HUGHES HUBBARD & REED LLP
One Battery Park Plaza
New York, New York 10004
Telephone: (212) 837-6000
Facsimile: (212) 422-4726

Attorneys for James W. Giddens,
Trustee for the SIPA Liquidation of MF Global Inc.

**UNITED STATES DISTRICT COURT**
**SOUTHERN DISTRICT OF NEW YORK**

| | |
|---|---|
| In re<br><br>MF GLOBAL INC.,<br><br>Debtor. | Bankruptcy Case No. 11-2790 (MG)<br>SIPA |
| CONOCOPHILLIPS COMPANY, et al.,<br><br>Plaintiffs,<br><br>v.<br><br>JAMES W. GIDDENS, Trustee for the SIPA Liquidation of MF Global Inc.<br><br>Defendant. | Case No. 12-CV-6014 (KBF) |

**MEMORANDUM OF LAW IN SUPPORT OF THE TRUSTEE'S AMENDED MOTION FOR AN ORDER CONFIRMING THE TRUSTEE'S DETERMINATION OF CONOCOPHILLIPS' CLAIMS TO CUSTOMER ACCOUNTS MARGINED WITH LETTERS OF CREDIT**

# TABLE OF CONTENTS

**Page**

PRELIMINARY STATEMENT ....................1

BACKGROUND ....................2

A. MFGI And The Role Of Margin In The Futures Markets. ....................2

B. The Collapse And Liquidation Of MFGI And The Shortfall In Customer Property. ....................4

C. The Trustee's Determination Of The ConocoPhillips Claims. ....................6

ARGUMENT ....................7

I. THE BANKRUPTCY CODE AND GOVERNING CFTC REGULATIONS SUPPORT THE TRUSTEE'S DETERMINATION OF CONOCOPHILLIPS' CLAIMS. ....................7

A. The Bankruptcy Code And The CFTC Regulations Direct That The Full Amount Of Letters Of Credit Are Customer Property In A FCM Liquidation. ....................7

1. The Plain Language Of The Regulation Supports The Trustee's Determination. ....................9

2. The Regulation's Promulgation History Leaves No Doubt About Its Meaning. ....................10

B. The Expiration Or Return Of A Letter of Credit Is A Transfer Of Customer Property. ....................13

II. CONGRESS DID NOT IMPLIEDLY OVERRIDE 17 C.F.R. § 190.08(a)(1)(i)(E) WITH SUBSEQUENT UNRELATED LEGISLATION. ....................16

A. Congress Expressly Delegated To The CFTC The Power To Determine What Is Included And Excluded From Customer Property. ....................16

B. Congress' Later Amendment Of The Bankruptcy Code And The Commodity Exchange Act Shows That It Agreed With The CFTC's Treatment Of Letters Of Credit. ....................17

C. The Bank Products And Dodd-Frank Acts Do Not Affect 17 C.F.R. § 190.08(a)(1)(i)(E). ....................19

1. The Bank Products Act ....................19

2. The Dodd-Frank Act ....................22

III. THE FEDERAL LAWS GOVERNING A COMMODITY BROKER LIQUIDATION ARE CONTROLLING. ....................23

CONCLUSION ....................26



62115380_1

**TABLE OF AUTHORITIES**

**Page(s)**

**CASES**

Am. Land Title Ass'n v. Clarke,
968 F.2d 150 (2d Cir. 1992)....................21

Auer v. Robbins,
519 U.S. 452 (1997)....................12

Bevill, Bresler & Schulman, Inc.,
59 B.R. 353 (D.N.J. 1986), appeal dismissed, 802 F.2d 445 (3d Cir. 1986)....................25

Boeing Co. v. United States,
537 U.S. 437 (2003)....................17, 22

Cardiano v. Metacon Gun Club, Inc.,
575 F.3d 199 (2d Cir. 2009)....................21

CFTC v. Schor,
478 U.S. 833 (1986)....................17

Chase Bank USA, N.A. v. McCoy,
131 S. Ct. 871 (2011)....................9, 12

Chevron U.S.A. Inc. v. Natural Res. Def. Council,
467 U.S. 837 (1984)....................21

E. Equip. & Servs. Corp.,
236 F.3d 117 (2d Cir. 2001)....................24

FDIC v. Bank of Boulder,
865 F.2d 1134 (10th Cir. 1988), aff'd en banc, 911 F.2d 1466 (10th Cir. 1990)....................25

Fid. Fed. Sav. & Loan Ass'n v. de la Cuesta,
458 U.S. 141 (1982)....................24

Forest Grove Sch. Dist. v. T.A.,
557 U.S. 230 (2009)....................17, 23

Garcia-Villeda v. Mukasey,
531 F.3d 141 (2d Cir. 2008)....................10

Hibbs v. Winn,
542 U.S. 88 (2004)....................9

Int'l Shoe Co. v. Pinkus,
278 U.S. 261 (1929)....................24

## TABLE OF AUTHORITIES
(Continued)

**Page(s)**

Kruse v. Wells Fargo Home Mortg., Inc.,
383 F.3d 49 (2d Cir. 2004)....................21

In re Lehman Brothers Holdings Inc. (Swedbank v. Lehman Brothers Holdings Inc.),
445 B.R. 130 (S.D.N.Y. 2011)....................17

Long Island Care at Home, Ltd. v. Coke,
551 U.S. 158 (2007)....................13

Mayo Found. For Med. Educ. & Research v. United States,
131 S. Ct. 704 (2011)....................21

Mullins v. City of New York,
653 F.3d 104 (2d Cir. 2011)....................13

SEC v. Albert & Maguire Sec. Co.,
378 F.Supp. 906 (E.D. Pa. 1974)....................24

Sec. Investor Prot. Corp. v. Bernard L. Madoff Invs. Sec. LLC,
401 B.R. 629 (Bankr. S.D.N.Y. 2009), aff'd sub nom. Rosenman Family, LLC v. Picard, 420 B.R. 108 (S.D.N.Y. 2009), aff'd, 395 Fed. Appx. 766 (2d Cir. 2010)....................25

Talk Am., Inc. v. Mich. Bell Tel. Co.,
131 S. Ct. 2254 (2011)....................12, 21

TRW Inc. v. Andrews,
534 U.S. 19 (2001)....................9

Wachovia Bank, N.A. v. Burke,
414 F.3d 305 (2d Cir. 2005)....................23

**CONSTITUTIONAL PROVISIONS**

U.S. Const., art. I, § 8....................24

**STATUTES AND RULES**

7 U.S.C. § 1a....................22

7 U.S.C. § 24(a).................... passim

7 U.S.C. § 24(c)....................18

11 U.S.C. § 362....................15

11 U.S.C. §§ 761-767.................... passim

**TABLE OF AUTHORITIES**
(Continued)

**Page(s)**

15 U.S.C. § 78fff-1(b) ........ 5

Commodity Futures Modernization Act of 2000, Pub. L. No. 106-554, 114 Stat. 2763 (Dec. 21, 2000) ........ 17, 19

Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1684 (July 21, 2010) ........ 18, 22, 23

**REGULATIONS**

17 C.F.R. § 39.11(e)(3)(iii) ........ 19

17 C.F.R. § 39.13(g)(10) ........ 19

17 C.F.R. §§ 190.01 et seq. ........ passim

**LEGISLATIVE AND ADMINISTRATIVE MATERIALS**

146 Cong. Rec. 27077 (2000) ........ 20

146 Cong. Rec. 27078 (2000) ........ 20

146 Cong. Rec. 27237 (2000) ........ 20

S. Rep. No. 95-989 (1978), reprinted in 1978 U.S.C.C.A.N. 5787 ........ 16

46 Fed. Reg. 57,535 (Nov. 26, 1981) ........ 11

48 Fed. Reg. 8716 (Mar. 1, 1983) ........ 11, 12

**OTHER AUTHORITIES**

Barron's Dictionary of Finance & Investment Terms (8th ed. 2010) ........ 3

James W. Giddens (the "Trustee"), as Trustee for the liquidation of MF Global Inc. ("MFGI") under the Securities Investor Protection Act ("SIPA"), by and through his undersigned counsel, respectfully submits this memorandum of law in support of the Trustee's Amended Motion for an Order Confirming the Trustee's Determination of the ConocoPhillips Company and ConocoPhillips Canada Marketing & Trading ULC (together, "ConocoPhillips") Claims to Customer Accounts Margined with Letters of Credit and states as follows:

## PRELIMINARY STATEMENT

There is a shortfall in customer property in the MFGI liquidation. This means that former MFGI customers are recovering less than 100 percent of their property, including margin that they posted with MFGI pre-liquidation. The ConocoPhillips companies seek different treatment simply because they were among a small handful of customers that posted margin in the form of letters of credit ("LOCs"). But the law does not permit such preferential treatment.

The Bankruptcy Code itself, in 11 U.S.C. § 766(h), directs that distributions are to be made to customers "ratably"; that means that if there is a shortfall, all customers must share the burden. The Commodity Futures Trading Commission ("CFTC") – the federal agency that Congress empowered to promulgate the rules governing commodity broker liquidations – promulgated a regulation to ensure that this principle applied specifically to LOCs. The Trustee's determination of ConocoPhillips' claims follows this regulation and results in the equitable treatment of all of MFGI's former customers.

Application of well-accepted principles of statutory and regulatory construction leaves no question that 17 C.F.R. § 190.08(a)(1)(i)(E) instructs the Trustee to consider the total amount of the ConocoPhillips LOCs as customer property. Any other reading of the regulation is contrary to the CFTC's own contemporaneous and current interpretation. And once the full

amount of the LOCs are customer property, the only equitable result is that the expiration or return of a LOC to the party posting it is a distribution of customer property to that customer.

ConocoPhillips has sought to overcome the only valid reading of the regulation by arguing that: (i) Congress impliedly overrode the CFTC regulation in later, unrelated legislation without any mention of that intent; and (ii) the CFTC exceeded its authority in enacting a bankruptcy regulation that conflicted with state law. A careful reading of the relevant statutes and their legislative history shows that these arguments are incorrect.

The issue of whether ConocoPhillips, or any customer that is able to post LOCs as margin, can circumvent the normal pro rata distribution of customer property is an important one. In this liquidation, if ConocoPhillips were to prevail, the $205 million in LOCs it posted instead of cash to margin its trading would not pass through the pro rata distribution process at all. This would mean that ConocoPhillips would receive more than its fair share of property, and the recovery prospects for all other MFGI customer-claimants – over 27,000 of them – would remain uncertain. Such inequitable treatment would be the opposite of what Congress and the regulator intended.

## BACKGROUND

### A. MFGI And The Role Of Margin In The Futures Markets.

MFGI was a futures commission merchant ("FCM") subject to regulation by the CFTC and a registered securities broker-dealer subject to SIPA. (Report of the Trustee's Investigation and Recommendations at 26, 31-32, attached in part to the Declaration of Marlena C. Frantzides sworn to on October 26, 2012 (the "Second Frantzides Decl.") at Ex. A.) As a FCM, MFGI executed buy and sell orders for commodities futures contracts on behalf of tens of thousands of customers. The ConocoPhillips entities were two of those customers.

Commodities futures contracts are standardized agreements for the purchase or sale of a commodity for delivery in the future at a predetermined price. Barron's Dictionary of Finance & Investment Terms 128 (8th ed. 2010). For example, a FCM customer can buy (through its FCM as agent at clearinghouses), 5,000 bushels of corn for delivery in March 2013 at $3.00 per bushel. Every day, the clearinghouse marks every contract to market, collecting losses and paying gains based on the changes in market prices. To ensure that FCMs and their customers will perform the obligations associated with their futures positions, clearinghouses require that FCMs, on behalf of their customers, post initial margin, also known as performance bond. FCMs in turn look to and require their individual customers to post initial margin. As regulated by the CFTC, the clearinghouses permit different forms of property as initial margin: cash, Treasury bills and notes, securities, and, most relevant here, LOCs. Regardless of the form, MFGI was permitted to access the margin pursuant to its customer contracts only in the event of a "default" by the customer. (See Customer Agreements, Second Frantzides Decl. at Exs. B at ¶ 5 and C at ¶ 4.)

A default occurs when a customer fails to meet its margin obligations. For example, when the FCM customer places a buy order for the March 2013 corn futures, the initial margin on the trade is based on a clearinghouse-determined amount that relates to the volatility of the underlying product. If the price of March 2013 corn futures increases, no margin call will occur, but if the price of March 2013 corn futures decreases, the customer could become under-margined, resulting in a margin call. If the customer deposits the required additional margin, no further action is taken. If, however, the customer fails to deposit the necessary additional margin, the FCM could declare the customer in default, at which point the FCM is permitted to liquidate the customer's position (i.e., sell the March 2013 corn). If in liquidating the position

the FCM incurs a loss, the FCM is contractually permitted to access the customer's margin to make itself whole. This could entail taking cash from the customer's account, selling a security or Treasury instrument, or drawing down on a LOC.

Customers' periodic account statements from the FCM reflect the amount of margin posted with a FCM by the customer. Cash receives its full value in the margin calculation. Treasury bills, Treasury notes, and securities are not given dollar-for-dollar value as margin but instead are booked at lower amounts to cover the risk that their liquidation value could be less. Like cash, LOCs are given their full face value as margin, reflecting the market assumption that the LOC is as good as cash and not at risk of being unavailable in its full amount. (See ConocoPhillips' Account Statements, attached in part to Second Frantzides Decl. at Exs. D and E.) That is, a customer that posts a $10 million LOC as margin with a FCM will have the same available margin as a customer that posts $10 million in cash. If a LOC expires, the customer would be required to post new margin to remedy the deficit. (See CME Group Clearing House Manual of Operations (December 2010) 158, Second Frantzides Decl. at Ex. F.)

**B. The Collapse And Liquidation Of MFGI And The Shortfall In Customer Property.**

Early in the morning of October 31, 2011 (the "Filing Date"), federal regulators became aware of significant compliance failures by MFGI. That afternoon, the Honorable Paul A. Engelmayer of the Southern District of New York entered an order commencing the liquidation of MFGI pursuant to the provisions of SIPA and appointing James W. Giddens as Trustee. (See Second Frantzides Decl. at Ex. G.) As a FCM and securities broker-dealer, MFGI is being liquidated pursuant to both SIPA and the Bankruptcy Code provisions enacted by Congress specifically to govern FCM liquidations (subchapter IV of chapter 7 of title 11, or 11

U.S.C. §§ 761-767), as well as the CFTC regulations promulgated to implement subchapter IV: 17 C.F.R. §§ 190.01 through 190.10 (the "Part 190 Regulations").[1]

Among the Trustee's most important duties in a FCM liquidation are marshaling and distributing the property of the former FCM customers. 15 U.S.C. § 78fff-1(b). The failed FCM's former customers are entitled to priority distributions before any other creditor claims are satisfied. See 11 U.S.C. § 766(h). To accomplish this, the Part 190 Regulations create separate pools of customer property from which all customers share ratably by account class, and these pools of customer property are distinct from the general estate. (See Brief of the CFTC Pursuant to the Court's November 17, 2011 Order 5-9, Second Frantzides Decl. at Ex. H.)

In the case of MFGI, there is a substantial shortfall in the two primary classes of customer property: one related to commodity futures trading on domestic exchanges ("4d Property") and one related to commodity futures trading on foreign exchanges ("30.7 Property"). To date, the Trustee has been able to return 4d Property at a rate of 80 cents on the dollar, while 30.7 Property has been returned at a rate of 5 cents on the dollar. (See Seventh Interim Status Report on Claims ¶ 13, Frantzides Decl. at Ex. I.)

The Bankruptcy Code and the Part 190 Regulations both demand that any shortfall of customer property be shared ratably by all customers in a given account class. 11 U.S.C. § 766(h); 17 C.F.R. § 190.01(n). As applied in the MFGI liquidation, if a former MFGI customer had $1 million in cash posted as margin for 4d trading and no open positions – i.e., a $1 million net equity – the Trustee has distributed 80 percent of that, or $800,000. Prior to MFGI's liquidation, MFGI would not have had the contractual right to access the $1 million in

1. The applicable Part 190 Regulations are those that were in effect as of October 31, 2011. They have been subsequently amended.

cash because the customer was not in default. But upon MFGI's liquidation, the $1 million is customer property subject to pro rata distribution for all customer-claimants. For customers that had posted margin in the form of non-cash collateral and wanted it returned to them rather than liquidated, the Trustee, where possible, permitted the customer to make a payment in exchange for the asset to keep the distribution level at 80 percent.

For example, the Trustee reached this arrangement with GFX Corporation ("GFX") regarding the LOC it had posted with MFGI to support its commodity futures trading. Specifically, to secure the return of the $20 million LOC GFX had posted as margin – the only asset in GFX's account except for a small debit – GFX wired 20 percent of its accounts' net liquidating value to the Trustee, and the Trustee returned the undrawn LOC to GFX. (See Limited Agreement and Reservation of Rights Between CME Group Inc. and James W. Giddens, Recitals ¶ I; Section 3.4, Second Frantzides Decl. at Ex. J.)

### C. The Trustee's Determination Of The ConocoPhillips Claims.

On May 22, 2012, the Trustee allowed ConocoPhillips' December 16, 2011 claims as customer claims, including in his determinations the customer net equity for each account class as directed by the Part 190 Regulations.[2] ConocoPhillips Company's net equity includes: (i) $135 million in 4d LOCs and $40,790,952 in other 4d Property; and (ii) $60 million in 30.7 LOCs and $25,755,528 in other 30.7 Property. ConocoPhillips Canada's net equity includes: (i) $1,546,818 in 4d Property, 72 percent of which has been returned; and (ii) $10 million in 30.7 LOCs and $24,866,553 in other 30.7 Property. The determination notices also

---

2. The specifics regarding ConocoPhillips' LOCs have been described in prior briefing and noted in the Court's order withdrawing the reference, so they are not repeated here. (Trustee's Bankruptcy Court Motion for an Order Confirming the Trustee's Determination of ConocoPhillips' Claims to Customer Accounts Margined with Letters of Credit (the "Trustee's Motion") at ¶¶ 16 – 25, Second Frantzides Decl. at Ex. K.)

record the transfers of customer property that have occurred since the Filing Date stating that "the face value of the LOCs posted by you with MFGI as margin for futures activity on foreign and domestic exchanges that either expired or were returned to you after the Filing Date is included in the amount already transferred to you." (See Notices of Trustee's Determination of Claims, Second Frantzides Decl. at Exs. L and M.).

ConocoPhillips has objected to the Trustee's determination. (Opposition of ConocoPhillips Company and ConocoPhillips Canada to the Trustee's Determination of Claims (the "Objection"), Second Frantzides Decl. at Ex. N.) In this motion, the Trustee seeks the Court's confirmation that his determination of ConocoPhillips' claims is correct.

## ARGUMENT

### I. THE BANKRUPTCY CODE AND GOVERNING CFTC REGULATIONS SUPPORT THE TRUSTEE'S DETERMINATION OF CONOCOPHILLIPS' CLAIMS.

In performing his statutory obligation to determine ConocoPhillips' customer claims in the MFGI liquidation, the Trustee made two determinations that: (i) the full amounts reflected in the ConocoPhillips LOCs are customer property, and (ii) the expiration or return of the LOCs is a transfer of customer property. The LOCs represent the value of ConocoPhillips' margin obligations on the Filing Date, and after the Filing Date that value must remain available for ratable distribution in accordance with the Bankruptcy Code provisions and the CFTC regulations that implement them.

#### A. The Bankruptcy Code And The CFTC Regulations Direct That The Full Amount Of Letters Of Credit Are Customer Property In A FCM Liquidation.

In 1978, Congress passed the Bankruptcy Reform Act, which, among other things, created a subchapter of the Bankruptcy Code specifically designed to govern the liquidation of a FCM like MFGI. In enacting this subchapter, Congress also made clear that the



62115380_1

Code itself was a "framework," and that the CFTC was to promulgate the rules to implement the Code provisions. The congressional framework provides that: (i) customer property includes "property received, acquired, or held to margin, guarantee, secure, purchase or sell a commodity contract"; and (ii) "the trustee shall distribute customer property ratably to customers on the basis and to the extent of such customer's net equity claims . . . ." 11 U.S.C. §§ 761(10); 766(h). Congress also specifically granted the CFTC the authority to determine what is and what is not customer property in a FCM liquidation:

> Notwithstanding Title 11, the [CFTC] may 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 in or excluded from customer property . . . .

7 U.S.C. § 24(a)(1) (emphasis added).

The CFTC exercised this authority in 17 C.F.R. § 190.08, and it addressed LOCs specifically:

> Customer property includes . . . [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 . . . .

17 C.F.R. § 190.08(a)(1)(i)(E) (the "LOC Provision"). There is no dispute here that the ConocoPhillips LOCs were exactly the type of margin that falls within this regulation. (Second Frantzides Decl. at Ex. N, p.3 (ConocoPhillips "provided [its LOCs] as collateral to support commodity contract trading"); Letter of Dec. 9 2011 from Mark C. Ellenberg, Esq., Second Frantzides Decl. at Ex. O (ConocoPhillips "posted the letters of credit as performance bonds"); Letter of Dec. 29, 2011 from Herbert M. Wachtell, Esq., Second Frantzides Decl. at Ex. P (ConocoPhillips "bargained to provide [LOCs] as collateral and not cash.").)

The only question of regulatory interpretation is whether "full proceeds" means (i) as the Trustee contends, the full face amount of the LOCs, or (ii) as ConocoPhillips contends, only that portion of the LOCs that MFGI would have been entitled to draw upon pre-liquidation to remedy a default by ConocoPhillips if ConocoPhillips had defaulted (which it did not). Under ConocoPhillips' proposed reading, the "full proceeds" of the LOCs is zero. The Bankruptcy Code's demand for ratable distribution; the regulation implementing the Code, and the CFTC itself all support the Trustee's position.

**1. The Plain Language Of The Regulation Supports The Trustee's Determination.**

The analysis of a regulation begins with its plain language. Chase Bank USA, N.A. v. McCoy, 131 S. Ct. 871, 878 (2011). The only proper reading of "full proceeds of a letter of credit" is the one proposed by the Trustee. Each word of a regulation must be given meaning. See TRW Inc. v. Andrews, 534 U.S. 19, 31 (2001) ("[N]o clause, sentence, or word shall be superfluous, void, or insignificant."). Accordingly, the word "full" in "full proceeds" cannot be ignored. Hibbs v. Winn, 542 U.S. 88, 101 (2004). The word "full" is far more compatible with the Trustee's reading – the total amount of the LOCs – than it is with ConocoPhillips' reading, which here would result in "full proceeds" meaning "no proceeds."

In fact, ConocoPhillips' proposed reading, that customer property only includes the portion of the LOCs that could have been drawn to remedy a default, would turn the definition of customer property on its head. For a default to occur, ConocoPhillips would have had to fail to meet a margin call. MFGI then could have declared a default, liquidating ConocoPhillips' commodities futures positions, and if it suffered a loss doing so, accessing ConocoPhillips' margin to make itself whole. So here the only way that MFGI would have

drawn on the LOC would have been if MFGI needed to do so to cover a loss that it had itself incurred on ConocoPhillips' behalf.

Thus "full proceeds" cannot mean that the proceeds of the LOC are customer property only to the extent they could have been accessed to cure a default. The portions of the LOC that were needed to cure a default by definition would not have been ConocoPhillips' property but rather would have been property that MFGI used to make itself whole. The same would hold true for any asset held as margin for any customer: if a customer that posted a Treasury bill had defaulted so that MFGI had to liquidate its position and then sell the Treasury bill, using a portion of the proceeds to make itself whole, those proceeds would no longer be included as customer property. Reading the regulation in ConocoPhillips' way would make all LOCs phantom customer property once a liquidation occurs, contradicting the statutory directive of ratable distribution and creating a disparity based on the forms of property used as margin. This is not an acceptable outcome in statutory interpretation. Garcia-Villeda v. Mukasey, 531 F.3d 141, 147 (2d Cir. 2008).

**2. The Regulation's Promulgation History Leaves No Doubt About Its Meaning.**

Even without the Supplementary Information, the Trustee's reading of the regulation is the proper one and the full amount of the ConocoPhillips LOCs should be considered customer property. However, to the extent the Court finds the plain language of the regulation to be ambiguous, the regulation's promulgation history – recorded in the Supplementary Information issued contemporaneously by the CFTC – removes any doubt about the regulation's proper interpretation.

The Supplementary Information contains a section (section 4 of the "Discussion of Major Substantive Issues") that specifically discusses the inclusion of the full proceeds of LOCs in customer property. This section makes clear that "full proceeds" means "full value":

> Section 190.08(a)(1)(i)(E) of the proposed regulations required that the full proceeds of a letter of credit received, acquired, or held by the debtor to margin, guarantee, or secure a commodity contract be deemed customer property. Under this approach, the trustee would be required to draw the full value of a letter of credit posted as margin and treat the funds received as customer property, irrespective of the margin obligation secured thereby.

48 Fed. Reg. 8716, 8718 (Mar. 1, 1983) (emphasis added). The CFTC originally proposed this regulation in November 1981, and then, by granting multiple extensions, permitted public comment on the proposed regulation through May 1982. 46 Fed. Reg. 57,535 (Nov. 26, 1981). As the CFTC wrote in the Supplementary Information, some commentators proposed that the CFTC amend its proposed regulation to say what ConocoPhillips would like it to say:

> Several of the commentators requested that the Commission amend its proposal to provide 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. This is necessary, the commentators argued, 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. These commentators further noted that 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.

48 Fed. Reg. 8716, 8718 (Mar. 1, 1983).

Thus, even before the regulation's final adoption, commentators sought to change the regulation to ConocoPhillips' proposed reading during an extended notice and comment period. This gave the CFTC the opportunity to consider the exact position that ConocoPhillips

advances here prior to the promulgation of the final regulations, and, as the CFTC said at the time: "The Commission . . . is not persuaded by this argument." Id.

The CFTC spelled out in the Supplementary Information, several important considerations in support of its rejection of the position advanced by ConocoPhillips:

- "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 [Bankruptcy] Code [citing 11 U.S.C. § 766];

- "it would be inherently unfair to treat letters of credit differently from other financial instruments such as Treasury Bills [sic] which have been deposited with commodity brokers as original margin"; and

- "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 [Bankruptcy] 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.

As a federal agency interpreting its own regulations, the CFTC is entitled to substantial deference. As the Supreme Court has repeatedly held "we defer to an agency's interpretation of its regulations, even in a legal brief, unless the interpretation is plainly erroneous or inconsistent with the regulations or there is any other reason to suspect that the interpretation does not reflect the agency's fair and considered judgment on the matter in question." Talk Am., Inc. v. Mich. Bell Tel. Co., 131 S. Ct. 2254, 2261 (2011); see also Chase Bank USA, N.A., 131 S. Ct. at 880; Auer v. Robbins, 519 U.S. 452, 461 (1997). The Second Circuit has explained that "[a] court's role in this circumstance is circumscribed. It is without authority to substitute its own independent interpretation of an agency's regulations for that of

the agency." See Mullins v. City of New York, 653 F.3d 104, 114 (2d Cir. 2011); see also Long Island Care at Home, Ltd. v. Coke, 551 U.S. 158, 171 (2007).

The CFTC's contemporaneous interpretation of its own regulation is not "plainly erroneous." Moreover, there is no reason here to believe that the interpretation reflects anything other than the agency's fair and considered judgment of the matter. The CFTC gave extensive time for public comment, considered from public commentators the exact position that ConocoPhillips puts forth today, sought advice from multiple sources on the best path forward, and then rejected the ConocoPhillips position with sound policy considerations. Under these circumstances, Supreme Court precedent and the law of this Circuit hold that an interpretation contrary to the CFTC's is improper.

### B. The Expiration Or Return Of A Letter of Credit Is A Transfer Of Customer Property.

The prior section demonstrates that the full value of the ConocoPhillips LOCs are customer property. For the LOCs that were unexpired at the time of the parties' interim agreement, this should end the inquiry. (See Interim Agreement, Second Frantzides Decl. at Ex. Q.) But for the LOCs that expired after the liquidation but before the parties had addressed them, ConocoPhillips raises another argument, namely: the full proceeds of the LOCs stopped being customer property upon their expiration. This argument is incorrect because (i) it frustrates the clear intent of the Part 190 Regulations, and (ii) it evades the mandate for "ratable" distribution in the Bankruptcy Code.

While MFGI was operational, the full value of the ConocoPhillips LOCs was used by ConocoPhillips to satisfy its margin obligations to MFGI. As soon as the MFGI liquidation commenced, the Part 190 Regulations fixed that same full value as customer property. As discussed in the prior section, the CFTC was clear about its intentions: it sought to

ensure equal treatment for large customers that could post LOCs as margin and for small customers that could not, and to achieve this goal, it exercised the authority given to it by Congress to make the full value of the LOCs customer property. ConocoPhillips' argument – that the post-liquidation expiration of LOCs pulls their full value out of the pool of customer property – would frustrate the CFTC's intent. Any customer fortunate enough to have its LOCs expire before the Trustee acted would receive back all of its margin – a windfall that customers that posted cash, Treasury notes, or securities could never receive.

ConocoPhillips' argument would also give this select class of customers a way around the Bankruptcy Code's demand for "ratable" distribution. 11 U.S.C. § 766(h). Under ConocoPhillips' theory the expiration of a LOC is not "ratable" – a customer with an expiring LOC would get its margin back at 100 cents on the dollar, while others in its account class could receive far less.

But the expiration of a LOC is a distribution to the customer that posted it. This is because of the way in which LOCs work: they shift the liquidity of the customer property to the issuing bank. For margin in the form of cash, the liquidity source is the bank account holding the cash. For margin in the form of securities, it is the Trustee's broker that liquidated the securities on the open market. For LOCs, the liquidity starts with the issuing bank but then makes its way immediately to ConocoPhillips: if there is a draw on a ConocoPhillips LOC, its banks look directly to ConocoPhillips for payment. ConocoPhillips' obligation to the bank for the full amount of the LOC is the functional equivalent of the property posted by other claimants in the form of cash or Treasury bills. When the Trustee returned to ConocoPhillips its unexpired LOCs pursuant to the interim agreement, he did more than just return pieces of paper: he eliminated

the possibility that ConocoPhillips would ever have to be the ultimate liquidity source for the customer property represented by the LOCs. This is a distribution to ConocoPhillips.

The analysis is no different for the LOCs that expired before the Trustee and ConocoPhillips reached an interim agreement. The day before the expiration of the LOCs, the full value was customer property, and ConocoPhillips had obligations to the issuing banks if the Trustee drew on them; the day after expiration, ConocoPhillips' obligation to the bank was reduced to zero, benefiting ConocoPhillips just as if it had received a return of cash. ConocoPhillips itself recognized the benefit of receiving back its LOCs, demanding their return from the Trustee in December of 2011. (See Second Frantzides Decl. at Exs. O and P.) ConocoPhillips did not send this demand letter until after LOCs valued at $60 million had already expired and did not inform the Trustee of those LOCs' existence. The reality of what occurred at expiration is that the liquidity obligation to the MFGI estate shifted: the banks were no longer responsible for this customer property (with a ConocoPhillips backstop); rather, ConocoPhillips was (and is) responsible for this customer property.[3]

* * *

The regulations, the promulgation history of the regulations, and the equitable purposes of the Bankruptcy Code all compel the same result: customers who post their margin as LOCs should be treated exactly the same in the face of a shortfall of customer property as customers who posted cash, securities, Treasury bills, or any other asset. The full proceeds of the LOCs are customer property as of the Filing Date and a LOC expiration does not change

3. While ConocoPhillips and the Trustee agreed to address their dispute in an orderly fashion in the interim agreement, a customer that simply benefited from an expired LOC and refused the Trustee's demand to return the customer property would be in violation of the automatic stay and subject to avoidance actions. 11 U.S.C. §§ 362, 764.

that. The Trustee's inclusion of the LOCs in ConocoPhillips' net equity, as well as his determination that their return or expiration was a distribution, was correct and should be confirmed.

## II. CONGRESS DID NOT IMPLIEDLY OVERRIDE 17 C.F.R. § 190.08(a)(1)(i)(E) WITH SUBSEQUENT UNRELATED LEGISLATION.

To avoid the impact of the Part 190 Regulations, ConocoPhillips argues that it should prevail because the LOC Provision was impliedly overridden by Congress with the Legal Certainty for Bank Products Act ("Bank Products Act") and the Dodd-Frank Wall Street Reform and Customer Protection Act ("Dodd-Frank Act"). In fact, these later statutes have nothing whatsoever to do with the CFTC's rule-making authority in FCM liquidations.

### A. Congress Expressly Delegated To The CFTC The Power To Determine What Is Included And Excluded From Customer Property.

Aware of the "unique problems" involved in a commodity broker liquidation, Congress created a special subchapter of the Bankruptcy Code for them. S. Rep. No. 95-989, at 7 (1978), reprinted in 1978 U.S.C.C.A.N. 5787, 5793. As Congress stated at the time, the new Bankruptcy Code provisions "provide . . . a framework," but not "detailed rules." Id. at 5794. "Instead general rulemaking authority has been delegated to the CFTC . . . ." Id.

Congress explicitly included within this rulemaking authority the issue that governs the Trustee's determination of ConocoPhillips' claim: what is and is not customer property in a commodity broker liquidation. 7 U.S.C. § 24(a)(1); see also section I.A. supra. This authority includes the authority to promulgate rules governing the treatment of many kinds of property – cash, securities, Treasury bills, and LOCs – that are otherwise outside of the CFTC's traditional "regulatory" purview. The rules that the CFTC promulgated pursuant to Congress' direction do not implicate the regulation of the items considered customer property

themselves, only how each must be treated in a FCM liquidation to assure ratable distribution to customers. ConocoPhillips' position – that over two decades later Congress withdrew part of the CFTC's authority to create these liquidation rules, despite the fact that it made no mention of any intention to do so – is incorrect. See In re Lehman Brothers Holdings Inc. (Swedbank v. Lehman Brothers Holdings Inc.), 445 B.R. 130, 136-37 (S.D.N.Y. 2011) (reasoning that Congress did not overturn a long standing bankruptcy principle in a later enacted statutory provision where "there is no mention in the legislative history that the Safe Harbor Provisions were intended to eliminate the mutuality requirement").

### B. Congress' Later Amendment Of The Bankruptcy Code And The Commodity Exchange Act Shows That It Agreed With The CFTC's Treatment Of Letters Of Credit.

It is well-accepted that "Congress is presumed to be aware of an administrative or judicial interpretation of a statute and to adopt that interpretation when it re-enacts a statute without change." Forest Grove Sch. Dist. v. T.A., 557 U.S. 230, 239-40 (2009). Where Congress declines to override a regulation, despite having the opportunity to do so, that "serves as persuasive evidence that Congress regarded that regulation as a correct implementation of its intent." Boeing Co. v. United States, 537 U.S. 437, 457 (2003); see also CFTC v. Schor, 478 U.S. 833, 846 (1986) ("[T]he congressional failure to revise or repeal the agency's interpretation is persuasive evidence that the interpretation is the one intended by Congress."). Here, Congress has amended subchapter IV of the Bankruptcy Code – the section of the Code implemented by the Part 190 Regulations at issue here – numerous times since 1978, and not once has it

suggested that it has any disagreement with the CFTC's treatment of LOCs as customer property.[4]

Congress has also amended its specific statutory grant of authority to the CFTC to promulgate the Part 190 Regulations (section 24 of the Commodity Exchange Act); indeed, it did so as part of the very Dodd-Frank Act that ConocoPhillips highlights. But in making this amendment, Congress did nothing to limit the CFTC's authority to promulgate customer property definitions (or any other Part 190 Regulations), nor did it indicate that it disagreed with any of the definitions that the CFTC had already promulgated. Instead, Congress increased the CFTC's rulemaking authority to broaden the customer property definition by exercising "its authority to ensure that securities held in a portfolio margining account carried as a futures account are customer property . . . ." 7 U.S.C. § 24(c). If Congress had any issue with the CFTC's customer property definition, including its treatment of LOCs, one of the multiple amendments to subchapter IV of the Bankruptcy Code, or the amendment to the statutory section that authorized the promulgation of the regulation itself would have been the place to say so. Congress did not say so.

---

4. Act of Jul. 27, 1982, Pub. L. No. 97-222, §§ 16-19, 96 Stat. 238 (July 27, 1982) (amending §§ 761, 764-66); Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, Title III, Subtitle H, §§ 485-89, 98 Stat. 383 (July 10, 1984) (amending §§ 761, 763-66); Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, Title V, § 501(d)(29), 108 Stat. 4146 (Oct. 22, 1994) (amending § 761); Commodity Futures Modernization Act of 2000, Pub. L. No. 106-554, § 1(a)(5), 114 Stat. 2763 (Dec. 21, 2000) (amending § 761); Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, Title IX, § 907(a)(3), (l), § 1502(a)(4), 119 Stat. 174 (April 20, 2005) (amending §§ 761 and 766 and adding § 767); Statutory Time-Periods Technical Amendments Act of 2009, Pub. L. No. 111-16, § 2(9), 123 Stat. 1607 (May 7, 2009) (amending § 764); Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, Title VII, Subtitle A, Part II, § 724(b), 124 Stat. 1684 (July 21, 2010) (amending § 761).

### C. The Bank Products And Dodd-Frank Acts Do Not Affect 17 C.F.R. § 190.08(a)(1)(i)(E).

The federal statutes relied upon by ConocoPhillips – the Bank Products and Dodd-Frank Acts – do not suggest any intent by Congress to override the CFTC's treatment of LOCs in a FCM liquidation. Indeed, a careful reading of the statutes leads to an inference of congressional support.

#### 1. The Bank Products Act

The Bank Products Act was enacted by Congress as title IV of the Commodity Futures Modernization Act of 2000 ("CFMA") and then amended by the Dodd-Frank Act in 2010. It provides as follows:

> No provision of the Commodity Exchange Act shall apply to, and the [CFTC] shall not exercise regulatory authority with respect to, an identified banking product if -
>
> (1) an appropriate banking agency certifies that the product has been commonly offered, entered into, or provided in the United States by any bank on or before December 5, 2000, under applicable banking law; and
>
> (2) the product was not prohibited by the Commodity Exchange Act and not regulated by the [CFTC] as a contract of sale of a commodity for future delivery (or an option on such a contract) or an option on a commodity, on or before December 5, 2000.

CFMA, Pub. L. No. 106-554, Title IV, § 403, 114 Stat. 2763 (Dec. 21, 2000) (amended 2010). "Identified banking products" are defined in a separate act and include numerous well-known banking products such as deposit accounts, savings accounts, debit accounts, CDs, loans, and LOCs.

Congress could not have meant by this to exclude entirely LOCs from any CFTC regulation. For example, CFTC regulations govern when LOCs are permissible margin for commodity customer accounts even outside of liquidation. 17 C.F.R. § 39.13(g)(10); 17 C.F.R. § 39.11(e)(3)(iii). In the liquidation context, Congress instructed the CFTC to determine what is

and what is not customer property. 7 U.S.C. § 24(a); 11 U.S.C. § 761(10)(A)(i). This includes the authority to address how LOCs should be treated. It would be illogical to give the CFTC the authority to determine whether cash, securities, Treasury instruments (and other assets that it does not regulate in the ordinary course) are or are not customer property, but to take no position on how LOCs should be treated in a FCM liquidation.

Recognizing this, ConocoPhillips might argue that the CFTC is permitted to promulgate regulations governing the treatment of LOCs in liquidation, but that the regulations may only treat LOCs exactly as they would be treated under state law; that is, any different treatment would constitute the exercise of "regulatory authority." But this too would be inconsistent with the CFTC's congressional charge. The CFTC was given authority by Congress to include or exclude all manner of assets from customer property, regardless of whether the CFTC had "regulatory authority" over those assets and without any state law restrictions.

At the very least, it is ambiguous what the phrase "regulatory authority" means in this statute, and this ambiguity requires analysis of (i) the legislative history, and (ii) the CFTC's own interpretation. Both support the proposition that the Bank Products Act was not meant to affect the CFTC's rulemaking authority concerning customer property in a FCM liquidation in any way.

First, the legislative history: the Bank Products Act was enacted as part of the CFMA, which had as its fundamental purposes "to modernize the regulation of our futures markets, to provide legal certainty for over-the-counter derivatives markets, and to authorize the trading of security products . . . ." 146 Cong. Rec. 27077 (2000). The Bank Products Act itself was intended "to clarify what is already the current state of the law that the CFTC does not regulate the traditional array of products that banks have been offering for years" and to ensure

that banking products are "not regulated as futures contracts." 146 Cong. Rec. 27078 (2000); 146 Cong. Rec. 27237 (2000) (emphasis added). This legislative history is important for two reasons. First, that the Bank Products Act was intended to clarify the current state of the law, which had included the CFTC's Part 190 Regulation for almost two decades, supports a conclusion that Congress had no (silent) intention of altering the CFTC's treatment of LOCs in a liquidation. Second, the legislative history sheds some meaning on the phrase "regulatory authority": it means that the bank products were not to be "regulated as futures contracts." When the CFTC regulates futures contracts, it does so pervasively and with a series of regulations that fill a book; the Bank Products Act was clarifying the existing state of the law that this set of pervasive regulations was never meant to apply to traditional bank products like savings accounts or LOCs. This is not what the CFTC was doing when it followed Congress' explicit direction to make determinations about what to include in or exclude from customer property.

Second, the CFTC's interpretation: both the Bank Products Act and the statutory provision that gave the CFTC the authority to promulgate the Part 190 Regulations are part of the Commodity Exchange Act, the same Act that created the CFTC. Federal agencies are accorded deference in their interpretation of the statutes that they are empowered to implement. See Chevron U.S.A. Inc. v. Natural Res. Def. Council, 467 U.S. 837, 843 (1984); Mayo Found. For Med. Educ. & Research v. United States, 131 S. Ct. 704, 714 (2011); Kruse v. Wells Fargo Home Mortg., Inc., 383 F.3d 49, 59-61 (2d Cir. 2004); Am. Land Title Ass'n v. Clarke, 968 F.2d 150, 155 (2d Cir. 1992). And the CFTC's interpretation is that the Bank Products Act did not limit the authority given to it by Congress in the Bankruptcy Reform Act. This is supported by the fact that the CFTC did not amend the LOC Provision when the Bank Products Act was

enacted in 2000 and that the CFTC reiterates its interpretation in legal briefing here. See Talk Am., Inc., 131 S. Ct. at 2261; see also Cardiano v. Metacon Gun Club, Inc., 575 F.3d 199, 207-08 (2d Cir. 2009). Further, Congress has never disagreed with that interpretation, despite having ample opportunity to do so when it amended the Bank Products Act in 2010 as part of the Dodd-Frank Act. See Boeing, 537 U.S. at 457.

Finally, the CFMA, of which the Bank Products Act was a part, also amended the specific subchapter of the Bankruptcy Code that deals with FCM liquidations – the very subchapter implemented by the Part 190 Regulations. These amendments redefined several terms in section 761 of the Bankruptcy Code. But what the amendments did not do was change in any way the definition of customer property in Section 761(h) of the Bankruptcy Code. If Congress disagreed with the CFTC's definition of customer property and intended to override it with the CFMA, it would not have done so opaquely and without comment in the Bank Products Act, while at the same time making no changes to the statutory definition of customer property that the LOC Provision was promulgated to implement.

**2. The Dodd-Frank Act**

The amendments to the Bank Products Act that Congress made as part of the Dodd-Frank Act in 2010 only further support the conclusion that these Acts had nothing to do with the CFTC's treatment of LOCs in a FCM liquidation. The Dodd-Frank Act was passed in response to the 2008 financial crisis "[t]o promote the financial stability of the United States." 124 Stat. at 1376. Its language concerning "regulatory authority" and "identified banking products" was not changed in any way relevant to this case. What is relevant, however, is the Dodd-Frank Act savings clause that eliminates the possibility that the Act divests the CFTC of any regulatory authority:

> Unless otherwise provided by the amendments made by [Title VII of Pub. L. 111-203, § 711 et seq.], the amendments made by that subtitle do not divest . . . the [CFTC] . . . of any authority derived from any other applicable law.

Id. at Title VII, Subtitle A, Part II, § 743, 124 Stat. at 1735 (codified at 7 U.S.C. § 1a note). Moreover, the Dodd-Frank Act specifically incorporated the FCM subchapter of the Bankruptcy Code – including its definition of customer property – when it made that subchapter applicable to new kinds of financial companies:

> in the case of any covered financial company or bridge financial company that is a commodity broker, apply the provisions of subchapter IV of chapter 7 the Bankruptcy Code, in respect of the distribution to any customer of all customer property and member property, as if such covered financial company or bridge financial company were a debtor for purposes of such subchapter.

Id. at Title II, § 210(m)(1)(A), 124 Stat. at 1504. When Congress re-enacts the very statutes that the CFTC has interpreted without change, that is compelling evidence that Congress agrees with the CFTC's long-standing interpretation, including its treatment of LOCs. Forest Grove Sch. Dist, 557 U.S. at 239-40.

## III. THE FEDERAL LAWS GOVERNING A COMMODITY BROKER LIQUIDATION ARE CONTROLLING.

ConocoPhillips contends that, even if the LOC Provision supports the Trustee's determination, ConocoPhillips should nonetheless prevail because Congress did not intend for the CFTC to preempt state laws when it gave the CFTC the power to promulgate the Part 190 Regulations. This contention is unsupportable.

The statute in which the Congress gave the CFTC its Part 190 rulemaking authority – 7 U.S.C. § 24(a) – is the first barrier. As described above, Congress gave the CFTC the power to determine what is and what is not customer property. There is no suggestion in the statute that in doing so the CFTC is permitted only to adhere to the law of whatever state would

happen to be applicable in making that determination. If that were the case there would be no need for the regulation to begin with. There is certainly nothing in the statute to support the argument that the CFTC exceeded its authority in enacting regulations that conflict with state law. Wachovia Bank, N.A. v. Burke, 414 F.3d 305, 314 (2d Cir. 2005) ("The proper focus is on whether the agency effecting preemption 'has exceeded [its] statutory authority or acted arbitrarily.'").

A closer reading of 7 U.S.C. § 24(a) only provides further support for this proposition: it directs the CFTC to promulgate rules that certain property will be identifiable to specific customers, that govern the operation of the commodity broker including the payment of margin on futures contracts, the persons to whom customer property and commodity contracts can be transferred, and that inform how customer net equity is to be determined – all without any reference to any requirement that the CFTC follow state laws in the process.

It is well-settled that the Bankruptcy Code itself preempts state laws, and it follows that the regulations that implement it have the same effect. U.S. Const., art. I, § 8, cl. 4. (granting Congress the authority to establish "uniform Laws on the subject of Bankruptcies throughout the United States"); see Fid. Fed. Sav. & Loan Ass'n v. de la Cuesta, 458 U.S. 141, 153 (1982) ("Federal regulations have no less preemptive effect than federal statutes."); E. Equip. & Servs. Corp., 236 F.3d 117, 120-21 (2d Cir. 2001) (holding that state law tort claims for violation of automatic stay "are completely preempted by federal bankruptcy law," because Congress established a "comprehensive federal system" that sets forth the substantive standards "govern[ing] . . . debtor's affairs and creditors' rights" in bankruptcy cases); Int'l Shoe Co. v. Pinkus, 278 U.S. 261, 265 (1929) ("States may not . . . interfere with or complement the Bankruptcy Act or . . . provide additional or auxiliary regulations."). Courts have recognized this

in SIPA proceedings as well. SEC v. Albert & Maguire Sec. Co., 378 F.Supp. 906, 912 (E.D. Pa. 1974) ("[i]t is much too late to argue that the provisions of the federal Bankruptcy Act are subordinate to state laws with which they are in conflict.").

Likewise, state laws that would interfere with federal determinations about the return of customer property have been preempted. See Bevill, Bresler & Schulman, Inc., 59 B.R. 353, 378 (D.N.J. 1986), appeal dismissed, 802 F.2d 445 (3d Cir. 1986) (holding that state laws that entitled the customer to a return of its customer property "would be inconsistent with SIPA, as construed in this opinion, and are therefore pre-empted under the Supremacy Clause."). And provisions of LOCs that run contrary to a federal plan have also been superseded. See FDIC v. Bank of Boulder, 865 F.2d 1134, 1141 (10th Cir. 1988), aff'd en banc, 911 F.2d 1466 (10th Cir. 1990).

ConocoPhillips' claims about preemption are in reality an attempt to use state contract law to avoid the federal pro rata distribution system that applies to customer property in a FCM liquidation. The Bankruptcy Code and the regulations that implement it simply do not work that way. Sec. Investor Prot. Corp. v. Bernard L. Madoff Invs. Sec. LLC, 401 B.R. 629, 636 n.12 (Bankr. S.D.N.Y. 2009), aff'd sub nom. Rosenman Family, LLC v. Picard, 420 B.R. 108 (S.D.N.Y. 2009), aff'd, 395 Fed. Appx. 766 (2d Cir. 2010) ("[T]his court will not entertain any form of relief grounded in state or common law that runs counter to SIPA.").

* * *

Based on explicit congressional authority, the CFTC promulgated the regulation that controls in this case. Congress never overrode the CFTC's position, and state law is not an obstacle to the operation of a federal bankruptcy regulation. The Trustee's determination of ConocoPhillips' claims should be confirmed.

## CONCLUSION

For the foregoing reasons, the Trustee respectfully requests that this Court enter an order confirming the Trustee's determination of ConocoPhillips' claims to customer accounts margined with LOCs, expunging the ConocoPhillips' Objection, and granting such further relief as this Court deems just.

Dated: October 26, 2012
New York, New York

HUGHES HUBBARD & REED LLP

By: ______________________
James B. Kobak, Jr.
James C. Fitzpatrick
Anson B. Frelinghuysen
Marlena C. Frantzides
One Battery Park Plaza
New York, New York 10004
Telephone: (212) 837-6000
Facsimile: (212) 422-4726
Email: kobak@hugheshubbard.com

Attorneys for James W. Giddens,
Trustee for the SIPA Liquidation of
MF Global Inc.