calculated using commercially reasonable means.

Reminder: just 11 days until the September 22 Bar Date!

If you are considering terminating a Lehman derivative contract or have been contacted by Lehman with an ADR Notice, please don't hesitate to get Chatham involved along with your legal team. We have helped almost 50 clients assign or terminate over 100 derivative contracts and would welcome the opportunity to talk about your situation.

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Derivative "Hobgoblins of the Night"

While we haven't seen the transcript yet from Wednesday's hearing, it sounds like the bankruptcy court will authorize Lehman to move forward with the alternative dispute resolution (ADR) procedure, with some modifications to the original motion. One of the remaining open items appears to be whether the creditor committee should be able to be involved in the mediation. Otherwise, the Order would appear to be very similar to the black lined version that Lehman has recently modified in response to numerous objections filed by active counterparties.

Responding to those objections, Lehman filed an omnibus response on Monday of this week. In the 99-page document, Lehman repaints the current picture: thousands of derivatives contracts are still open, resulting in a complex administrative, financial and legal problem, and solving the problem quickly and efficiently is the goal of the ADR Procedures.

We touched on several of Lehman's modifications to the ADR Procedure motion as a result of the objections in our last update, but wanted to summarize Lehman's response to the set of objections they received. From the omnibus response:

"The number and complexity of the Debtors' Derivatives Contracts are unprecedented for a Chapter 11 case...No prior Chapter 11 debtors, including those in Enron, has had as many or as complex derivatives contracts as are involved in these cases...The Derivatives ADR Procedures represent the next critical step in the Debtors' global strategy to capture and maximize the value of Derivatives Contracts with Recovery Potential by expediting in the least expensive manner the resolution of disputes involving Derivatives Contracts."

While Lehman addresses the objections line by line in their omnibus response, Lehman also highlights "five fatal fallacies" from their point of view underlying the objections:

1. Non-defaulting parties think their read of the law is correct.
2. Non-defaulting parties assume Lehman will act in bad faith.
3. Non-defaulting parties assume Lehman will let the contract obligations go away-"that is not going to occur."
4. (My favorite): Non-defaulting parties "conjure hobgoblins of the night, ignoring that the Derivatives ADR Procedures are non-binding." The omnibus response sums up the ADR Procedure as: "Simply stated, the mediator is not a decision-maker...Counterparties can decline to settle if good-faith efforts fail."

If you are considering terminating a Lehman derivative contract or have been contacted by Lehman with an ADR Notice, please don't hesitate to get Chatham involved along with your legal team. We have helped almost 50 clients assign or terminate over 100 derivative contracts and would welcome the opportunity to discuss your situation and possible next steps.

5. Non-Defaulting parties fail to recognize that mediation is better than litigation. "The Objections also ignore the alternative: the Debtors could commence an adversary proceeding in this Court."

Fallacies aside, the court appears to have taken the creditor committee objection under consideration, and we will provide another update as soon as we have more information on that point. Since it appears that an ADR Procedure will be approved, if you have an active derivative contract (e.g. you have not received a termination agreement), you should expect to receive an ADR Notice from Lehman in the near future. The ADR Notice will be the first step in the procedure, followed by a one-hour call. We talked about the proposed ADR procedures in detail in our updates #6 and #8--please let us know if you would like to receive copies of those updates, or just give us a call. We want to be a part of your team to help navigate through this process as your financial advisor.

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Proposed Modifications to the Alternative Dispute Resolution Procedures

More than 60 counterparties filed objections to the proposed Alternative Dispute Resolution (ADR) Procedure motion, resulting in a delay of the hearing to August 26, 2009. A blackline showing proposed changes to the motion was also posted to the docket.

We discussed the proposed ADR Procedures in detail in our Newsletter #6, but wanted to re-cap a few of the highlights and include updated information from the proposed changes to the motion (in italics). The ADR Procedures would require non-defaulting parties with unresolved or active derivative contracts with Lehman to comply with the following:

- Respond to Lehman's ADR Notice within 20 calendar days with a Statement of Position including a Response (either Agree to Settle or Deny Demand). *The blacklined motion proposes Lehman include a brief explanation describing the demand and why the amount is being demanded.*
- Lehman would have 15 days to reply to the non-defaulting party's Response, either modifying the Demand, providing additional info, making a counteroffer or rejecting the Response entirely. Originally the motion allowed for Lehman to "fail to respond" to the Response; *however, the blackline alters the language such that Lehman would be required to respond.*
- Once Lehman has provided their Reply, if the dispute isn't resolved then the process moves to mediation. Originally the business principal from the non-defaulting party would have been required to appear in person. *The proposed change in the blacklined motion would allow the principal to appear via VTC at the non-defaulting party's expense.*
- Ultimately, if resolution isn't achieved through the mediation process and both parties are deemed to have cooperated in good faith, the dispute process continues either informally or in court. The ADR Blackline clarifies that the ADR procedures would not *"result in either parties rights, remedies, claims and defenses [being] impaired, waived or compromised in any further proceedings should no settlement or compromise result from participation in these Derivatives ADR Procedures."*
- One last point to highlight from the blackline, *the mediator will provide monthly updates to the court including the number of ADR Notices served on Derivatives Counterparties, the number of settlements reached after mediation, the number of mediations still pending, the number of mediations that have terminated without settlement, and the cumulative dollar amount of settlements reached with Derivatives Counterparties following service of ADR Notices.*

Resolving the derivatives dispute at a fair price appears to be the optimal outcome, simultaneously providing an acceptable compromise on the termination value while also removing future litigation risk. At a certain absolute dollar amount, we expect that

Lehman will no longer be able to negotiate at a sufficiently acceptable discount.

One data point this week was that we saw a relatively small contract settled with Lehman at a significant discount to the mark-to-market value. This data point contradicts our experience to date in discussing the "Try to Settle" course of action (from our Newsletter #7) with corporate clients and prospects, presumably due to the order of magnitude difference in payment amount. Chatham worked on the client's behalf to obtain preliminary market quotations and calculate an ISDA-based termination amount for the client to use in negotiation with Lehman. While the original proposed termination amount was not accepted by Lehman, the methodology for a counteroffer was spelled out and agreed to. In the end, the client was able to terminate the derivative contracts at a substantial discount to the mark-to-market value.

Give us a call and we would be happy to fill in a few of the details and see if we can help you negotiate a fair termination value under the terms of the ISDA agreed to by both parties.

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Three Alternatives to Consider for Non-Defaulting Parties

In our last newsletter we outlined the alternative dispute resolution (ADR) motion that Lehman filed and the impact that it could have on a non-defaulting party if Lehman gained the rights of the Calculation Agent as a result of the ADR procedures. While we are not attorneys (corporate, contract, bankruptcy or otherwise) we have read the ISDA and we have a business advisor's perspective on three possible courses of action a non-defaulting party can take:

1. Let It Ride. In light of the Bar Order Date and ADR motion, it is uncertain how Lehman will take action on active derivative contracts, and you might opt to leave your derivative contract in place. This is a popular alternative and could have the following outcomes:

Best case outcome. For active trades, the best case requires rates to move in your favor resulting in a more favorable mark-to-market termination amount; otherwise it would be better to terminate today for the full mark-to-market value. Waiting to see what will happen means taking a risk that the market improves, but the hope would be that rates improve relative to your current position resulting in a more favorable absolute termination value.

Worst case outcome. The worst case would be that rates move against your position from today through the day that Lehman delivers a termination notice and the mark-to-market value on that date is significantly worse than today's. In this case you would wish you had terminated prior to the notice, because you would either need to pay the higher amount or dispute the amount, potentially in litigation.

Regardless of the outcome, the biggest benefit to "letting it ride" until Lehman requests a termination value, is that once the termination value is paid you can put the issue behind you.

2. Try to Settle. Instead of leaving the contract in place until Lehman contacts you, you might decide to proactively reach out to Lehman to mutually agree on a termination amount. In a pre-bankruptcy world, that termination amount should equal the mark-to-market value plus transaction costs. However, since the reason you would try to terminate the contract now is that a bankruptcy event has occurred (and is continuing) you might feel that the current termination value should be at a discount to the mark-to-market value.

Best case outcome.

The best case scenario is that you are able to negotiate a payment better than 95 to 100 cents on the dollar (which is where we estimate Lehman may start the discussion). This is an area where Chatham can help arm you with market information and an understanding of the ISDA process that you can use to level the playing field and substantiate your offer.

Worst case outcome.

Worst case, Lehman might require that the full mark-to-market amount be delivered. If rates were to move against your position during the negotiation process, this could result in a worsening value. Eventually you would need to either terminate under the ISDA (if you still have this ability based on future court rulings) or pay the mark-to-market amount to Lehman. As with the "Let It Ride" option, the benefit to mutual settlement is the removal of future litigation risk and the ability to put this issue behind you.

3. Follow an ISDA Termination Process. Under an ISDA Termination process, you would follow the ISDA protocol for terminating (Chatham can help here) and deliver a termination payment as a result of the ISDA calculations. These calculations contemplate the mark-to-market value of the product, but also incorporate the market value as well as other costs that you incurred as a result of the Lehman bankruptcy. A downside to this approach is that it is uncertain how long you may have to wait for the ultimate negotiation, which could take the form of informal negotiation, mediation or litigation.

Best case outcome. The best case scenario under this approach requires time and a court ruling upholding the original signed contract and ISDA methodology. This approach could result in the best possible outcome as the ISDA termination value is likely to be at a discount to the mark-to-market value (due to the changes in the market and credit environment).

Worst case outcome. A worst case scenario following the ISDA would be if Lehman disagrees with the termination amount and perhaps even the right to terminate, and pursues a full mark-to-market value in court, resulting in a court judgment for the full mark-to-market value. Although you would have incurred legal fees and other expenses in following the ISDA process, the worst case outcome under this scenario isn't too far from the other scenarios.

Lehman has communicated an aggressive strategy. In response, let us help you (in conjunction with your attorney team) gather the appropriate market information to make an informed decision about how to proceed in fairly terminating your derivative, or in defending your claim.

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Lehman Files Motion for Alternative Dispute Resolution Procedure

Lehman's legal team filed a motion this week asking the bankruptcy court to approve a mediation process aimed at speeding resolution of outstanding derivative contracts. This alternative dispute resolution (ADR) procedure would apply to both contracts that have not been terminated and contracts that have been terminated by one party but not resolved through delivery of a signed termination Confirmation. Chatham knows of very few end users (those who are not banks) who have received signed termination confirmations so this motion will have wide impact if approved.

Lehman seems to be targeting contracts that are currently "in the money" to Lehman in order to monetize these contracts and optimize "Recovery Potential" for the creditors. Left to individual disputes, the resolution of the positions would require time and money in litigation. These derivative contracts are complicated and in the motion, Lehman indicates that agreeing on valuations is expected to be difficult and likely to be completed only after the bankruptcy trial and appeal process.

Lehman's proposed Derivative ADR Procedures ignore the ISDA Master and Schedule Agreement (Agreement) in two important ways. First, Lehman may be given the right to terminate the contract. Second, and more importantly, Lehman is essentially proposing that they become the Calculation Agent. They will deliver the settlement amount that you accept or have to dispute, and any amount that you then submit is essentially a point in a negotiation.

A paraphrase of the ADR is as follows:

1. *Lehman serves the non-defaulting party a Derivatives ADR Notice demanding settlement. This settlement, or opening offer, will have been determined in conjunction with Lehman's creditor committee.*
2. *The non-defaulting party has 20 days to respond to the notice with a Response, either accepting or declining Lehman's offer (the latter requires an explanation). Failure to respond by the non-defaulting party could result in Lehman seeking the full amount that it demands or could send the process directly to mediation.*
3. *Lehman then has 15 days to respond with a Reply to Response. In this Reply, Lehman, after discussing with the creditor committee, can modify the proposal, provide a counteroffer, or restate its original demand. Denying the non-defaulting party's Response would send the process directly to mediation.*
4. *At any point after delivery of the initial Derivatives ADR Notice, either party may request a 1-hour conference call that must occur within 5 days of the request. Both parties' counsels and advisors may participate in this call, and the purpose of the call would likely be to discuss the process and probable outcomes of the mediation.*
5. *Mediation would occur in New York City, and all parties would appear in person. The motion states: "Each party must have a business principal in attendance*

having settlement authority."

- 6. If approved by the court, this motion would require that Lehman's counterparties answer the notice, engage in settlement discussions and comply with the directions of the mediator and court.*

Mediation could have some positive outcomes, including keeping the resolution out of court (confidentiality), minimizing time and expense relative to litigation, and potentially providing more flexibility than a court resolution. Mediation could also come with a sizeable hard dollar cost, if the Market Quotation or Loss methodology in the Agreement would have yielded a better settlement value to the non-defaulting party. The Agreement did not contemplate that Early Termination Events become negotiated settlements. Clearly, Lehman Brothers Derivative Products did not follow this procedure when acting as the Calculation Agent in transactions that it had the right to terminate.

In working with a number of non-defaulting counterparties, Chatham has seen informal negotiation emerge as a popular first step in the strategy to resolve outstanding derivatives with Lehman. This proposal by Lehman is currently just a motion, but if approved at the hearing scheduled for August 5, 2009 would formalize that process.

Now more than ever we advocate bringing an experienced financial advisor on to your team who can put Lehman's opening offer in context and help you respond to their notices, if ordered by the court. The Agreement allows Lehman, as defaulting party to provide a replacement transaction or equivalent and that the non-defaulting party, in many cases, be compensated for loss of bargain, cost of funding, and cost of replacement.

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Lehman's Derivatives Wind-down Strategy

Lehman has terminated 99.5% of derivatives contracts.

Lehman Brother's bankruptcy estate is making significant progress on eliminating its outstanding derivatives positions. Alvarez & Marsal (A&M), the Lehman restructuring advisor, met with creditors on July 8, 2009 to provide an update on the restructuring progress. A&M reports that nearly 1.2 million derivatives trades existed at the time of bankruptcy but only 5,858 remain. A&M also reports an "active disposition" strategy combined with an "assertive legal strategy."

The remaining positions are proving difficult for Lehman to assign, although it had the right to do so since December 2008. A&M states that "much of the remaining portfolio is less attractive to potential assignees--long dated, weak or obscure credits, and 'no collateral' contracts." Lehman continues to request rights and waivers from the bankruptcy court to wind-down the small number of remaining nuisances.

How do you terminate YOUR remaining position?

The irony of Lehman's stated aggressive termination approach is that Lehman has rejected recent termination notices from our clients. Lehman appears intent upon dictating the final value of the trade or denying that a termination occurred.

Conversely, those with Lehman trades may be able to attest to the "assertive" nature of the Lehman unwind strategy. Lehman responded this week to a number of early terminations from our clients with requests for additional documentation, requests for spreadsheets with complete calculations, and requests for counterparty dealer names used in the calculation process, even if the calculation was done under the Loss payment measure in accordance with the ISDA Master Agreement.

It is interesting to see how different Lehman's approach was when the shoe was on the other foot. Following the September 15, 2008 bankruptcy filing by Lehman Brothers Holdings, Lehman's AAA entity, Lehman Brothers Derivative Products, (LBDP) was required to unwind all derivatives positions and was the Calculation Agent. Several of our clients had derivative transactions in place with LBDP and received a Calculation Statement with the termination amount and two sentences describing how market quotes weren't available:

"Pursuant to the Agreement, LBDP polled the Dealer Group for Market Quotations for the group of Terminated Transactions listed on Schedule I attached hereto, but was unable to obtain any quotations from such group. In accordance with industry standards, LBDP reverted to Loss methodology to determine the above Termination Amount."

Lehman clearly is not willing to accept today the same protocol that they chose to follow themselves.

Chatham is well versed in the ISDA protocol for early termination. We have specific Market Quotation and Loss examples from market maker banks. Chatham is also aggregating best practices among individuals facing Lehman.

In previous newsletters (please let us know if you have not received them and would like a copy), we discussed your rights as the Calculation Agent, commercially reasonable methods of computing Loss, Lehman's actions of denying Early Termination Notices, and the recent Bar Order Date. **As a reminder, you only have 68 days (and counting) to terminate and submit a claim with Lehman before the window closes.**

If you are considering terminating your Lehman derivative, Chatham Financial can work with your team and your legal counsel to help navigate the process as cost effectively as possible, ensuring calculations are commercially reasonable and adequately documented to mitigate potential dispute or disallowance of a claim. Chatham Financial has worked with its clients and their legal teams to terminate over 100 Lehman-related derivatives with a total notional of over \$7 billion. We have followed Market Quotation, Loss and Close-out protocols, terminated assets and liabilities, and have experience with the various Lehman entities. Our clients' first terminations were completed immediately in September and we continue to work with clients still considering termination.

If you terminated your Lehman derivative and the calculation is challenged, we can assist in dispute resolution by providing independent valuations, derivatives forensics, and expert reports.

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BAR DATE ORDER: Lehman's Bankruptcy Court Set Deadline for Filing Claims

On July 2, 2009 while many Americans were preparing for a long Independence Day weekend, Lehman's attorneys and the United States Bankruptcy Court for the Southern District of New York entered a Bar Date Order setting September 22, 2009 as the last day to file a Proof of Claim related to pre-petition claims against Lehman. These claims would include market quotation or loss calculations associated with derivatives contracts.

What does this mean for you if you have a Lehman swap still outstanding? **You may only have 77 days (and counting) to terminate your swap with Lehman before the window closes.** After September 22, 2009, although your derivative may still be active, you will no longer be in the driver's seat when determining whether the swap will be terminated or how much any Early Termination payment amount will be.

In addition to the Proof of Claim Form that will need to be submitted prior to the Bar Date, the Court has approved Lehman's Derivative Questionnaire and has set a "Questionnaire Deadline" of October 22, 2009. Along with the Questionnaire, you will be required to submit additional supporting documentation, which could include the ISDA Master Agreement, any applicable credit support document, and calculation statements demonstrating amounts determined as a result of Market Quotation, Loss or Close-Out Amount. You may be able to submit some or all of this documentation electronically, although the website that will be used is not yet operational (lehman-claims.com).

In previous newsletters (please let us know if you have not received them and would like a copy), we discussed your rights as the Calculation Agent, commercially reasonable methods of computing Loss, and Lehman's actions of denying Early Termination Notices.

Don't try this at home! If you are considering terminating your Lehman derivative, Chatham Financial can work with your team and your legal counsel to help navigate the process as cost effectively as possible, ensuring calculations are commercially reasonable and adequately documented to mitigate potential dispute or disallowance of a claim. At Chatham we believe that terminating a Lehman swap requires a strong team comprised of well-informed business decision-makers, experienced attorneys and a trusted financial advisor. We want to be part of your team and advocate for you through this process as your financial advisor.

Chatham Financial has worked with its clients and their legal teams to terminate over 100 Lehman-related derivatives with a total notional of over \$7 billion. We have followed Market Quotation, Loss and Close-out protocols, terminated assets and liabilities, and have experience with the various Lehman entities. Our clients' first terminations were completed immediately in September and we continue to work with

clients still considering termination.

If you terminated your Lehman derivative and the calculation is challenged, we can assist in dispute resolution by providing independent valuations, derivatives forensics, and expert reports.

Contact us to discuss your Lehman termination:

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TERMINATION DENIED: The Bankruptcy Code vs. ISDA

Through Chatham's involvement in terminating Lehman derivatives, we are aware that Lehman has begun to alert counterparties that it may deny derivatives terminations. Lehman's bankruptcy estate is now asserting that Termination Notices based upon Lehman's bankruptcy are outside the permissible window given the amount of time that has passed since the firm filed for protection on September 15, 2008. Consequently, Lehman is now reserving the right to dispute the validity of any Early Termination Notice.

According to Lehman, the Bankruptcy Code prohibits the enforcement of ipso facto clauses that permit the termination of contracts solely based on the filing of bankruptcy cases (11 USC 365(e)(1)). Lehman further asserts that while the Bankruptcy Code permits a party under certain circumstances to "liquidate, terminate, or accelerate a swap agreement," (11 U.S.C. 560), Lehman interprets that this authorization is available only for terminations effected solely as a result of the insolvency, financial condition or bankruptcy of the debtor (see, e.g. In Re Enron Corp., 306 B.R. 465 (Bkrcty.S.D.N.Y. 2004)).

If you still have derivatives transactions in place with Lehman, it is important, now more than ever, to know your rights under ISDA and to have the proper team of legal and economic professionals on your side.

Lehman has drawn a new battle line -

Lehman will first declare that your Termination Notice is not valid. After winning that battle, then you have to demonstrate your losses according to the ISDA protocol. Lehman is stating its opinion; however, the Honorable James Peck, Lehman's bankruptcy judge, has not made this ruling. Section 6(a) of the ISDA has no stated timeline.

All the downside with none of the upside -

The pathway to termination of your derivatives is arguably now more difficult. However, remaining in the transaction has no benefits as a hedge (unless the termination would trigger a breach of a covenant or similar) as Lehman will not make any payments to you. If you have not been making payments, Lehman is compounding those amounts at LIBOR + 12.5%.

A shot across the bow to heed -

Lehman would strongly prefer to terminate derivatives contracts through the bankruptcy court. However, ISDA gives rights and privileges to the non-defaulting party including the right to recover loss of bargain, cost of funding, cost of a replacement hedge, as well as fees and expenses. It is in your best interest to terminate under the rules of ISDA in order to preserve these rights. While there is no official statute of limitation for Early Terminations, bankruptcy courts have ruled that at

one point in time you do lose your ability to claim an event of default.

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If you are considering terminating your Lehman derivative, Chatham Financial can help navigate the process to ensure the calculation is commercially reasonable so you don't leave money on the table, and that the calculation is adequately documented to mitigate potential dispute.

If you terminated your Lehman derivative and the calculation is challenged, we can assist in dispute resolution by providing independent valuations, derivatives forensics, and expert reports.

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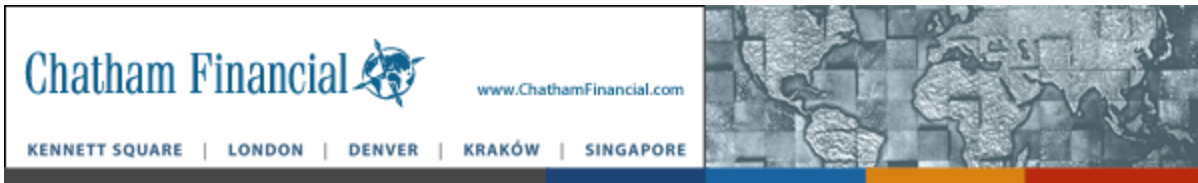
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Are Your Loss Calculations Commercially Reasonable?

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Through our involvement, we are aware that many borrowers have been unable to find replacement counterparties to take assignment of their Lehman positions. In the current credit environment, it is unusual for a borrower to find a market-maker able to face the borrower under comparable terms. The biggest hurdles are downgrade triggers, off-market positions, and unsecured relationships. Unable to assign the derivative, a borrower may opt for early termination of their Lehman position and re-establish a new hedge under current market terms. Following this common set of events, the resulting calculation method for the final payment would revert to Loss (assuming 1992 ISDA Master Agreement).

ISDA defines the characteristics of a Loss Calculation and establishes the guideline that the calculation must be reasonably determined in good faith. The components of Loss to be considered in the calculation are:

Cost of funding -

Many clients with Lehman derivatives were not required to post an independent amount or collateral. However, current replacement counterparties are often requiring independent amounts and imposing margin calls. Allocating or raising funds to post as an independent amount may result in a significant cost of funds. Additionally, the daily margin calls can be unpredictable and may add to the cash collateral requirements.

Loss or cost of a replacement hedge -

Credit charges paid to a replacement counterparty represent costs incurred as result of terminating, liquidating, obtaining or reestablishing any hedge or related trading position. As the cost of credit has generally gone up since the time Lehman filed for bankruptcy, this component tends to be higher now than when the original hedge was executed.

Loss of bargain -

Many terms that were agreed to by Lehman over the past several years are no longer available in the market such as downgrade triggers and unsecured relationships. In the current market, replacement counterparties drive the terms of the new relationship, resulting in unfavorable yet unavoidable concessions in order to replace the former derivative.

Loss does not include a party's legal fees and out-of-pocket expenses. However, you can be reimbursed for these types of fees and expenses under Section 11. "Expenses" of the 1992 ISDA.

If you are considering terminating your Lehman derivative, Chatham Financial can help navigate the process to ensure the calculation is commercially reasonable so you don't leave money on the table, and that the calculation is adequately documented to mitigate potential dispute.

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Rights of the Non-Defaulting Counterparty

Chatham Financial has worked with its clients--public and private, large and small--and their legal teams to terminate over 100 Lehman-related derivatives with a total notional of over \$7 billion. We have followed Market Quotation, Loss and Close-out protocols, terminated assets and liabilities, and have experience with the various Lehman entities. Our clients' first terminations were completed immediately in September and we continue to work with clients still considering termination.

Through our involvement we are aware that the Lehman bankruptcy estate has started to reach out to counterparties with terminated derivatives. Lehman's bankruptcy estate, its financial advisor Alvarez & Marsal, and its outside legal counsel Weil Gotshal are skilled and experienced in maximizing settlement amounts. In many cases Lehman is contesting the early termination payment amount; furthermore, Lehman is assessing a charge of LIBOR + 12.50% on all unpaid amounts.

Chatham Financial understands that to receive demands for payment and the possibility of bearing interest expenses at high rates may be intimidating. It is important to know your rights under ISDA:

You are the calculation agent

(except for transactions facing Lehman's AAA terminating facility)

Recently a Lehman representative contacted our client via email stating that Lehman calculated a termination amount that was a greater liability than the Market Quotation amount submitted. The email provided wiring instructions and stated that unpaid amounts would be compounded at LIBOR + 12.50%. Upon a subsequent phone call with Lehman, Chatham Financial explained that ISDA protocol was followed and our client's calculated amount could not be disputed. Lehman conceded the point and dropped the claim.

You have the right but not the obligation to exercise Early Termination

From the Lehman Brothers bankruptcy Docket No. 2257: "In connection with any termination agreement, the Debtors are authorized, but not required, to provide a release to the Counterparty to the extent that the Debtors determine such a release is appropriate." It is important to consider your covenants and obligations before removing derivatives.

You can be reimbursed for fees and legal expenses

From the 1992 ISDA: "Section 11. Expenses. A Defaulting Party will, on demand, indemnify and hold harmless the other party for and against all reasonable out-of-pocket expenses, including legal fees and Stamp Tax, incurred by such other party by reason of the enforcement and protection of its rights under this Agreement or any Credit Support Document to which the Defaulting Party is a party or by reason of the early termination of any transaction, including, but not limited to, costs of collection."

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