
Hughes Hubbard & Reed

Lehman Team Prevails in Appeal of 'Repo' Claims

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One Battery Park Plaza • New York, New York 10004-1482 • +1 (212) 837-6000

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Hughes Hubbard won the latest round in a legal battle over whether nearly \$200 million in repurchase transaction claims qualify for customer protection under the Securities Investor Protection Act (SIPA) liquidation of Lehman Brothers Inc. (LBI).

On Feb. 26, 2014, U.S. District Judge Denise Cote upheld a bankruptcy court decision that the claims don't qualify because claimants, a group of banks, didn't entrust property to the broker-dealer. "The banks do not qualify as 'customers' under SIPA," Judge Cote said. "The banks have not met their burden of demonstrating the existence of a fiduciary relationship between the banks and LBI."

In U.S. Bankruptcy Judge James Peck's June 2013 ruling, he agreed with the position Hughes Hubbard took on behalf of James W. Giddens, trustee for Lehman's SIPA liquidation, that the repos were proprietary transactions giving rise to breach of contract claims rather than customer claims. Repo claimants Hudson City Savings Bank, the Federal Deposit Insurance Corporation and CarVal Investors UK appealed the ruling in August. Their appeal focused on the requirements for "customer" status under SIPA.

Relying on Second Circuit precedent (including previous Hughes Hubbard SIPA cases) requiring a claimant to entrust property in order to qualify as a broker's "customer," Judge Cote held that the repo claimants did not "entrust" securities with LBI and were not SIPA customers. The repo transactions were not one-sided transfers—they involved the mutual exchange of property between counterparties in a sophisticated financial transaction. Noting that LBI did not act on behalf of the repo claimants, Judge Cote held that the parties did not have a fiduciary relationship and instead "the agreements had the characteristics of an ordinary debtor-creditor relationship."

Although the parties disputed whether repo transactions more closely resemble a purchase and sale of securities or a loan secured by securities, Judge Cote found "no matter how the agreements are characterized, the banks are not entitled to 'customer' status under SIPA."

Hughes Hubbard's victory was reported by Reuters. The repo litigation is being handled for Giddens by Michael Salzman, James B. Kobak Jr., Christopher Kiplok and Seth Schulman-Marcus.

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James W. Giddens



Michael E. Salzman



James B. Kobak, Jr.



Christopher K. Kiplok

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