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UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In Re: MF GLOBAL INC., Debtor.	Case No. 11-2790 (MG) SIPA
KOCH SUPPLY & TRADING, LP, Plaintiff, v. JAMES W. GIDDENS, Trustee for the SIPA Liquidation of MF Global Inc., Defendant.	Adv. Pro. No. 12-01754 (MG)

MEMORANDUM OF LAW IN SUPPORT OF TRUSTEE'S MOTION FOR SUMMARY JUDGMENT ON COUNTERCLAIM

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James W. Giddens (the "Trustee"), as Trustee for the liquidation of MF Global Inc. ("MFGI" or "Debtor") under the Securities Investor Protection Act ("SIPA"), 15 U.S.C. §§ 78aaa *et seq*., by and through his undersigned counsel, respectfully submits this memorandum of law in support of his Motion for Summary Judgment on the Trustee's Counterclaim for declaratory relief.

PRELIMINARY STATEMENT

1. In moving for summary judgment on his counterclaim, the Trustee seeks a declaration that, upon the liquidation of MFGI, the full value of a certain letter of credit posted by Plaintiff Koch Supply & Trading, LP ("KS&T"), as margin in support of its commodities trading with MFGI constitutes "customer property," and therefore such full value must be immediately returned to the estate for inclusion in the pro rata distribution of customer property to former customers of MFGI. There are no material facts in dispute that would prevent the Court from granting this declaration. The Trustee asks this Court to determine in effect whether, in the administration of a commodity broker liquidation with a shortfall of customer property in the commodity customer estate, a customer who posted a letter of credit as margin should be treated preferentially to a customer who posted cash or securities as margin in support of commodities trading.

2. While in other contexts under Title 11 (the "Bankruptcy Code" or "Code") the proceeds of letters of credit are independent from a debtor's estate, a letter of credit posted by a customer as margin in support of commodity trading is plainly treated differently in the context of a commodity broker liquidation. Congress recognized over thirty years ago that the liquidation of a commodity broker is distinct from other proceedings administered under Chapter 7 and delegated to the Commodity Futures Trading Commission (the "CFTC") general

rulemaking authority with respect to, among other things, the definition of customer property in the specific context of a commodity broker liquidation. Pursuant to that authority, the CFTC adopted 17 C.F.R. § 190.08 ("Part 190.08"), which supplements the Bankruptcy Code's general treatment of letters of credit, and requires instead that "the full proceeds of a letter of credit . . . received, acquired or held to margin" be deemed customer property. Part 190.08(a)(1)(i)(E).

3. In adopting this specialized treatment of letters of credit in connection with commodity broker liquidations, the CFTC explicitly contemplated the precise issue now presented to this Court, explaining that "[i]f letters of credit are treated differently than Treasury bills, or other non-cash deposits, there would be a substantial incentive to use and accept such letters of credit as margin as they would be a means of avoiding the pro rata distribution of margin funds, contrary to the intent of the Code." 48 Fed. Reg. 8716-01, 8717, 1983 WL 170488 (1983). Consistent with this objective of equal treatment, the CFTC explained that Part 190.08's inclusion of letters of credit as customer property "require[s] a trustee to draw on the full proceeds of letters of credit irrespective of their terms." *Id.*

4. There is no doubt that the applicable CFTC regulations exempt letters of credit posted as margin with commodity brokers from the treatment of letters of credit generally under the Bankruptcy Code. Therefore, the full value of the letter of credit at issue here, $20 million, is customer property that must be included in the pro rata distribution of such property by the MFGI estate.

5. As the CFTC has made clear that letters of credit posted as margin should be treated no differently than margin posted in another form, the Trustee seeks to recover the customer property from KS&T, just as he would if KS&T were holding $20 million of customer property in the form of Treasury bills. KS&T has argued against the Trustee's recovery,

claiming: (i) the letter of credit at issue expired two months after the Filing Date, on December 31, 2011, and (ii) the Trustee is not within his contractual rights to drawn down on that letter of credit because the default provision in the letter of credit has not been met. KS&T's defenses are meritless. First, the economic consequence of the expiration of the letter of credit at issue was to reduce KS&T's contingent liabilities by a value of $20 million—which value consisted of $20 million of MFGI customer property—in advance of the Trustee's pro rata distribution of such property. Second, KS&T's argument ignores the CFTC's direction that pursuant to Part 190.08, the "full proceeds of [a] letter[] of credit *irrespective of [its] terms*" are customer property even where the letter of credit "condition[s] payment on delivery of a certification that additional funds are required to margin or to cover a default with respect to a contract." 48 Fed. Reg. 8716-01, 8717 (emphasis added). Third, KS&T's rationale abrogates the clear language of and policy underlying Part 190.08's specialized treatment of letters of credit: to treat customers that post letters of credit as margin the same as customers that deposit other forms of non-cash margin. *Id.*

6. Pursuant to the automatic stay in place under 11 U.S.C. § 362 and the MFGI Liquidation Order entered by the Honorable Paul A. Engelmayer, United States District Judge of the District Court for the Southern District of New York, in the case captioned *Securities Investor Protection Corp. v. MF Global Inc.*, Case No. 11-CIV-7750 (PAE), former MFGI customers are enjoined from taking "any act to obtain possession of property of the estate," which includes retention by a customer of its property belonging to the MFGI customer estate. *See* 11 U.S.C. § 362(a)(3). (*See also* Alinikoff Decl., Ex. A (MFGI Liquidation Order at III(C).) Accordingly, KS&T's possession of the $20 million of customer property upon the expiration of the letter of credit at issue violates the automatic stay, as it has recovered

possession of *its* property from MFGI in advance of the Trustee's pro rata distribution of the MFGI customer estate.

7. In adopting Part 190.08, the CFTC made clear its intent "to assure that customers using a letter of credit to meet original margin obligations [are] treated no differently than customers depositing other forms of non-cash margin or customers with excess cash margin deposits." 48 Fed. Reg. 8716-01, 8718. If KS&T is permitted to retain possession of *its* property that is due to the MFGI customer estate, KS&T will have priority treatment as compared to all other former MFGI customers that deposited other forms of non-cash margin or had excess margin obligations as of the Filing Date. Such an inequitable result is plainly contrary to the purpose and spirit of the Bankruptcy Code. Indeed, the only way for KS&T to prevail here is to establish that there are legitimate grounds for invalidating 17 C.F.R. §§ 190.01 through 190.10 (the "Part 190 Regulations")—particularly Part 190.08. KS&T is unable to meet that high burden and make such a showing.

STATEMENT OF FACTS

The SIPA Proceeding

8. Prior to its liquidation, MFGI was a futures commission merchant (a "FCM") subject to regulation by the CFTC. (Alinikoff Decl., Ex. B (Report of the Trustee's Investigation and Recommendations at 26, 31-32).) MFGI was also a registered securities broker-dealer subject to SIPA and regulation by the Securities and Exchange Commission.[1] (*Id.*)

9. Upon application by the Securities Investor Protection Corporation ("SIPC") on the Filing Date, the District Court entered the MFGI Liquidation Order. That order,

[1] As a securities broker-dealer, MFGI was also subject to regulation by the Financial Industry Regulatory Authority and the Chicago Board Options Exchange. (Alinikoff Decl., Ex. B (Report of the Trustee's Investigation and Recommendations at 26-27).) Because the Trustee's Motion for Summary Judgment relates to MFGI's role as a FCM, the relevant CFTC regulations are examined.

inter alia: (i) appointed James W. Giddens as Trustee for the liquidation of the business of MFGI under 15 U.S.C. § 78eee(b)(3); and (ii) removed the case to the Bankruptcy Court, before the Honorable Martin Glenn, for all purposes, as required by 15 U.S.C. § 78eee(b)(4) (the "SIPA Proceeding"). (Alinikoff Decl., Ex. A (MFGI Liquidation Order).)

10. Pursuant to 15 U.S.C. § 78fff(b) (2012), "to the extent consistent with the provisions of [SIPA]," the Trustee shall conduct the liquidation of MFGI "[i]n accordance with, and as though it were being conducted under chapters 1, 3 and 5 and subchapters I and II of chapter 7 of Title 11." The Trustee is also "subject to the same duties as a trustee in a case under chapter 7 of Title 11, including, if the debtor is a commodity broker." SIPA § 78fff-1(b).

11. The commodity broker liquidation provisions of the Bankruptcy Code, codified at 11 U.S.C. §§ 761-767 ("subchapter IV of chapter 7" or the "Commodity Broker Liquidation Provisions"), govern the liquidation of FCMs like MFGI. Congress granted the CFTC, in its role as the government regulator for FCMs, general rulemaking authority to enact regulations to govern the liquidation of a "commodity broker that is a debtor under chapter 7 of Title 11." 7 U.S.C. § 24(a). Those regulations, which are *singularly* applicable to a FCM liquidation, are found at the Part 190 Regulations.

12. The Part 190 Regulations provide detailed rules for the liquidation of a FCM, with a special focus on the identification, marshaling, and equitable pro rata distribution of the property of the FCM's former customers through the vehicle of the Bankruptcy Code. Specifically, the definition of "customer property" in the context of a FCM liquidation is set forth at Part 190.01(o) and includes property listed in Part 190.08. Included in the scope of customer property under Part 190.08 are the "full proceeds of a letter of credit if such letter of

credit was received, acquired or held to margin, guarantee, secure, purchase or sell a commodity contract." Part 190.08(a)(1)(i)(E).

13. Upon entry of the MFGI Liquidation Order, the commodity futures accounts of tens of thousands of customers, and the property in those accounts, came under the Trustee's control for administration under SIPA and the Part 190 Regulations. (Alinikoff Decl., Ex. C (Trustee's First Interim Report ¶ 15).) KS&T is one of those customers. Notwithstanding the significant efforts of the Trustee the MFGI estate is faced with a substantial shortfall in customer funds.

14. On November 15, 2011, the Trustee filed an Application for Expedited Relief (the "Trustee's Application"), which requested, among other things, that the Court allow the Trustee to proceed with the administration of the MFGI estate pursuant to the "procedures prescribed in 17 C.F.R. § 190.08 . . . for the allocation and distribution of commodity futures customer property to claimants." (Alinikoff Decl., Ex. D (Trustee's Application ¶ 31) [SIPA ECF No. 144].) Shortly thereafter, this Court entered the MFGI Claims Process Order approving the Trustee's request to, among other things, "satisfy commodity futures customer claims" pursuant to the "procedures prescribed in 17 C.F.R. § 190.08 for allocation and distribution of commodity futures customer property." (Alinikoff Decl., Ex. E (MFGI Claims Process Order, at 4) [SIPA ECF No. 423].)

The KS&T Letter of Credit

15. Prior to MFGI's liquidation, KS&T traded commodity futures contracts through MFGI pursuant to the parties' Customer Agreement, dated January 1, 2002 (the "Customer Agreement").[2] (Alinikoff Decl., Ex. F (Customer Agrmt.).) KS&T, like all other

[2] The parties to the Customer Agreement are KS&T and Man Financial, Inc., predecessor to MFGI.

customers who actively traded through MFGI, was required to post margin. (*Id.* (Customer Agrmt. ¶ 3).) Nearly every MFGI customer posted margin in the form of cash or securities. KS&T, however, was one of a small handful of MFGI customers (nine in total) that instead posted margin in the form of letters of credit.[3]

16. As of the Filing Date, KS&T had posted two letters of credit to margin its futures trading activity through MFGI: (i) an irrevocable standby letter of credit issued by Royal Bank of Scotland N.V., in an amount (as amended) of $20 million for the joint benefit of MFGI and the Chicago Mercantile Exchange in support of its domestic exchange trading pursuant to section 4d of the Commodities Exchange Act (the "CEA"); and (ii) an irrevocable standby letter of credit issued by JP Morgan Chase Bank, N.A., in an amount (as amended on October 11, 2011) of $20 million for the benefit of MFGI in support of its foreign exchange trading pursuant to 17 C.F.R. § 30.7 (the "30.7 LOC") (Alinikoff Decl., Ex. I). Only the 30.7 LOC is the subject of the parties' current dispute.

17. Eighteen days before MFGI was placed into liquidation, KS&T and MFGI amended the value of the 30.7 LOC to its present $20 million value.

18. As of the Filing Date, MFGI's books reflected a $20 million margin value in connection with KS&T's foreign futures trading accounts at MFGI. (Alinikoff Decl., Ex. J (KS&T Equity Run Report, at "F2 USD - Secured," Oct. 31, 2011).)

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[3] ConocoPhillips Company and ConocoPhillips Canada (collectively "ConocoPhillips") are the only other former MFGI commodity futures customers that dispute the Trustee's position on letters of credit. On October 4, 2012, the Honorable Katherine B. Forrest of the U.S. District Court for the Southern District of New York granted ConocoPhillips' motion to withdraw the reference of the Trustee's Motion for an Order Confirming the Trustee's Determination of ConocoPhillips' Claims to Customer Accounts Margined with Letters of Credit (the "Mot. to Confirm Determination of ConocoPhillips"). *ConocoPhillips Co. v. Giddens*, Case No. 12-CV-6014 (KBF) (the "Contested Matter"); (Alinikoff Decl., Ex. G (Mem. & Order, Oct. 4, 2012 [Contested Matter ECF No. 26].) The briefing schedule in the Contested Matter is similar to the schedule in place here. (Alinikoff Decl., Ex. H (Contested Matter Br. Sched.) [Contested Matter ECF No. 27].)

19. Two months after the Filing Date, on December 31, 2011, pursuant to its terms, the 30.7 LOC expired.

The KS&T Customer Claim

20. On April 6, 2012, KS&T filed an untimely customer claim with the Trustee in the SIPA Proceeding seeking a return of property from MFGI "in the event that the Trustee recovers any property from KS&T on account of the 30.7 [LOC]." (Alinikoff Decl., Ex. K (KS&T Customer Claim at 3, Apr. 6, 2012).) In its claim, KS&T takes the position that the LOC is *not* customer property, and that it therefore should be considered outside of the normal pro rata distribution process, allowing KS&T to keep the full proceeds of the 30.7 LOC outright.

21. On June 22, 2012, the Trustee denied KS&T's customer claim.[4] (*See* Alinikoff Decl., Ex. L (Notice of Trustee's Determination of Claim, June 22, 2012).) KS&T filed an objection on July 20, 2012, disputing the Trustee's determination. (Alinikoff Decl., Ex. M (KS&T Opp'n to Trustee's Notice of Determination of Claim ("KS&T Objection")).)

22. KS&T commenced this proceeding (the "Adversary Proceeding") on July 19, 2012, by filing a complaint against the Trustee. Pursuant to the Court's So-Ordered Joint Briefing Schedule (the "Briefing Schedule") [ECF No. 23], KS&T filed an amended complaint on October 5, 2012, seeking a declaratory judgment that it does not have any liability to the estate under 11 U.S.C. §§ 362, 542, 549, 550, or 764 in connection with the 30.7 LOC. (*See* Am. Compl. at 7 [ECF No. 24].) The Trustee answered the amended complaint and, pursuant to the Briefing Schedule, filed a counterclaim for a declaratory judgment that: (i) the face value of the 30.7 LOC, $20 million, with interest, constitutes customer property pursuant to 11 U.S.C. §§ 761-767 as supplemented by Part 190.08; and (ii) KS&T must immediately pay to the Debtor

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[4] The Trustee fully reserves his right to contest KS&T's commodity futures customer claim, filed on April 6, 2012, including on the ground of untimeliness.

the face value of the 30.7 LOC, $20 million, with interest, pursuant to the Trustee's powers under Part 190.08 and Title 11, including §§ 362, 542, 549, 551, or 764, for inclusion in the pro rata distribution of customer property to former customers of MFGI. (*See* Answer to Am. Compl. [ECF No. 25].)

23. In addition to the Adversary Proceeding, on July 20, 2012, KS&T also commenced an action in the U.S. District Court for the Southern District of New York to withdraw the reference of this proceeding to the Bankruptcy Court. *Koch Supply & Trading, LP v. Giddens*, Civ. Case No. 12-CV-05596 (NRB). (Alinikoff Decl., Ex N (KS&T Mot. to Withdraw the Reference at 2) [ECF No 4].) That motion is fully briefed and pending before the Honorable Naomi Reice Buchwald.

ARGUMENT

24. The standards governing a summary judgment motion are well settled. *See, e.g., In re S.W. Bach & Co.*, 435 B.R. 866, 877 (Bankr. S.D.N.Y. 2010); *In re Mason Hill & Co.*, Case No. 95-99999 (SMB), 2004 WL 2659579, at *4 (Bankr. S.D.N.Y. Oct. 18, 2004). Pursuant to Federal Rule of Civil Procedure 56, made applicable to these proceedings pursuant to Rule 7056 of the Federal Rules of Bankruptcy Procedure, a court must grant summary judgment "if the movant shows that there is no genuine dispute as to any material fact and the movant is entitled to judgment as a matter of law." Fed. R. Civ. P. 56(a). Accordingly, the moving party initially bears the burden of establishing that the undisputed facts entitle him to judgment as a matter of law. *Mason Hill,* 2004 WL 2659579, at *4 (citing *Rodriguez v. City of New York,* 72 F.3d 1051, 1060-61 (2d Cir. 1995)). Upon carrying this burden, to withstand a grant of summary judgment in favor of movant, the nonmoving party must then "set forth specific facts that show triable issues, and cannot rely on pleadings containing mere allegations or denials." *Id.* (citing

Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 586-87 (1986)). "In deciding whether material factual issues exist, the Court must resolve all ambiguities and draw all reasonable inferences against the moving party." *Id.* (citations omitted).

25. No "material factual issues" exist here that would preclude this Court from granting summary judgment in favor of the Trustee on his counterclaim. *See id.* The legal issue presented is quite simple: whether, pursuant to the Commodity Broker Liquidations Provisions as supplemented by the Part 190 Regulations, the full value of the 30.7 LOC constitutes property belonging to the MFGI customer estate, which is being held by KS&T in advance of the Trustee's pro rata distribution of such property and in violation of the automatic stay.

26. The clear intent of the Part 190 Regulations is to ensure that, in a commodity broker liquidation, customers who posted letters of credit "to meet original margin obligations [are] treated no differently than customers depositing other forms of non-cash margin." 48 Fed. Reg. 8716-01, 8718. Consistent with this objective, the CFTC considered that upon the liquidation of a commodity broker, the full face value of such letters of credit should be "deemed" customer property for inclusion in the pool of assets subject to pro rata customer distribution. *Id.* Accordingly, as of the Filing Date, the full proceeds of the 30.7 LOC—$20 million—are customer property belonging to the MFGI customer estate. The economic reality, therefore, is that upon expiration of that 30.7 LOC, $20 million of MFGI customer property operated to reduce KS&T's contingent liabilities by that amount, and KS&T's possession of those proceeds continues in violation of the automatic stay.

I. THE FULL PROCEEDS OF LETTERS OF CREDIT POSTED AS MARGIN ARE "CUSTOMER PROPERTY" PURSUANT TO PART 190.08

27. In furtherance of the CFTC's goal of ensuring equal treatment of customers of failed FCMs, Part 190.08 provides that, upon liquidation of a FCM, the full face

value of a letter of credit held by a FCM to margin a customer's futures trading is "customer property" within the meaning of Chapter 7 of the Bankruptcy Code and Part 190.08. Accordingly, that full face value—here, $20 million—is an asset of the FCM's customer estate that must be included in the pro rata distribution of such property to former customers.

A. Part 190.08's Definition of "Customer Property" to Include the Full Proceeds of Letters of Credit is Supported by the Commodity Broker Liquidation Provisions' Definition and the CFTC's Congressional Mandate

28. Part 190.08's inclusion of the full proceeds of letters of credit held by FCMs as margin in its definition of "customer property" not only complements the Commodity Broker Liquidation Provisions' definition, but also comports with the CFTC's Congressional mandate to "provide that certain cash, securities, other property, or open contractual commitments are to be included in or excluded from customer property." S. Rep. No. 95-989 (1978), *as reprinted in* 1978 U.S.C.C.A.N. 5787, 1978 WL 8531, at *159. Correspondingly, the CEA explains that the CFTC "may provide that certain cash, securities, other property, or commodity contracts are to be included in or excluded from customer property." 7 U.S.C. § 24(a)(1) (2012) (effective Nov. 6, 1978).

29. In administering the liquidation of MFGI, the Trustee's duties include liquidating the commodity broker arm of MFGI to the extent not inconsistent with SIPA. SIPA § 78fff-1(b). That liquidation is administered pursuant to the Commodity Broker Liquidation Provisions, as supplemented by the CEA, 7 U.S.C. § 1 *et seq.,* and the Part 190 Regulations promulgated by the CFTC thereunder. *In re MF Global Inc.*, No. 11-2790 (MG), 2012 WL 769519, at *2 (Bankr. S.D.N.Y. Mar. 7, 2012).

30. The Commodity Broker Liquidation Provisions were enacted pursuant to the Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (1978). In enacting these

specialized provisions, Congress recognized the unsuitability of the existing bankruptcy law to deal with the liquidation of a commodity broker:

> Since the first comprehensive bankruptcy legislation was enacted in 1800, bankruptcy laws have never specifically addressed the *unique problems* raised by commodity broker bankruptcies. With no cohesive policy for guidance, courts dealing with commodity broker bankruptcies have applied existing laws which are not necessarily consistent with the structure of, and may be potentially disruptive of, commodity futures, options, and leverage markets.

S. Rep. No. 95-989, 1978 WL 8531, at *7 (emphasis added). (*See also* Alinikoff Decl., Ex. O (CFTC Statement in Response to ConocoPhillips' Motion to Withdraw the Reference (the "CFTC Statement") at 5-7) [Contested Matter ECF No. 20].)

31. In light of the "unique problems raised by commodity broker bankruptcies," Congress further directed that implementation of the Commodity Broker Liquidation Provisions would require regulation in addition to the procedures set forth at §§ 761-767 of the reformed Bankruptcy Code:

> The commodity broker subchapter provides *only a framework* within which commodity broker liquidations are to be administered. Due to the germinal state of regulation of the commodities industry, the subchapter does not provide detailed rules to cover every contingency. Instead, general rulemaking authority has been delegated to the CFTC with respect to the contents and determination of net equity; definition of 'customer property,' 'member property' 'commodity options dealer,' 'commodity contract,' and 'clearing organization' . . .

S. Rep. No. 95-989, 1978 WL 8531, at * 8 (emphasis added).

32. It is well settled that where "Congress has explicitly left a gap for the agency to fill, there is an express delegation of authority to the agency to elucidate a specific provision of the statute by regulation." *Chevron v. Natural Res. Def. Council, Inc.*, 467 U.S. 837, 843-44 (1984). Pursuant to this express delegation of authority, the CFTC adopted the Part 190 Regulations to provide a comprehensive set of instructions to a trustee administering the liquidation of a commodity broker estate. (*See, e.g.* Alinikoff Decl., Ex. O (CFTC Statement at

5-7).) The Part 190 Regulations are consistent with the framework provided by the Commodity Broker Liquidation Provisions and the CFTC's Congressional mandate. They also amplify the subchapter where—in the CFTC's view—special provisions are necessary to square the "unique problems" raised by the liquidation of a commodity broker with the fundamental purpose of the Commodity Broker Liquidation Provisions: "to ensure that the property entrusted by customers to their brokers will not be subject to the risks of the broker's business and will be available for disbursement to customers if the broker becomes bankrupt." S. Rep. No. 95-989, 1978 WL 8531, at *106.

33. Of particular note here is the accord between the Commodity Broker Liquidation Provisions' definition of "customer property" and that of Part 190.08, including Part 190.08's treatment of letters of credit. In amending the Bankruptcy Code, Congress set forth a baseline definition of "customer property" at § 766(10). In enacting the CEA, Congress directed the CFTC to "provide with respect to a commodity broker that is a debtor under chapter 7 of title 11, by rule or regulation - that certain cash, securities, other property, or commodity contracts are to be included or excluded from customer property." 7 U.S.C. § 24(a)(1). Pursuant to this directive, the CFTC determined that, among other things, letters of credit should be treated in a specialized manner in the context of a commodity broker liquidation and included in the scope of customer property in accordance with that treatment. *See* Part 190.08(a)(i)(E).

34. The Commodity Broker Liquidation Provisions define "customer property" as:

> cash, a security, or other property, or proceeds of such cash, security, or property, received, acquired, or held by or for the account of the debtor, from or for the account of a customer— (A) including— (i) *property received, acquired, or held to margin, guarantee, secure, purchase, or sell a commodity contract*. . .

11 U.S.C. § 761(10)(A)(i) (emphasis added).

35. Similarly, pursuant to Part 190.08(a), "customer property" includes, in relevant part:

> (i) cash, securities, or other property or the proceeds of such cash, securities or other property received, acquired, or held by or for the account of the debtor, from or for the account of a customer, including a non-public customer, which is:
>
> (A) *Property received, acquired or held to margin, guarantee, secure, purchase or sell a commodity contract*; . . .
>
> (E) *The full proceeds of a letter of credit if such letter of credit was received, acquired or held to margin, guarantee, secure, purchase or sell a commodity contract* . . .
>
> (ii) All cash, securities, or other property which: . . .
>
> (G) Is property of the debtor that any applicable law, rule, regulation, or order requires to be set aside for the benefit of customers, unless including such property in the customer estate would not significantly increase the customer estate. . . .

Part 190.08(a)(1)(i)-(ii) (emphases added).

36. In defining the scope of customer property to include, *inter alia*, "the full proceeds of a letter of credit if such letter of credit was received, acquired or held to margin," the CFTC was clearly acting within the limits of its Congressional authority to "provide that certain cash, securities, other property, or open contractual commitments are to be included or excluded from customer property." S. Rep. No. 95-989, 1978 WL 8531, at *159, *amending* 7 U.S.C. § 24(a)(1).

37. Finally, in passing the Dodd-Frank Wall Street Reform Act ("Dodd-Frank"), Congress amended various portions of the Bankruptcy Code and the CEA. 12 U.S.C. § 5301, Pub. L. 111-203, 2010 H.R. 4173, at Title II & VII (July 21, 2010). Significantly, Congress left untouched the scope of customer property as designated by Part 190.08, including the treatment of letters of credit under Part 190.08(a)(1)(i)(E). The CFTC adopted final regulations to implement the new statutory provisions enacted by the Dodd-Frank's Title VII.

See 77 Fed. Reg. 6336-01 (Feb. 7, 2012) (codified at 17 C.F.R. pts. 22 & 190). Consistent with the Dodd-Frank mandate, the CFTC's Dodd-Frank Part 190 Rule Amendments did not alter the scope of customer property, which continues to include "[t]he full proceeds of a letter of credit if such letter of credit was received, acquired or held to margin, guarantee, secure, purchase or sell a commodity contract." Part 190.08(a)(1)(i)(E).

38. Where "Congress is, or should be, aware of an interpretation of a statute by the agency charged with its administration, Congress' amendment or reenactment of the statutory scheme without overruling or clarifying the agency's interpretation is considered as approval of the agency interpretation." *See Casey v. Comm'n of Internal Revenue*, 830 F.2d 1092, 1095 (10th Cir. 1987); *see also Isaacs v. Bowen*, 865 F.2d 468, 473 (2d Cir. 1999). In enacting Dodd-Frank, Congress was undoubtedly aware of and considered the Part 190 Regulations, including Part 190.08's definition of customer property, and chose not to overrule or clarify the CFTC's interpretation of customer property thereunder. Specifically, Dodd-Frank addressed 7 U.S.C. § 24—the section of the CEA directing the CFTC to enact regulations defining the scope of customer property in a commodity broker liquidation (*i.e.,* the Part 190 Regulations). *See* 7 U.S.C. § 24(a)(1). In amending the CFTC's regulatory powers with respect to the definition of customer property, Dodd-Frank *enlarged* the CFTC's regulatory authority in this regard, directing the CFTC to "exercise its authority to ensure that securities held in a portfolio margining account carried as a futures account are customer property and the owners of those accounts are customers for the purposes of subchapter IV of chapter 7 of title 11." Dodd-Frank, Title VII, Sec. 763(c), *codified at* 7 U.S.C. § 24(c) (2012). Therefore, because Congress clearly considered the scope of the CFTC's rulemaking authority and its interpretation of customer property under the Commodity Broker Liquidation Provisions and Part 190

Regulations, and because Congress did not overrule or clarify the CFTC's interpretation in that regard, Part 190.08's treatment of letters of credit is considered to be approved by Congress' passage of Dodd-Frank. *Casey,* 830 F.2d at 1095.

B. The Commodity Broker Liquidation Provisions and Part 190.08 Require the Full Proceeds of Letters of Credit to Be Included in the Pro Rata Distribution of Customer Property to Former Customers of Failed FCMs

39. The purpose of the Commodity Broker Liquidation Provisions is to ensure that the risk of a commodity broker's bankruptcy is not borne by the customer. *See, e.g., In re Stotler & Co.*, 144 B.R. 385, 392 (N.D. Ill. 1992). Accordingly, under the Commodity Broker Liquidation Provisions, as supplemented by the Part 190 Regulations, "commodity customers are granted the highest priority against the bankrupt broker's estate, thereby furthering the purposes of the [CEA] by enhancing customer protection and promoting customer confidence in commodity markets generally." *See, e.g., In re Bucyrus Grain Co.*, 127 B.R. 45, 51-52 (D. Kan. 1988) (citing S. Rep. No. 95-989, 1978 WL 8531, at *7-8), *appeal dismissed*, 905 F.2d 1362 (10th Cir. 1990). The mechanism by which this objective is achieved is the customer distribution scheme, defined at § 766(h) of the Commodity Broker Liquidation Provisions as modified by the Part 190 Regulations, which requires a trustee to distribute all customer property on a pro rata basis.

40. Pursuant to § 766(h) of the Commodity Broker Liquidation Provisions, a trustee is required to distribute customer property as follows:

> Except as provided in subsection (b) of this section, the trustee shall distribute customer property ratably to customers on the basis and to the extent of such customers' allowed net equity claims, and in priority to all other claims, except claims of a kind specified in section 507(a)(2) of this title that are attributable to the administration of customer property.

11 U.S.C. § 766(h).

41. Similarly, Part 190.01(o) directs the Trustee to both § 766(h) and Part 190.08 in distributing customer property, explaining that "[c]ustomer property [and] customer estate are used interchangeably to mean the property subject to pro rata distribution in a commodity broker bankruptcy which is entitled to the priority set forth in § 766(h) of the Bankruptcy Code and includes certain cash, securities, and other property as set forth in § 190.08(a)."

42. Consequently, the pro rata distribution of customer property described at § 766(h) is supplemented by the property listed in Part 190.08, which includes the full proceeds of letters of credit received by FCMs as margin in support of a customer's commodity futures trading.

43. The decision to include the full proceeds of letters of credit as customer property in the context of a commodity broker liquidation was not without its detractors. In vetting the Part 190 Regulations before implementation, the CFTC, as required, published the proposed broker-dealer liquidation instructions for comment on November 24, 1981. 46 Fed. Reg. 57535-01, 1981 WL 112816 (Nov. 24, 1981) (codified at 17 C.F.R. pt. 190). With specific regard to letters of credit, the CFTC noted that "[l]etters of credit are singled out for special treatment because the Commission believes that it is important to make clear that the full value of a letter of credit posted as margin would be drawn in the event of a bankruptcy and the full proceeds thereof would be treated as customer property." *Id.* at 57553.

44. As the CFTC noted in its final rule adoption, several commentators took issue with Part 190.08's "special treatment" of letters of credit and requested an amendment providing "that letters of credit be drawn upon only in accordance with their terms and only to the extent of the margin owing by the depositor." 48 Fed. Reg. 8716-01, 8718. Those

commentators also argued that such an amendment to Part 190.08 was necessary because "to permit the trustee to bring the full proceeds of a letter of credit into the estate would impose a burden on customers who post letters of credit as security and would therefore discourage their use." *Id.* Finally, commentators also noted that without an amendment, "the proposed rule would require a trustee to draw the full proceeds of letters of credit *irrespective of their terms* even though they generally condition payment on delivery of a certification that additional funds are required to margin or to cover a default with respect to a contract." *Id.* (emphasis added).

45. The CFTC, in accordance with the Commodity Broker Liquidation Provisions' main objective of customer protection, rejected any such proposed amendments to Part 190.08's treatment of letters of credit. Instead, the CFTC noted that:

> The Commission's proposal was intended to assure that customers using a letter of credit to meet original margin obligations *would be treated no differently* than customers depositing other forms of non-cash margin or customers with excess cash margin deposits. If letters of credit are treated differently than Treasury bills or other non-cash deposits, there would be a substantial incentive to use and accept such letters of credit as margin as they would be a means of avoiding the pro rata distribution of margin funds, contrary to the intent of the Code.
>
> * * * *
>
> In making this determination, the Commission also was guided by certain additional policy considerations. First, the Commission recognizes that standby letters of credit are not subject to banking reserve requirements and may be uncollateralized. In a period of major changes to the financial services which may be extended by banks and some corresponding uncertainty as to the wisdom of virtually unrestricted writing of standby letters, the Commission believes that it would be unwise to adopt a policy which would further encourage the use of letters of credit and, indeed, their substitution for other forms of margin. Second, it would be inherently unfair to treat letters of credit differently from other financial instruments such as Treasury Bills which have been deposited with commodity brokers as original margin. Third, encouraging the use of letters of credit would favor large customers at the expense of smaller market participants since only larger customers are permitted to make non-cash deposits of margin. This would contravene the spirit and intent of the Code's limitations on the return of specifically identifiable property which were intended to assure parity between customers with margining power and those without it.

Id. at 8718-19 (emphasis added).

46. The language of Part 190.08, as well as the commentary enacting it, could not be more clear: the full proceeds of a letter of credit—if such letter of credit was received, acquired or held to margin commodities trading—are property of a failed FCM's customer estate and subject to pro rata distribution. In enacting this regulation, the CFTC recognized the inherent contradiction between the Code's purpose and the treatment of letters of credit in the commodity broker liquidation context absent such a specialized regulation. Indeed, this is precisely the type of "unique problem raised by commodity broker bankruptcies" for which Congress directed the CFTC to create a contingency; Part 190.08(a)(1)(i)(E) is just that contingency. S. Rep. No. 95-989, 1978 WL 8531, at *7.

II. KS&T'S POSSESSION OF $20 MILLION INTENDED AS MARGIN TO SUPPORT ITS COMMODITY TRADING IS A VIOLATION OF THE AUTOMATIC STAY PURSUANT TO 11 U.S.C. § 362 AND THE MFGI LIQUIDATION ORDER

47. KS&T's possession of the full value of the 30.7 LOC—$20 million—is a retention of its property that first belongs to the MFGI customer estate before KS&T may possess it. Such retention continues in violation of the automatic stay in place pursuant to 11 U.S.C. § 362 and the MFGI Liquidation Order.

A. Pursuant to Part 190.08, the Full Value of the 30.7 LOC—$20 Million—is Customer Property Belonging to the MFGI Customer Estate

48. It is beyond dispute that, as of the Filing Date, the "full proceeds" of the 30.7 LOC—$20 million—are customer property subject to the identical treatment afforded to other forms of non-cash margin, such as Treasury bills. Part 190.08(a)(1)(i)(E). In fact, such treatment is reflected in MFGI's books and records, which as of the Filing Date reflect a $20 million margin value in connection with KS&T's foreign futures trading accounts at MFGI. (Alinikoff Decl., Ex. J (KS&T Equity Run Report, at "F2 USD - Secured," Oct. 31, 2011) (reflecting $20 million margin value ("MV").) The value reflected is identical to that of other

customers who posted Treasury bills. As of the Filing Date, both forms of margin were assets of the MFGI customer estate.

49. In determining whether the "full proceeds" of the 30.7 LOC—$20 million—are customer property to be included in the pro rata distribution to MFGI customers, the plain language of Part 190.08 is controlling. *Chevron*, 467 U.S. at 843-44 ("If Congress has explicitly left a gap for the agency to fill, there is an express delegation of authority to the agency to elucidate a specific provision of the statute by regulation. Such legislative regulations are given controlling weight unless they are arbitrary, capricious, or manifestly contrary to the statute."); *see also In re Donald Sheldon & Co.*, 148 B.R. 385, 387 (Bankr. S.D.N.Y. 1992) (SIPA) (holding that "proceeds" of liquidated brokerage firm assets constitute customer property where such assets were purchased by hypothecating fully paid customer securities). As discussed *supra*, Part 190.08 includes as customer property "the full proceeds of a letter of credit if such letter of credit was received, acquired or held to margin;" that comports with the definition set forth at § 766(10) and the Congressional mandate directing the CFTC to "provide . . . by rule or regulation - that certain cash, securities, other property, or commodity contracts are to be included or excluded from customer property." 7 U.S.C. § 24(a)(1).

50. Accordingly, the full proceeds of the 30.7 LOC, like all other margin funds, are customer property belonging to the MFGI customer estate—they must first be brought into the estate and added to the pool of MFGI customer property for pro rata distribution before KS&T can make a claim to those funds as a former customer. *See, e.g., Bucyrus*, 127 B.R. at 51-52 (funds deemed to be customer property "should be a part of the customer property to be apportioned among customers," and once included, customers may then make a valid claim against such property).

51. The Trustee respectfully submits that judgment for the Trustee declaring the full proceeds of the 30.7 LOC—$20 million—plus interest, constitutes customer property pursuant to 11 U.S.C. §§ 761-767 as supplemented by 17 C.F.R. 190 *et seq.*, is appropriate.

B. Neither the Expiration of Nor the Default Provision in the 30.7 LOC Limits the Trustee's Right to Recover the Customer Property in Possession of KS&T

52. KS&T has contended that even if the Court accepts the Trustee's proposition that the full proceeds of a letter of credit are customer property, the Court would still have to find in favor of KS&T because: (i) in order to draw on the 30.7 LOC prior to its expiration, the Trustee would have had to present to the issuing bank evidence of KS&T's default under the terms of the Customer Agreement, and it is uncontested that no such default occurred; and (ii) the Trustee's right to 30.7 LOC customer property extinguished upon expiration of the 30.7 LOC. (Alinikoff Decl., Ex G (KS&T Mot. to Withdraw the Reference at 2) [ECF No 4].)

53. KS&T's arguments necessarily fail for three reasons: (i) the economic reality is that upon expiration of the 30.7 LOC, $20 million of MFGI customer property operated to reduce KS&T's contingent liabilities by that amount, in advance of the Trustee's pro rata distribution of such property; (ii) KS&T's argument ignores the CFTC's direction that pursuant to Part 190.08, the "full proceeds" of a letter of credit are customer property "*irrespective of [the letter of credit's] terms,*" 48 Fed. Reg. 8716-01, 8717 (emphasis added); and (iii) KS&T's rationale abrogates the policy reason underlying Part 190.08's specialized treatment of letters of credit: to treat customers that posted letters of credit as margin the same as customers that deposited other forms of non-cash margin.[5] *Id.*

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[5] The Trustee also notes that the estate's right to recover the $20 million in customer property held by KS&T as of the Filing Date was preserved prior to expiration of the 30.7 LOC pursuant to, inter alia: (i) the Trustee's (*cont'd . . .*)

(i) The Post-Petition Expiration of the 30.7 LOC Reduced KS&T's Contingent Liabilities with $20 Million of MFGI Customer Property in Advance of the Pro Rata Distribution

54. Contrary to KS&T's proposition, the expiration of the 30.7 LOC does not result in the corresponding "expiration" of the customer property associated therewith. Part 190.08(a)(1)(i)(E) (customer property includes "the full proceeds of a letter of credit . . . received, acquired or held to margin"). In a post-petition context, the only consequence of a post-petition expiration is to distribute MFGI customer property to KS&T in advance of the Trustee's distribution of that property to all customers with valid claims.

55. Pursuant to the Code's definition of "claim," MFGI's "claim" to the full proceeds of the 30.7 LOC arose when it was appointed as the beneficiary thereunder; therefore, the Trustee's "claim" to the full proceeds already existed as of the Filing Date. 11 U.S.C. § 101(5)(A) (defining "claim" as the "right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured"). Correspondingly, as of the Filing Date, the "debt" or "liability on [the Trustee's] claim" to the full proceeds of the 30.7 LOC became fixed in accordance with the Part 190 Regulations' treatment of letters of credit posted as margin. 11 U.S.C. § 101(12); *see also In re ATS Prods. Corp.*, No. 01-13220F, 2003 WL 25947346, at *14 (E.D. Pa. June 5, 2003).

56. Similarly, the CFTC has made clear its interpretation that "[o]nce the FCM is placed into bankruptcy, the Trustee's right to that money, and any resulting obligations on the part of the customer are *fixed*." (Alinikoff Decl., Ex. P (CFTC Mem. in Supp. of the Trustee's Mot. to Confirm, at 24) [Contested Matter ECF No.33] (emphasis added).) The CFTC

Application (Alinikoff Decl., Ex. D (Trustee's Application ¶ 31) [SIPA ECF No. 144]); and (ii) the MFGI Claims Process Order (Alinikoff Decl., Ex. E (MFGI Claims Process Order, at 4) [SIPA ECF No. 423].)

went on to add that it "stressed the need 'to fix' each customer's 'bankruptcy losses at a particular point in time." *Id.* (*citing* 46 Fed. Reg. at 57547). Accordingly, the Trustee's possessory right to the 30.7 LOC proceeds is not extinguished or limited by virtue of the expiration of the 30.7 LOC.

57. As the Trustee's claim to the $20 million of customer property was fixed as of the Filing Date under Part 190.08, the only function of the post-petition expiration of the 30.7 LOC is to shift the party in possession of those assets. Prior to expiration of the 30.7 LOC, $20 million of KS&T's credit line at the issuing bank was accessed, and KS&T made use of the "full value" of that $20 million from the moment the letter of credit was issued—using it to margin its commodity trading activities through MFGI. Correspondingly, such value—$20 million—was reflected in KS&T's relevant account at MFGI as of the Filing Date. (*See* Alinikoff Decl., Ex J (KS&T Equity Run).) Upon expiration of the 30.7 LOC, KS&T's contingent liabilities were reduced by an amount equal to the full proceeds of the 30.7 LOC—$20 million. The Trustee demands that KS&T return those "full proceeds" to the estate for pro rata distribution among all former MFGI customers. *See* 48 Fed. Reg. 8716, 8717. Had the 30.7 LOC not expired, pursuant to Part 190.08, the Trustee could have sought to recover the $20 million assets from the issuing bank, which in turn would have recovered those assets directly from KS&T. Upon expiration, however, KS&T—as opposed to the issuing bank—is responsible for this customer property.[6]

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[6] In the alternative, the Trustee fully reserves the right to demand the full proceeds of the 30.7 LOC from the issuing bank as a draw on KS&T's line of credit to the extent that the Court holds that the estate's right to possession of the full proceeds of the 30.7 LOC, which must be drawn "irrespective of [its] terms," does not expire until the Trustee has made a final distribution of the estate's customer property to the former customers of MFGI. 48 Fed. Reg. 8716-01, 8718. This result is also consistent with the CFTC's goal of ensuring that "customers who posted letters of credit to meet original margin obligations [are] treated no differently than customers depositing other forms of non-cash margin or customers with excess cash margin deposits." *Id.*

(ii) KS&T's Defenses are in Contravention of the Plain Language of Part 190.08

58. The plain language of Part 190.08(a)(i)(1)(e) clearly requires that "the full proceeds of a letter of credit . . . received, acquired or held to margin" be included as customer property of the estate. This plain language is controlling "unless [it is] arbitrary, capricious, or manifestly contrary to the statute." *Chevron*, 467 U.S. at 844. That is clearly not the case here.

59. Because Congress explicitly directed the CFTC to "provide that certain cash, securities, other property, or open contractual commitments are to be included in or excluded from customer property," S. Rep. No. 95-989, 1978 WL 8531, at *159, Congress "expressly delegate[ed] . . . authority to the [CFTC] to elucidate a specific provision of the statute by regulation," *Chevron*, 467 U.S. at 843-44. Pursuant to that delegation, the CFTC concluded that within the context of a commodity broker liquidation and contrary to the treatment of letters of credit generally, the "full proceeds" of letters of credit posted as margin are customer property upon liquidation of a FCM. A post-petition expiration of the letter of credit is not tantamount, as KS&T suggests, to an expiration of those proceeds.

60. Moreover, the Part 190 Regulations' enacting commentary make clear that a letter of credit's full proceeds are "deemed" customer property upon liquidation of a FCM "irrespective of [the letter of credit's] terms even though they generally condition payment on delivery of a certification that additional funds are required to margin or to cover a default with respect to a contract." 48 Fed. Reg. 8716-01, 8718. This further confirms that neither the default provision of the 30.7 LOC nor its expiration can operate to limit the Trustee's right to possess its full proceeds and include it in the pro rata distribution of customer property.

(iii) KS&T's Defenses Contravene the Bankruptcy Code's and the Part 190 Regulations' Stated Purpose of Equal Customer Treatment

61. To allow KS&T to evade the pro rata distribution of customer property by virtue of the expiration of the 30.7 LOC would undermine the CFTC's stated objective of ensuring "that, in a commodity broker liquidation, customers who posted letters of credit to meet original margin obligations [are] treated no differently than customers who deposited other forms of non-cash margin." 48 Fed. Reg. 8716, 8717. KS&T's circumvention of the pro rata distribution scheme "would favor [KS&T] at the expense of smaller market participants since only larger customers [such as KS&T] are permitted to make non-cash deposits of margin" and such a result "contravene[s] the spirit and intent of the Code's limitations on the return of specifically identifiable property which were intended to assure parity between customers with margining power and those without it." *Id.*

C. KS&T's Retention of the Full Face Value of the 30.7 LOC Continues in Violation of the Automatic Stay

62. The commencement of a SIPA liquidation operates as a stay of, among other things, "any act to obtain possession of . . . or to exercise control over property of the estate." 11 U.S.C. § 362(a)(3); *see also* SIPA § 78fff(b) (applying chapter 3 of title 11); SIPA § 78fff-1(b) (applying chapter 7 of title 11); *SIPC v. Blinder Robinson & Co.*, 962 F.2d 960, 965 (10th Cir. 1992); *SIPC v. Bernard L. Madoff Inv. Sec. LLC*, 429 B.R. 423, 430 (Bankr. S.D.N.Y. 2010), *aff'd*, 848 F. Supp. 2d 469 (S.D.N.Y. 2012). The MFGI Liquidation Order similarly provides "that all persons and entities are notified that, subject to the other provisions of 11 U.S.C. § 362, the automatic stay provisions of 11 U.S.C. § 362(a) operate as a stay of: (E) any act to obtain possession of property of the estate or property from the estate." (Alinikoff Decl., Ex. A (MFGI Liquidation Order at III).) "Nothing is more basic to bankruptcy law than the automatic stay and nothing is more important to fair case administration than enforcing the stay

violation." *In re Lehman Brothers Holdings*, 433 B.R. 101, 112 (Bankr. S.D.N.Y. 2010), *aff'd*, 445 B.R. 130 (S.D.N.Y. 2011).

63. To enforce the automatic stay under § 362(a) of the Code, the debtor must "show what property of the estate is implicated and that some entity or individual is attempting to obtain possession or exercise control over such property." *In re Golden Distribs.*, 122 B.R. 15, 19 (Bankr. S.D.N.Y. 1990). Section 541 of the Bankruptcy Code defines "property of the estate" broadly to include "all legal or equitable interests of the debtor in property as of the commencement of the case," "wherever located and by whomever held." 11 U.S.C. § 541(a)(1) (2012); *see also In re Madoff*, 848 F. Supp. 2d 469, 478 (S.D.N.Y. 2012). Moreover, § 541's legislative history "will bring everything of value that the debtor has into the estate." *In re S.W. Bach*, 435 B.R. at 877 (internal quotations omitted).

64. As discussed *supra*, pursuant to Part 190.08, the full proceeds of the 30.7 LOC are property of the estate in which the Trustee had a "legal or equitable interest[] . . . as of the commencement of the case," 11 U.S.C. § 541(a)(1), and retention of those proceeds by any party other than the Trustee constitutes a violation of § 362(a)(3). The automatic stay provision prohibits attempts by former customers of MFGI from obtaining their money or property from the estate in advance of the Trustee's distribution of customer property; before such time, that property is the estate's, not the customers'. *Blinder*, 962 F.2d at 965 (finding that the automatic stay provisions of the Bankruptcy Code prevent individual customers "from taking virtually any action to collect debts owed to them or to recover their property held by the [liquidating] broker-dealer"); *see generally Lehman Brothers Holdings*, 433 B.R. at 108 ("creditor's refusal to pay amounts owed to a debtor constitutes a violation of the automatic stay"); *In re Lehman Brothers Inc.*, 458 B.R. 134, 144 (Bankr. S.D.N.Y. 2011) (parties' good faith legal dispute did not excuse

stay violation that occurred when creditor, without moving for relief from stay, exercised control over property of estate by retaining funds).

65. By retaining possession of the $20 million proceeds of the 30.7 LOC, KS&T is retaining customer property as "a means of avoiding the pro rata distribution of margin funds, contrary to the intent of the Code" and the Part 190 Regulations. 48 Fed. Reg. 8716-01, 8718.[7] Before KS&T has a right to possess those funds, they must first be returned to the estate, added to the pool of customer property, and then distributed on a pro rata basis to all of MFGI's former customers with allowed claims, as directed by § 766 of the Code and the Part 190 Regulations. *See Bucyrus*, 127 B.R. at 51-52.

66. Accordingly, the Trustee respectfully submits judgment in favor of the Trustee declaring that KS&T must immediately pay to MFGI the face value of the 30.7 LOC—$20 million, with interest—pursuant to the Trustee's powers under 17 C.F.R. 190 *et seq*. and § 362 of the Code, so that such property may be included in the pro rata distribution of customer property to former customers of MFGI.

CONCLUSION

67. For the foregoing reasons, the Trustee respectfully requests the Court grant summary judgment in his favor on the Trustee's counterclaim by entering a declaration that: (i) the face value of the 30.7 LOC constitutes customer property pursuant to 11 U.S.C. §§ 761-767 as supplemented by 17 C.F.R. §§ 190 *et seq.*; and (ii) KS&T must immediately pay to the Debtor the face value of the 30.7 LOC—$20 million, with interest—pursuant to the Trustee's powers under the Part 190 Regulations and 11 U.S.C. § 362, for inclusion in the pro

[7] The Trustee also submits that KS&T's retention of the customer property is equally subject to avoidance pursuant to 11 U.S.C § 764 by virtue of KS&T's receipt of $20 million in MFGI customer property in advance of the Trustee's pro rata distribution.

rata distribution of customer property to former customers of MFGI. The Trustee also respectfully requests that Court grant such other and further relief that the Court deems just and proper.

Dated: New York, New York
October 26, 2012

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