

Lehman Brothers Situation - general comments re tax situations

This paper, commenting on general tax issues, was prepared for the LMA by Clifford Chance. Please note the paper only provides general guidance and no reliance should be placed on it in relation to specific situations.

1. UK borrowers under loans where the lenders include a non-UK Lehman entity which is acting through a UK branch (e.g. Lehman Commercial Paper Inc, UK Branch).

It is likely the Lehman entity will have ceased to carry on a trade for UK tax purposes and, if this is the case, the usual withholding tax exemption a UK borrower would have relied upon may not be available. In such circumstances, the borrower will be required to withhold tax from its interest payments going forward; whether it is required to gross-up will depend upon the terms of the facility agreement.

2. UK borrowers under loans where the lenders include a US Lehman entity which is not acting through a UK branch

The Lehman entity may have ceased, as a technical matter, to qualify for the benefit of the UK/US double tax treaty. If so, any treaty clearances the Lehman entity received would be invalid, and UK borrowers which had previously relied upon those clearances to pay interest without withholding tax would, going forward, have to withhold tax. Again, whether such borrowers are required to gross-up will depend upon the precise terms of the facility documents.

Clifford Chance has raised both the above issues with HM Revenue & Customs, and understands that HMRC is currently formulating a policy having regard to the technical provisions in question and the obvious desire not to unnecessarily put borrowers in a difficult position.

3. Non-UK participants under LMA-style English law subparticipations where a Lehman UK banking entity is a Grantor

As they are in administration, such Lehman entities' regulatory status is likely to have been suspended. If so, the usual withholding tax exemption for payments of interest by banks and other regulated entities will cease to apply, and payments of interest under subparticipations to non-UK participants will be subject to UK withholding tax at 20%. Participants are of course likely to receive only partial payment of amounts owing by Lehman grantors - there is likely to be a degree of uncertainty (and room for argument) regarding the extent to which payments from such grantors constitute interest and are subject to this withholding. In some cases relief may be available under a double taxation treaty. In other cases, where possible, participants may wish to transfer their participations to affiliates who are in the UK or do qualify for treaty relief.

4. Non-UK lenders to Lehman

For the same reason noted in the previous paragraph, interest payments by Lehman to non-UK lenders may be subject to UK withholding tax at 20%, subject to treaty relief. Again, assigning/transferring to UK or treaty-qualified entities may be advisable to minimise withholding exposure going forwards.

The position noted in 1 to 4 above will need to be revisited when circumstances change, e.g. where Lehman assets/companies are bought by third parties or when/if Lehman entities cease to be in administration/Chapter 11 and enter bankruptcy/liquidation.