Neutral Citation Number: [2017] EWHC 522 (Comm)

Case No: CL-2014-000919

IN THE HIGH COURT OF JUSTICE
QUEEN'S BENCH DIVISION
COMMERCIAL COURT

Royal Courts of Justice
Strand, London, WC2A 2LL

Date: 20/03/2017

Before :

MR JUSTICE KNOWLES CBE

- -

Between :

LBI EHF (in winding up)	**Claimant**
- and -	
(1) RAIFFEISEN ZENTRALBANK ÖSTERREICH AG	**Defendants**
(2) RAIFFEISEN BANK INTERNATIONAL AG	

- -
- -

Benjamin Pilling QC and Edward Jones (instructed by **Stewarts Law LLP**) for the **Claimant**
Guy Philipps QC and Richard Power (instructed by **Stephenson Harwood LLP**) for the **Defendants**

Hearing dates: 8, 12, 13, 14, 15 and 19 December 2016

- -

Approved Judgment

I direct that pursuant to CPR PD 39A para 6.1 no official shorthand note shall be taken of this Judgment and that copies of this version as handed down may be treated as authentic.

.....

MR JUSTICE KNOWLES

Mr Justice Knowles :

Introduction

1. The Claimant ("LBI") was the bank formerly named Landsbanki Islands hf. It entered into a number of trades with the Defendants ("RZB"). On 7 October 2008 LBI failed. At that date there were eleven open positions between LBI and RZB relating to "repo" trades and three open positions relating to securities lending trades.

2. These trades were on the terms of two master agreements. The repo trades were on the terms of the Global Master Repurchase Agreement 2000 edition (the "GMRA"). The securities lending trades were on the terms of the Global Master Securities Lending Agreement 2000 edition (the "GMSLA").

3. The dispute between the parties concerns valuation. There is a first question, which is whether default notices were effectively served by RZB on 8 October 2008.

Effective service of default notices

4. RZB contends that it sent default notices by fax at 14:11 and 17:46 on 8 October 2008. LBI has not traced any receipt of default notices, and challenges RZB's contention.

5. There is no dispute that service by fax was permissible under the GMRA and the GMSLA. LBI criticised the choice of fax over other permissible means, but the short point is that the parties had agreed that fax might be used.

6. In both the GMRA and the GMSLA the fax number was specified. The GMRA provided by paragraph 14(a)(ii) and (b)(iii), so far as material:

> "(a) Any notice or other communication to be given under this Agreement … (ii) may be given in any manner described in sub-paragraphs (b) … below;
>
> …
>
> (b) … any such notice or other communication shall be effective … (iii) … if sent by facsimile transmission, at the time when the transmission is received by a responsible employee of the recipient in legible form (it being agreed that the burden of proving receipt will be on the sender and will not be met by a transmission report generated by the sender's facsimile machine) …"

The GMSLA provided by paragraph 21.1:

> "Any notice or other communication in respect of this Agreement may be given in any manner set forth below to the address or number … set out in paragraph 4 of the Schedule and will be deemed effective as indicated: … (iii) if sent by facsimile transmission, on the date that transmission is received by a responsible employee of the recipient in legible form (it being agreed that the burden of

> proving receipt will be on the sender and will not be met by a transmission report generated by the sender's facsimile machine) …"

7. It was the evidence of Mr Ronald Wiesinger of RZB that on 7 October 2008 LBI had, after receiving a margin call, stated it was "unable to make any payments today". This together with news of the appointment of a Resolution Committee to LBI caused RZB, on Mr Wiesinger's evidence, to decide to terminate the trades on grounds of LBI's default. RZB's legal department drafted default notices and, on his evidence, his colleague Ms Jordan-Sima sent those notices by fax. I accept this evidence.

8. The available documentation includes transmission receipts marked "OK". The receipt contains the number for LBI but commencing "0207" rather than "0044207". I am prepared to accept that this does not show the way in which the number was dialled, but shows the answerback of the machine reached. Neither party called expert evidence on the point, so I am left to assess the matter with limited tools. I am influenced in my assessment by the greater likelihood of Ms Jordan-Sima dialling correctly rather than incorrectly. This was not, on Mr Wiesenger's evidence, the first occasion on which the number had been dialled; it had been used for previous fax confirmations of trades.

9. Were the faxes received in legible form? On a balance of probabilities my conclusion is that they were. It is not in issue that the fax machine at LBI was still being used. Indeed it is LBI's case that it was being checked from 7 October 2008 onwards. There is greater likelihood of the faxes being received in legible form than in illegible form.

10. Were the faxes received by a "responsible employee" of LBI? LBI contended that "responsible employee" means "an employee with responsibilities relevant to the default, i.e. someone who will recognise a … notice for what it is, and what steps will be taken as a result". In my judgment that reads far too much into the phrase. It would allow the quality of the recipient's systems and procedures to affect the position considerably. I cannot accept that the parties would intend the uncertainty involved.

11. Less ambitiously, reference was made to a remark in Henderson on Derivatives (Second Edition, 2010), discussing the 1992 ISDA Master Agreement. Mr Henderson writes: "who is a responsible official (presumably not the employee in the fax room)". It may be that Mr Henderson's remark drew particularly upon the word "official" (which is not the word in the present case). And Mr Henderson is right to point out that the use of fax to serve notices invites issues. But for my part I respectfully question why the employee in the fax room is not a "responsible employee". The employee in the fax room has been given responsibility by his employer as the first point of receipt of this form of communication to his employer. Other forms of giving notice under the GMRA and GMSLA focussed on the moment of receipt or delivery rather than reading. This is why I cannot accept the submission of LBI that the words "responsible employee" means "someone who will appreciate what the … notice is and what it signifies".

12. Mr Hjortur Jonsson of LBI gave evidence that incoming faxes were being regularly collected from the machine. I am prepared to accept that it is more likely than not that the faxes were collected, and by an employee with responsibility for collecting them.

13. I accept that LBI has looked hard, not least in complying with its disclosure obligations in this litigation, to see whether it can find default notices from RZB for these trades. I do not accept that the fact that LBI has not found any notices is of much weight in an assessment of whether notices were received, when considered against the evidence I have identified above.

14. I was not persuaded that LBI had a reliable system for recording or storing faxes, so as to allow me to place much weight on the fact that the faxes were not to be found in a particular place. Mr Jonsson accepted that the fact that the legal department did not have a copy of a notice did not mean that it did not exist. It is a sign of his uncertainty on the matter that he contacted RZB to ask if they had sent default notices.

Valuation

15. No Default Valuation Notice (as defined by the GMRA) was served by RZB by the Default Valuation Time (of 15 October 2008). In those circumstances the GMRA provided, by paragraph 10(e)(ii) that:

> "… the Default Market Value of the relevant Equivalent Securities … shall be an amount equal to their Net Value at the Default Valuation Time; provided that, if at the Default Valuation Time the non-Defaulting Party reasonably determines that, owing to circumstances affecting the market in the Equivalent Securities … in question, it is not possible for the non-Defaulting Party to determine a Net Value of such Equivalent Securities … which is commercially reasonable, the Default Market Value of such Equivalent Securities … shall be an amount equal to their Net Value as determined by the non-Defaulting party as soon as reasonably practicable after the Default Valuation Time".

"Equivalent Securities" was given this definition:

> "… with respect to a Transaction, Securities equivalent to ["equivalent to" was also defined] Purchased Securities under that Transaction. If and to the extent that the Purchased Securities have been redeemed, the expression shall mean a sum of money equivalent to the proceeds of the redemption"

16. "Net Value" was defined by paragraph 10(d)(iv) of the GMRA as meaning:

> "… at any time, in relation to any Deliverable Securities or Receivable Securities, the amount which, in the reasonable opinion of the non-Defaulting Party, represents their fair market value, having regard to such pricing sources and methods (which may include, without limitation, available prices for Securities with similar maturities, terms and credit characteristics as the relevant Equivalent Securities or Equivalent Margin Securities) as the non-Defaulting party considers appropriate, less, in the case of Receivable Securities, or plus, in the case of Deliverable Securities, all Transaction Costs which would be incurred in connection with the purchase or sale of such Securities."

17. In the present case the parties had not agreed a "generally recognised source" of prices for Securities as the definition of "Market Value" in the GMRA contemplated

they might. Nor did RZB make the determination described in the proviso contained in paragraph 10(e)(ii) of the GMRA.

18. LBI contends that the meaning to be given to the words "fair market value" should be informed by the way in which those words have been used in a variety of other legal and financial contexts both domestically and internationally. In this connection reference was made to definitions in the International Valuation Standards published by the International Valuation Standards Council, in the International Financial Reporting Standards published by the International Accounting Standards Board, in the American Society of Appraisers' Business Valuation Standards, and in the United States Treasury Regulations. I do not consider it is a reliable approach to take definitions offered by those sources when the words appear without those definitions in the GMRA.

19. LBI argues that the definitions in the sources mentioned, and other illustrations, "show that there is a consistently recognised concept associated with fair market value involving a willing buyer, willing seller, knowledge of the asset in question and a lack of compulsion", and a determination that should be carried out regardless of counterparty impairment.

20. I do not consider the words are to be limited in this way. In the context of the GMRA, when called into action the words are words that will have to work in a whole range of factual scenarios. LBI submitted, drawing on definitions found elsewhere, that a critical point in the meaning for which it contended was the lack of compulsion. This, it was submitted, excluded from the "fair market value" prices achieved in a distressed market. I find the submission that lack of compulsion is within the meaning of the words difficult to reconcile with the fact that under paragraph 10(e)(i) of GMRA the non-Defaulting Party may actually sell the securities, in what may be a distressed market, and determine the Default Market Value on the basis of the prices obtained, provided always that it acts in good faith.

21. The matter is more usefully approached by addressing first the words "reasonable opinion of the non-Defaulting Party". Here the parties both drew upon the judgments of Rix LJ in Socimer Bank Ltd v Standard Bank Ltd [2008] EWCA Civ 116; Bus LR 1304 and of Blair J in Lehman Brothers International (Europe) v Exxonmobil Financial Services BV [2016] EWHC 2699 (Comm). Thus LBI accepted that it followed from the judgment of Rix LJ that the task for the Court was to put itself into the shoes of the decision maker (here RZB, the non-Defaulting party) and ask what decision RZB would have reached, acting rationally and not arbitrarily or perversely.

22. In Exxonmobil, a case also concerned with the 2000 edition of GMRA, Blair J said:

> 279. In the present case, there was no decision, and the court is concerned with the "counterfactual". The process was explained in *WestLB AG v Nomura Bank International plc* [2012] EWCA Civ 495, which was also a financial case in which the decision maker ought to have, but did not, conduct a valuation exercise. At [58], Rix LJ said:
>
> > "… in the present case the decision maker is not the court, with or without expert or other evidence to assist it: the decision maker, with an absolute discretion, is Nomura (whether Nomura International or Nomura Bank). In

> circumstances where it ought to have, but has not conducted a valid valuation exercise, the question, as the judge rightly put to himself, is how would Nomura have decided the matter, on or at least as at 30 September 2008, had it made a valid determination, honestly and rationally: *Socimer* at [65]-[66]."
>
> 280. Accordingly, I accept EMFS's submission that the securities should be ascribed a fair market value in accordance with the opinion which EMFS (acting rationally) would have formed had it conducted the valuation exercise required by paragraph 10(e)(ii) of the GMRA. This is largely a question of fact.
>
> 281. … The extent of a contractual discretion depends on its terms, and the test of rationality applies within those terms (see e.g. *Braganza v BP Shipping Ltd* [2015] 1 WLR 1661 at [32], Baroness Hale, and at [54], Lord Hodge).
>
> …
>
> 284. There was some debate between the parties in their post-hearing submissions as to how the test is to be applied, but in view of my factual conclusions below it is not necessary to go into the detail. It is sufficient to say that the test is one of rationality, applied in a commercial manner in accordance with the authority set out above.
>
> …
>
> 331.… Under the contract, the exercise in determining the "fair market value" is a broad one. The non-Defaulting Party is entitled to have regard to such pricing sources and methods, which may include without limitation available prices for securities with similar maturities, terms and credit characteristics, as it considers appropriate.
>
> …
>
> 365. It is correct, of course, that the test of rationality gives considerable leeway to the non-Defaulting Party. But it is nevertheless an important boundary, and if crossed, the other creditors wrongly lose out."

23. There may be a range of possibilities that do not cross the important boundary. A useful approach in my view is for the Court to examine carefully what the non-Defaulting party contends it would have taken as "fair market value" and why.

24. RZB's final position in this respect was set out in written closing submissions. These figures, and the information used, form Appendix A to this judgment.

25. I bear fully in mind that the figures contended for in RZB's final position were provided as a statement of its position, rather than as evidence of opinion from an expert witness or evidence from a witness of fact called by RZB. Notwithstanding, in the circumstances addressed below I am prepared to accept that the figures contended for meet the requirement for a rational, honest determination of fair market value as at 15 October 2008.

26. Expert evidence was provided from Dr David Ellis and Mr David McClean. Generally I found the evidence of the expert witnesses called did not assist greatly. I do not mean any disrespect to the experts in saying this. The task in hand is not one of independent expert valuation. Dr Ellis had no direct experience of the situation facing RZB. And I found Mr McClean's evidence largely to be evidence of what he did or would do, rather than what lay within and what lay outside the range of rational views.

27. Indeed Mr McClean confirmed in his oral evidence that the opinion he was asked to give was "on what I thought the right method to use and, consequently, what the right value to reach was". In a stage at the trial when the two experts gave evidence concurrently, Mr McClean gave evidence that other market counterparties used his method and I am prepared to accept that. That method was, in effect, to mark to a model rather than to actual market prices. This still does not mean that the method was the only one available to RZB within the words "fair market value".

28. In the result the experts provided views of figures they would reach, looking back, but what I am tasked to decide is the view that RZB would have reached. Of course the views of the experts lie in the background as some help in checking whether figures are not rational.

29. I accept the evidence of Mr Wiesenger of RZB that as soon as the Default Notice had been dispatched to LBI, RZB asked for bids from 10 institutional counterparties. It also enlisted its own traders and sales people to help sell the positions. The response RZB received supported a decision by RZB to place orders to sell, setting a price or limit.

30. Algorithm-based prices were shown on Bloomberg and, in particular, on a Bloomberg screen known as BGN. RZB used these for a range of internal purposes. However at the time and in the circumstances prevailing RZB did not consider these to represent a practical and commercial realisable value. This view was based on experience from the Lehman default in September, and it was a rational view. Mr McLean, the expert called by LBI, favoured the use of Bloomberg or BGN prices but was prepared to recognise that it was "questionable" or "difficult" to execute at these prices in the market circumstances prevailing. He also ventured, in the course of the discussion on this subject, that it would be rational for RZB "to put a haircut on the securities". That is consistent with the figures put forward by RZB.

31. The only activity experienced by RZB on 15 October 2008 itself was a bid shown by Citi at 45 for ICICI (USD) bonds and a request by Citi that RZB place an order with it at 80 for RAK Bank bonds. This leaves little other available material, and all this in times that were financially exceptional and serious.

32. The figures RZB puts forward do not apply prices from days other than 15 October but they do include adjustments from price information available on other days. I have looked at each of those adjustments and am prepared to accept them as meeting the requirements of rationality and good faith.

33. LBI submits that RZB "might have looked for all sorts of other bits of information that would be relevant to fair market value". I am unable to treat as irrational an assessment of fair market value based on the information RZB did have in the present

case and without more. I do not rule out that the position may be different in the circumstances of other cases. There is no doubt that the information available in the present case was imperfect, and it is to be noted that it includes the Bloomberg or BGN prices despite what I have said above. However the circumstances at that time were imperfect. Any assessment of fair market value would have been imperfect but the non-Defaulting party was nonetheless entitled to make one.

Other issues and alternative cases

34. In light of the conclusions I have reached a number of other issues do not arise. It is also unnecessary to deal with the alternative cases raised by RZB.

Conclusion

35. I do not understand it to be in issue that the conclusions I have reached have the result that LBI's claim fails. I am grateful to the legal teams for the assistance I have received, and for argument of great ability.

Appendix

The figures for which RZB contended, and the information used

Wells Fargo / Wachovia

On 15 October 2008, RZB had the following information available to it:

On 8 October 2008 Goldman Sachs showed an indicative level of 70.

On the same day Citi was showing an indicative level of 63 but could not get a firm bid.

On 14 October 2008 the limit of the order with Goldman Sachs was increased to 85 but it was not possible to find any buyers.

The Bloomberg price on 15 October 2008 was 82.902.

RZB contended it would have determined that the fair market value of the bond on 15 October 2008 was no higher than **75.**

Morgan Stanley

On 15 October 2008, RZB had the following information available to it:

> On 8 October 2008 JP Morgan showed an indicative level of 56 but could not get a firm bid.
>
> Goldman Sachs could not get a firm bid and recommended that RZB place an order with them at 55.
>
> Citi showed an indicative level of 54 but could not get a firm bid.
>
> On 9 October 2008 the position was sold at 49 via JP Morgan.
>
> The Bloomberg price on that day was 53.375.
>
> On 15 October 2008 the Bloomberg price was 72.67.
>
> The BGN price had increased by 36% between the date of sale and the valuation date.

RZB contended it would have determined that the fair market value of the bond on 15 October 2008 was no higher than **67** (a 36% increase on the sale price).

RZB

On 15 October 2008, RZB had the following information available to it:

> On 8 October 2008 Goldman Sachs told RZB that it could not find any bids for the bonds.
>
> On the same date Citi showed an indicative level of 77 but could not find a firm bid.
>
> After some internal discussions, the trader of RZB bought the bond on 8 October 2008 for 81.
>
> The Bloomberg price on that day was 83.838.
>
> On 15 October 2008 the last Bloomberg price showing was of 9 October 2008, being 83.32.

RZB contended it would have determined that the fair market value of the bond on 15 October 2008 was **81**.

Countrywide

On 15 October 2008, RZB had the following information available to it:

On 8 October 2008 JP Morgan showed an indicative level of 87 but could not get a firm bid.

Goldman Sachs said they could not get an order for the bonds but recommended that RZB place an order for 88. They could not find any buyer at that level.

Citi was showing an indicative bid of 86 but could not get a firm bid.

On 14 October 2008 JP Morgan showed a firm bid at 85 for the full size and RZB concluded the sale.

The Bloomberg price on 14 October 2008 was 92.021.

The Bloomberg price on 15 October 2008 was 92.038.

RZB contended it would have determined that the fair market value of the bond on 15 October 2008 was **85**.

Transneft USD (Transneft 1)

On 15 October 2008, RZB had the following information available to it:

On 8 October 2008 it had been unable to sell the bond at 83 (via Citi)

No firm bid could be received from JP Morgan for 79 on 8 October 2008.

Goldman Sachs could not find any bids at all on 8 October 2008.

On 14 October 2008 RZB had sold a USD 8.3 million part of the holding at 74.

The Bloomberg price on 14 October 2008 was 79.321.

The Bloomberg price on 15 October 2008 was 78.233.

RZB contended it would have determined that the fair market value of the bond on 15 October 2008 was **74**.

Transneft EUR (Transneft 2)

On 15 October 2008, RZB had the following information available to it:

On 8 October 2008 Citi showed an indicative level of 75 but could not get a firm bid.

Goldman Sachs could not find any bids.

On the same date JP Morgan showed an indicative level of 76 and RZB sold at that price.

The Bloomberg price on that date was 82.722.

On 15 October 2008, the Bloomberg price had fallen by approximately 5% to 78.606.

RZB contended it would have determined that the fair market value of the bond on 15 October 2008 was **73**.

Gazprom

On 15 October 2008, RZB had the following information available to it:

On 8 October 2008 Citi showed an indicative bid of 80 but could not get a firm bid.

JP Morgan showed an indicative bid of 74 but could not get a firm bid.

Goldman Sachs could not find any bids for the bond.

On 14 October 2008 the bond was sold via Citi at 70.

The Bloomberg price on 14 October 2008 was 77.500.

The Bloomberg price on 15 October 2008 was 74.500, a fall of nearly 4%.

RZB contended it would have determined that the fair market value of the bond on 15 October 2008 was no higher than **68**.

ICICI EUR

On 15 October 2008, RZB had the following information available to it:

On 8 October 2008 Goldman Sachs told RZB that it could not find any bids for this bond.

Citi showed an indicative level of 88 but could not get a firm bid.

RZB placed an order to sell at 88.

On the same day, Citi showed a bid of 80 and RZB sold at that level.

The Bloomberg price on 8 October 2008 was 99.49.

The Bloomberg price on 15 October 2008 was 99.508.

RZB contended it would have determined that the fair market value of the bond on 15 October 2008 was **80**.

ICICI USD

On 15 October 2008, RZB had the following information available to it:

On 8 October 2008, Citi showed an indicative level of 58 but could not get a firm bid.

RZB placed an order to sell at 68 with Citi on 8 October 2008 but Citi was unable to find a bid.

RZB had placed an order with Barclays to sell at 84 but Barclays was unable to find a bid.

On 9 October 2008 RZB sold a tranche of USD 2 million via Citi at a price of 60.

The Bloomberg closing price on that day was 90.192.

On 13 October 2008 RZB placed an order with Citi to sell USD 5 million at 68 but no bid was received.

On 14 October 2008 Citi showed an indicative bid of 50, which was declined.

Barclays had still not found any bidders at 84.

On 15 October, the best firm bid shown by Citi was 45.

The last Bloomberg price on 15 October 2008 was 93.211 (14 October 2008), an increase of about 3.3%.

RZB contended it would have determined that the fair market value of the bond on 15 October 2008 was no higher than **62**.

RAK Bank

On 15 October 2008, RZB had the following information available to it:

On 8 October 2008, JP Morgan had been unable to obtain a firm bid at 74.

Goldman Sachs could not find any bids for the bond.

On 14 October 2008, Citi explained that it had a chance to sell the bond and requested that RZB place an order with it at 80.

On 15 October 2008 that order was still with Citi but could not be executed.

RZB contended it would have determined that the fair market value of RAK Bank was no higher than **80**.

Qatar Alaq Sukuk

On 15 October 2008, RZB had the following information available to it:

On 8 October 2008, RZB was informed by Goldman Sachs that it would have no tradeable bid in the bond.

On 9 October an order to sell at 87.5 was placed with HSBC.

HSBC's feedback was that it would be difficult to get any counter-bids. It was unable to find a bidder.

On 13 October 2008 Citi was asked for a level at which it would be reasonable to sell the bond.

On 14 October 2008 Citi stated that it thought a sell order with a limit of 65 to 70 would be a realistic level. However, no firm bid could be received.

On 15 October the sell order was still with Citi at a limit of 80 but no tradeable bid could be received.

RZB contended it would have valued the Sukuk at no higher than **67.5**.

Overall value

As set out above, and as summarised in the table below, RZB contended that had it carried out the valuation required by paragraph 10(e)(ii) of the GMRA, it would have determined that the Net Value of the GMRA Securities was no higher than **€74,665,604**.

Issuer	*ISIN*	*Nominal*	*Curr.*	*Price*	*Value (currency)*	*Value (EUR) at 15.10.08 (EUR1 = USD1.35)*
Wachovia	XS0286634711	2,000,000	EUR	75	1,500,000	1,500,000
Morgan Stanley	XS0298900217	2,000,000	EUR	67	1,340,000	1,340,000
RZB	XS0326967832	10,000,000	EUR	81	8,100,000	8,100,000
Countrywide	XS0236024310	14,753,000	EUR	85	12,540,050	12,540,050
Transneft 1	XS0306899765	13,000,000	USD	74	9,620,000	7,125,925
Transneft 2	XS0306900795	11,000,000	EUR	73	8,030,000	8,030,000
Gazprom	XS0294275853	10,000,000	USD	68	6,800,000	5,037,037
ICICI	XS0293980461	5,000,000	EUR	80	4,000,000	4,000,000
ICICI	XS0305773292	12,000,000	USD	62	7,440,000	5,511,111
RAK Bank	XS0231692236	2,500,000	USD	80	2,000,000	1,481,481
Qatar Alaq Sukkuk	XS0313358508	40,000,000	USD	67.5	27,000,000	20,000,000
						74,665,604