IN THE HIGH COURT OF JUSTICE
CHANCERY DIVISION
COMPANIES COURT

IN THE MATTER OF

LEHMAN BROTHERS INTERNATIONAL (EUROPE)

(in administration)

AND IN THE MATTER OF THE COMPANIES ACT 2006

REPLY TO THE EXPERT OPINION OF GERO FISCHER

BY

PROFESSOR PETER O. MÜLBERT

Table of contents

I, **Professor Peter Otto Mülbert**, of University of Mainz, Faculty of Law and Economics, 55099 Mainz Germany, **WILL SAY** as follows:

I. INTRODUCTION AND BACKGROUND

1. I have examined the expert opinion of Dr Gero Fischer (the **Fischer Opinion**) as to matters of German law relating to the Waterfall II application. I note that the views expressed in the Fischer Opinion regarding the rules and basic principles of contractual interpretation (paragraphs 29 – 34)[1], the meaning of the second sentence of clause 3(4) of the German Master Agreement (paragraph 72), the need to establish loss for the purposes of section 288(4) of BGB (paragraphs 68 – 70)[2] and, subject to the comments made below, the expression of a claim under section 288(4) or the second sentence of clause 3(4) of the German Master Agreement as a rate or amount (paragraphs 86 – 89) are broadly in agreement with the views I expressed in my opinion as to matters of German law. In this reply, I have dealt with matters where I disagree with the views expressed in the Fischer Opinion or where I wish to highlight differences in opinion. As far as a point raised by the Fischer Opinion is not addressed in this reply, that does not indicate any agreement or disagreement with it.

2. As a preliminary matter, I note that the Fischer Opinion deals with certain matters relating to German insolvency law. In particular, paragraphs 64 and 80 deal with the question of whether a default under section 286 BGB can occur upon or following the commencement of insolvency proceedings and paragraphs 45 – 58 and paragraph 81 deal with the question of how the close-out amount under the German Master Agreement should be calculated following the commencement of insolvency proceedings.

3. On the first point, while I agree that a default is generally required in order to claim default interest under section 288 BGB, I do not consider that the provisions of the German Insolvency Code, or German insolvency law more broadly are relevant to the question of whether such a default has occurred (or is capable of occurring) given that LBIE is not subject to any insolvency proceedings in Germany. Whether a default satisfying the requirements of Section 286 BGB has occurred in any instance is a question of fact and may involve consideration of the consequences of LBIE having entered English insolvency proceedings. Although Dr Fischer states, in paragraph 82, that nothing turns on the fact that the insolvency proceedings in question were, in fact, commenced in England, this is in the context of his analysis in respect of section 104 of the Insolvency Code (referred to in paragraph 4 below); it is not in the context of his analysis in respect of what would satisfy the requirements for a default. In my view, English insolvency law must be relevant here (given that LBIE is subject to insolvency proceedings in England and not in Germany) and I am not competent to deal with matters of English insolvency law without further instruction as to how such law operates or the question of default as a matter of fact in any given instance.

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[1] I note that Dr Fischer concludes, in paragraph 34, that the terms of the German Master Agreement are standard form clauses that must be interpreted in accordance with objective standards. For the reasons given in paragraph 25 of my opinion, I consider that this will depend on the specific facts and whether the clause in question was subject to individual negotiation. It is not clear, though, whether anything would turn on this distinction.

[2] In paragraph 70 of the Fischer Opinion, Dr Fischer states that the abstract calculation of loss referred to in that paragraph is not available to commercial investors such as investment companies and insurance companies. I refer to paragraph 50 of my opinion where I set out my views as to whether the abstract method of calculation is available to other types of investors. Again, though, it is not clear what turns on this distinction.

4. On the second point, it is unclear to me why it is relevant to decide how the close-out amount would be calculated as a matter of German insolvency law given that I am instructed and understand that such principal claims have been agreed with LBIE pursuant to claim determination deeds or settlement agreements. I have therefore not dealt with this question in my reply.

5. For the purpose of this reply, the terms in paragraph 21 of my opinion are to be understood in the same way as defined there.

II. REPLY

Issue 1: Higher payment obligations as a consequence of the assignment

6. In paragraph 13 of the Fischer Opinion, Dr Fischer states that, in his opinion, "*the debtor must not be exposed to the disadvantage of a greater damage of the assignee*". This conclusion, which Dr Fischer seeks to explain at paragraphs 96 – 106 of the Fischer Opinion is apparently based on the case law of the German Federal Court of Justice and section 404 BGB. At paragraph 105 of the Fischer Opinion, Dr Fischer states as follows:

   "*The considerations of the German Federal Court of Justice – which in my view are correct – together with the general principle in German Civil Law that contracts cannot be made that impose obligations on third parties, support the view that a change of creditor cannot entail greater obligations for the debtor, including in the sphere of damages, than there would have been to the original creditor.*"

7. I disagree with this conclusion. Provided that the Damages Interest Claim[3] has been included in the transfer to a third party, it will be calculated by reference to the assignor's losses for the period prior to the transfer and by reference to the assignee's losses for the period following the transfer.[4] That is the case even if the effect is that the debtor may have to pay more as a consequence of the assignment. As admitted in the Fischer Opinion (para. 101) this corresponds to the prevailing opinion in the German legal literature,[5] while only a few authors take a contrary point of view.[6]

8. Sections 404, 406 and 407 BGB provide for several explicit rules which protect the debtor against legal disadvantages as a result of the assignment, i.e. disadvantages in his legal position as a consequence of the assignment, clearly demonstrating that the protection of the debtor provided by statutory law is not absolute.[7] Even if, as stated in the Fischer Opinion (para. 105), sections 404, 406 and 407 BGB imply a general principle that a debtor should not suffer any disadvantages as a consequence of the transfer, this principle would be limited to legal disadvantages. It cannot be extended

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[3] Any claim pursuant to Section 280 para. 1, in conjunction with Sections 280 para. 2, 286 and 288 German Civil Code for damages incurred which are capable of being expressed as a rate (see para. 21 of my opinion).

[4] See paragraphs 70-74 of my opinion.

[5] *Busche* in Staudinger, BGB, Section 398 n. 82; *Grüneberg* in Palandt, BGB, Section 398 n. 19; *Schwenzer* in AcP 182 (1982), 214, 234; *Hoffmann* in WM 1994, 1464, 1466; *Gernhuber* in Festschrift Raiser, p. 57, 86; cf BGH NVwZ-RR 2008, 674 n. 19 et seq (by citing *Grüneberg* in Palandt, BGB, 67th edition Section 398 n. 18a, now n. 19); BGH, NJW-RR 1992, 219 sub (not taking a stand).

[6] See para. 103 of the Fischer Opinion for references.

[7] *Busche* in Staudinger, BGB, Section 404 n. 2.

to factual disadvantages, e.g. disadvantages that may result from the fact that the new creditor (assignee) is behaving differently from the former creditor (assignor). This limitation is broadly accepted; even in the Fischer Opinion (para. 104) the generally applicable principle is limited to "*the legal position of the debtor*".

9. Insofar as damages are higher by referring to the person of the assignee than by referring to the person of the assignor, this presents a factual disadvantage, not a "legal" disadvantage.[8] The assignment does not affect the legal basis for calculating damages laid down in sections 249, 252 BGB.[9] The only difference is a factual one: a change in the person serving as the point of reference for calculating damages. A comparison of the situations dealt with by sections 404, 406 and 407 BGB and the question at hand, namely the replacement of the person serving as the point of reference for calculating damages, offers obvious support for the categorization as a mere factual disadvantage. Sections 404, 406 and 407 BGB deal with a debtor's contractual or statutory position vis-à-vis the creditor and which should not be affected by the assignment. Therefore, as stated in the Fischer Opinion (para. 105) these provisions "govern the question of objections, the capacity to offset, and the question of performance", which are all legal objections – in a broad sense – against the assigned claim. These provisions cannot be extended also to protect the debtor against factual disadvantages that result from facing a different person as creditor.

Issue 2: First sentence of clause 3(4) GMA contains a contractual downward modification of the statutory default interest rate

10. Having dealt with section 288 BGB in paragraphs 35 – 43 of the Fischer Opinion, Dr Fischer then states, in relation to clause 3(4) of the German Master Agreement, that this "*clause provides for a separate stipulation under which the person in possession of the claim is entitled in the event of a default*". I disagree that clause 3(4) provides a separate stipulation. Instead, the first sentence of clause 3(4) of the German Master Agreement contains a contractual downward modification of the statutory default interest rate (section 288 para. 1 BGB) for certain claims under the German Master Agreement and does not provide a separate contractual claim for default interest.

11. The reading of the first sentence as a contractual default interest claim would only make sense if, by implication, the right to statutory interest under section 288 para. 1 BGB was also waived by the first sentence. Nothing in the German Master Agreement indicates that the first sentence of clause 3(4) should replace section 288 para. 1 BGB, and, more to the point, there is no good reason why the parties would replace the statutory claim with a contractual claim which does not offer any advantages to the creditor over the statutory claim. Significantly, the Fischer Opinion does not argue that the first sentence of clause 3(4) is to be construed as an implied waiver of the right to statutory interest under section 288 para. 1 BGB (with the effect that the first sentence would replace the statutory claim with a contractual claim).

12. In addition, as already stated in my opinion (paragraphs 51-60), to construe the first sentence of clause 3(4) as a separate contractual basis for claiming default interest, rather than a downward modification of the rate specified in section 288 para. 1 BGB,

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[8] See *von Olshausen*, Gläubigerrechte und Schuldnerschutz bei Forderungsübergang und Regreß, p. 52 f.

[9] Moreover, the Minimum Damages Interest Claim (Section 288 BGB), awarding a rate determined by statute or by contract, does not depend on the situation of the assignor or of the assignee.

would disregard the wording of the first sentence which only deals with the interest rate as such, but not with the legal basis for being entitled to claim the rate as default interest.

Issue 3: Section 288 BGB as a subcategory of the general right to claim for damages for delay of performance

13. In paragraph 3 of the Fischer Opinion, Dr Fischer states that the claim under section 288(1) BGB is not a subgroup of the general damages claim for delay of performance pursuant to section 280 paragraphs 1 and 2 in conjunction with section 286 BGB. This position is also asserted in paragraph 38 of the Fischer Opinion. I disagree with this analysis for the reasons given below.

14. The legal prerequisites for a Minimum Damages Interest Claim pursuant to section 288 para. 1 BGB are:
    - (i) a money debt that results from a (legal) relationship between the parties based on contract or statute and
    - (ii) the default of the debtor.

    The requirements for a default within the meaning of section 288 para. 1 BGB are governed by section 286 BGB.[10]

15. As stated by the BGH in a landmark decision in 1979, the Minimum Damages Interest Claim is a subcategory of the general right to claim damages for delay of performance pursuant to section 280 para. 1 and 2 in conjunction with section 286 BGB.[11] This follows from the clarification in section 288 para. 4 BGB to the effect: "*The assertion of further damage is not excluded*" and, in particular, from the reference to "further" damage. Default interest awarded by section 288 para. 1 BGB serves as compensation for a (hypothetical) minimum loss suffered by the creditor.[12] In the event of a payment default in accordance with section 286 BGB, section 288 para. 1 BGB deviates from the requirement of actual damages, to award the creditor with a claim to compensate this minimum loss. The purpose of this derogation from general principles (i.e. the waiver of the need to demonstrate a damage actually incurred by the creditor), as already stated in my opinion, is to incentivize the debtor to pay on time.

16. The categorization of section 288 para. 1 BGB as a subcategory of the general right to claim damages for delay of performance indicates that that provision does not constitute a separate cause of action but serves as an ancillary rule to sections 280 and 286 BGB. However, even if section 288 para. 1 BGB would qualify as an independent basis for a claim,[13] this would only amount to a purely dogmatic classification and, thus, be a matter of legal theory, but would be without any practical relevance for the case at hand.

Issue 4: A claim for loss of profits is capable of expression as a rate under the circumstances given in paragraphs 37 and 38 of my opinion

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[10] See para. 28 of my opinion.

[11] See BGH, BGHZ 74, 231, 235 I.2.b.bb): "This provision is a specific expression of the principle that the debtor must reimburse the damage caused by delay, which is laid down in § 286 para 1 BGB." (unauthorized translation).

[12] BGH, NJW 1953, 337; KG Berlin, decision of 18 February 2014 – 26a U 60/13 (juris) n. 55.

[13] See paragraph 38 of the Fischer Opinion for further references.

17. Paragraph 87 of the Fischer Opinion appears to suggest that a claim for loss of profits is only ever capable of expression as a lump sum rather than a rate. In it, Dr Fischer states: "*If the damage, however, does not consist of lost interest income or in interest expense, it can only be asserted in the form of an amount. This is especially true if the creditor asserts that he would have used the owed money for an investment that would have brought him a profit (for example, an investment in shares which would have generated a particular capital gain for the period in question, or buying a machine with which he would have performed profitable work)*". I do not agree that a claim for loss of profits is *only ever* capable of expression as a lump sum rather than a rate.

18. In the context of the share investment example given in paragraph 87 of the Fischer Opinion, a distinction has to be made: if the purpose of investing in the shares is to generate an income by way of fixed return such as dividends, there is no reason why a claim for loss of profits could not be expressed as a rate rather than a lump sum, particularly if the investment period is not known at the time the claim is being asserted. To award a damage claim as an amount requires the final amount of such damage to be known at the time of the judgment being rendered. If, by contrast, the creditor were to claim for the loss of profit arising from a particular sale that was contemplated by the creditor, then I agree that the claim would only usually be capable of expression as an amount.

Issue 5: Damages Claims as a result of a default in the payment of the close-out amount under the GMA

19. In paragraph 79 of the Fischer Opinion, Dr Fischer states that the German Master Agreement "*does not provide for interest on the compensation claim: neither cl.7-9 nor any other provisions suggest that cl. 3(4) is also supposed to be applicable to this claim.*" I can see the force in this statement (for the reasons given below) although the contrary argument would be that there is no express exclusion of clause 3(4) in clauses 7 – 9 of the German Master Agreement. In any event, for the reasons given below, I do not consider that this would have any difference in practice to the calculation of the Further Damages Interest Claim (as defined in my opinion) and so the analysis in paragraphs 21 to 22 is included for the sake of completeness only.

20. In the case of a default (under section 286 BGB)[14] in the payment of the single compensation claim within the meaning of Clause 9 of the German Master Agreement (the "**Single Compensation Claim**")[15], regardless of whether clause 3(4) of the German Master Agreement applies, the debtor is entitled to claim damages pursuant to section 280 para. 1, in conjunction with sections 280 para. 2, 286 and 288 BGB. That includes a Minimum Damages Interest Claim pursuant to section 288 para. 1 BGB[16] whereby the statutory default interest rate applies. This implies that the default rate of interest per year is five percentage points above the basic rate of interest (section 247

[14] For the requirements of a default, see para. 28 of my opinion.

[15] Clauses 7, 8 and 9 of the German Master Agreement provide the rules for the termination (clause 7 of the German Master Agreement), the claims for damages and compensation for benefits received (clause 8 of the German Master Agreement) as well as for the creation of the Single Compensation Claim (clause 9 of the German Master Agreement), all together the so-called *close-out netting.* According to clause 9 of the German Master Agreement, all claims between the parties shall be netted [and] combined to a single compensation claim denominated in Euro.

[16] See paras. 29-32 of my opinion.

BGB)[17]. Neither clause 3(4) of the German Master Agreement nor clauses 7, 8 or 9 of the German Master Agreement have any impact on the statutory legal consequences of a default in the payment of the Single Compensation Claim.

21. Although there is a contrary argument (as outlined in paragraph 19 above), I consider that, on balance, clause 3(4) of the German Master Agreement only applies to claims for a delay in payment in respect of regular contractual payments as a result of the entering into a individual transaction within the meaning of clause 1(2) of the German Master Agreement and not to the Single Compensation Claim. This interpretation – following the principles of interpretation explained in paragraphs 23-26 of my opinion – results from the wording and the context of clause 3(4) within the German Master Agreement although I am not aware of any case law or academic commentary on the point.

22. According to clause 1(1) of the German Master Agreement the parties intended to enter into financial derivatives transactions. Clause 2 of the German Master Agreement sets out the procedure for the agreement of single financial derivatives transactions under the German Master Agreement. In turn, clause 3 of the German Master Agreement provides the rules for the payment of such single transactions. In this context, it could be argued that clause 3(4) only stipulates a contractual downward modification of the statutory default interest rate within the meaning of section 288 para. 1 BGB in cases of non-payment of obligations resulting from individual transactions within the meaning of clause 1(2) of the German Master Agreement. In addition, the position of clause 3(4) of the German Master Agreement at an earlier stage of the agreement than clause 9 of the German Master Agreement – as the provision pursuant to which the Single Compensation Claim is created – potentially indicates its irrelevance for the Single Compensation Claim.

23. Moreover, clauses 7, 8 and 9 of the German Master Agreement have no bearing on whether a late payment of the Single Compensation Claim may result in damages claims for delayed payment. In particular clause 7(3) of the German Master Agreement only refers to regular contractual payments within the meaning of clause 3(1) of the German Master Agreement, but not to Damages Claims as a result of a late payment of the Single Compensation Claim. This interpretation results from (i) the wording and the position of the clause within the German Master Agreement and (ii) the parties' (hypothetical) intention and according to the requirements of good faith, considering common usage and the objective meaning of the terms of contract.

   a. The irrelevance of clauses 7, 8 and 9 for a Damages Claim resulting from the late payment of the Single Compensation Claim follows from the wording of clause 7(3) of the German Master Agreement in conjunction with Clause 3(1) of the German Master Agreement, which do not refer to the Single Compensation Claim (although the counter-argument is that clauses 7, 8 and 9 do not expressly state that clause 3(4) does not apply to the Single Compensation Claim). In addition, the position of clause 7(3) of the German Master Agreement as an exclusion clause ahead of clause 9 as the clause creating the Single Compensation Claim indicates the irrelevance of clause 7(3) of the German Master Agreement for a Damages Claim as a result of a default in paying the Single Compensation Claim.

[17] See para. 30 of my opinion.

b. In no event can the German Master Agreement be construed to preclude the right of the creditor to claim damages because of a delay in payment of the Single Compensation Claim. Otherwise, a delay would be without sanction for the debtor. Such an interpretation would clearly deviate from the reasonable intention of the parties.

24. As a consequence, if the debtor is in default (under section 286 BGB) in the payment of the Single Compensation Claim, a Damages Claim pursuant to section 280 para. 1, in conjunction with sections 280 para. 2, 286 (and 288) BGB arises independently of the close-out netting and independently of the contractual downward modification of the statutory default interest rate in Clause 3(4) of the German Master Agreement. That implies that for a Minimum Damage Interest Claim within the meaning of section 288 para 1 BGB the statutory default interest rate applies. There is no impact, however, on the calculation of the Further Damages Interest Claim as defined in my opinion.

III. Statement regarding the expert's duty to the court

25. I have understood that I owe an overriding duty to the court to assist the court by providing objective, unbiased opinions within the areas of my expertise and that I should not assume the role of an advocate on behalf of the party from whom I receive instructions.

IV. Statement of truth

26. I confirm that I have made clear which facts and matters referred to in this report are within my own knowledge and which are not. Those what are within my knowledge I confirm to be true. The opinions I have expressed represent my true and complete professional opinions on the matter to which they refer.

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Professor Peter O. Mülbert

Dated: July 31, 2015

ANNEX A

ADDITIONAL MATERIALS RELIED UPON IN MAKING THE REPLY

1. Court decisions

1.1 Federal High Court (Bundesgerichtshof – BGH)

BGH, decision of 26 April 1979 - VII ZR 188/78 = BGHZ 74, 231

2. Books and Articles

von Olshausen, Gläubigerrechte und Schuldnerschutz bei Forderungsübergang und Regreß, 1988
Schwenzer in Archiv für civilistische Praxis (AcP) 182 (1982), p. 214 et seq
Hoffmann in Wertpapier Mitteilungen (WM) 1994, p. 1464 et seq
Gernhuber in Festschrift für Raiser (1973), Synallagma und Zession, p. 57 et seq

3. Statutory materials - The German Civil Code (Bürgerliches Gesetzbuch - BGB)

Section 406 Set-off in relation to the new oblige
Section 407 Legal acts in relation to the previous obligee

4. Expert Opinions

Expert Opinion of Professor Peter O. Mülbert as to Matters of German Law

Expert Opinion of Gero Fischer as to Matters of German Law
(Original version in German and English translation)