

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

IN RE:)
MF GLOBAL INC.,) Adversary No. 11-2790 (MG) SIPA
Debtor.)

**REPLY OF THE SECURITIES INVESTOR PROTECTION CORPORATION
REGARDING APPLICABLE LIQUIDATION PROCEDURES**

JOSEPHINE WANG
General Counsel

CHRISTOPHER H. LAROSA
Senior Associate General Counsel - Litigation

LAUREN ATTARD
Assistant General Counsel

SECURITIES INVESTOR PROTECTION
CORPORATION
805 Fifteenth Street, N.W., Suite 800
Washington, D.C. 20005-2207
Telephone: (202) 371-8300

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Pursuant to the Court's order of November 17, 2011, the Securities Investor Protection Corporation ("SIPC") submits this reply memorandum regarding the procedures applicable in the instant liquidation proceeding of MF Global, Inc. ("Debtor") under the Securities Investor Protection Act ("SIPA"), 15 U.S.C. §§ 78aaa et seq. SIPC concurs in, and adopts, the SIPA Trustee's ("SIPA Trustee") reply regarding the issues raised by John Cassimatis and by the "Physicals Customers" and "Metals Clients." Sapere Wealth Management LLC, Granite Asset Management, and Sapere CTA Fund, L.P. ("Sapere"), along with the "Commodity Customer Coalition" ("CCC"), raise several additional issues, including: (1) commodities customers are entitled to an absolute priority in all assets held by the Trustee; (2) the Trustee has a conflict between his duty to securities and commodities customers; (3) the Trustee does not have discretion "to ignore the Part 190 rules;" and (4) the Trustee must immediately bring actions to recover missing customer property owed to commodities customers against "each and every entity" that received such property. Louis J. Freeh ("Chapter 11 Trustee"), the trustee for the Chapter 11 proceeding of the Debtor's parent, MF Global Holdings Ltd. ("Holdings"), takes the opposite tack, contending that the Commodity Futures Trading Commission's ("CFTC") Part 190 rules, 17 C.F.R. Part 190, do not apply in this proceeding, and that the Trustee has no power to reallocate property from the Debtor's general estate to the fund of customer property allocable to the Debtor's commodities customers. SIPC responds to these arguments below.

**APPLICABILITY OF PART 190 RULES, PRIORITY OF COMMODITY
CLAIMS, AND ALLOCATION OF ESTATE PROPERTY**

As noted, both Sapere and the CCC suggest that the Trustee has a duty to apply the CFTC's Part 190 rules such that commodity customers enjoy an absolute priority in all estate property, regardless of classification, until their claims have been satisfied in full. According to

Sapere, this super-priority is justified because “media reports” indicate that the Debtor misappropriated property held for its commodities customers and transferred that property to third parties, using its securities broker-dealer business as a conduit. Sapere concludes that the fund of customer property allocable to the Debtor’s commodities customers suffered a shortfall caused by the Debtor’s misconduct, and that this purported loss somehow creates an irreconcilable conflict between the Trustee’s duties to the Debtor’s commodities and securities customers.

Sapere and the CCC misunderstand the law applicable in a SIPA liquidation and assume as fact their speculations regarding events that are still under investigation and as to which no conclusions have been reached. As made clear in the opening memoranda filed by the SIPA Trustee and SIPC, SIPA, by its express terms, balances a trustee’s obligations to the Debtor’s commodities and securities customers. In this regard, SIPC provides that a SIPA trustee is subject to the duties applicable to a trustee operating under the Commodity Broker Liquidation provisions of Subchapter IV of Chapter 7 of the Bankruptcy Code, 11 U.S.C. §§ 761-67 – and, by extension, the Part 190 rules promulgated by the CFTC to implement those provisions – but only to the extent that those duties are consistent with SIPA or “as otherwise ordered by the court.” See SIPA § 78fff-1(b). The statute thus contemplates the liquidation under SIPA of an entity that is both a futures commission merchant and a securities broker-dealer, and provides clear rules about how the liquidation is to be conducted. Ignoring those rules – in fact, inverting them, as Sapere and the CCC suggest – is not an option.

In any event, the only areas where an accommodation of the interests of commodities and securities customers may be in question are the allocation between the commodities, securities, and general estates of any recoveries by the SIPA Trustee, and the possible reallocation of

general estate assets to the commodities and securities estates. No such allocation or reallocation is imminent, and any attempt to craft a rule governing such allocations would be premature at this point. Moreover, contrary to Sapere's assertions, the factual predicate necessary for such allocations does not exist at the present time. It is likely, for example, that, to the extent permissible at all, any reallocation of general estate property would be impacted by the relative sizes of the shortfalls in customer property allocable to the commodities and securities estates. "Media reports" notwithstanding, the SIPA Trustee repeatedly has made clear that he has not concluded his investigation and is not certain of either the magnitude of any shortfall in customer property or how any such shortfall can or should be allocated between the Debtor's commodities and securities estates.

For the same reason, it would be premature for the Court to address the question whether the Trustee, and/or the Court, has the power to reallocate general estate assets to the commodities estate. Sapere and the CCC insist that such reallocation is not only permissible, but mandatory, while the Chapter 11 Trustee asserts the contrary, citing the only case that has explored the issue. See In re Griffin Trading Co., 245 B.R. 291, 308-19 (Bankr. N.D. Ill. 2000), vacated as mooted sub nom., Inskip v. MeesPierson N.V. (In re Griffin Trading Co.), 270 B.R. 882 (N.D. Ill. 2001). Not only has the SIPA Trustee not reached a conclusion as to the amount of any shortfalls, he has noted that there is not at this time a substantial general estate property to allocate should it appear possible to do so. As the Trustee has not proposed any reallocation of general estate assets, and as the factual predicate for any such reallocation is missing, the Court should not attempt to resolve this issue at present. Instead, the Court should do so only in the context of an appropriate factual record, and upon the Trustee's request, at a later stage in the Trustee's investigation.

AVOIDANCE ACTIONS

In the same vein, the CCC next argues that the Trustee should be ordered to immediately commence avoidance actions against “each and every entity” that received transfers of customer property from the Debtor. Again, this argument is premised on an incorrect understanding of the law and an assumption of facts not yet established or known. To the extent consistent with SIPA, Chapters 1, 3, and 5, and Subchapters I and II (and IV, in this case) of Chapter 7, apply in a SIPA liquidation. See SIPA § 78fff(b). Accordingly, consistent with SIPA, and with limited modifications not relevant here, a SIPA trustee has the same powers and duties as a trustee in a Chapter 7 proceeding. See SIPA §§ 78fff-1(a) and (b). Those powers include discretion concerning whether to bring the avoidance actions provided for in the Bankruptcy Code and under state law made applicable by the Code. See, e.g., In re Tognetti, 2006 WL 2587544 at *8 (Bankr. S.D.N.Y. June 21, 2006); In re Toronto, 165 B.R. 746, 755 n. 12 (Bankr. D. Conn. 1994) (“[W]hether or not to seek the avoidance of a preference rests in the discretion of the trustee...”).

For the reasons stated above, the Trustee does not presently have the factual predicate necessary to enable him to make informed decisions concerning whether and against whom to bring avoidance actions, and there is no reason to require him to make those decisions now. The applicable limitations periods extend for several years into the future, and the Trustee’s investigation of the events surrounding the Debtor’s failure is ongoing and has not been completed. See, e.g., 11 U.S.C. § 546(a); Lippe v. Bairnco Corp., 225 B.R. 846, 852-53 (S.D.N.Y. 1998) (describing statute of limitation for claims brought under New York’s Debtor Creditor Law).

Accordingly, the Court should address this issue only if necessary in the future, and then only in the context of a ripe dispute between the parties and on the basis of a fully-developed factual record.

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Respectfully submitted,

JOSEPHINE WANG
General Counsel

/s/ Christopher H. LaRosa
CHRISTOPHER H. LAROSA
Senior Associate General Counsel - Litigation

LAUREN ATTARD
Assistant General Counsel

SECURITIES INVESTOR PROTECTION
CORPORATION
805 15th Street, N.W., Suite 800
Washington, D.C. 20005
Telephone: (202) 371-8300
Facsimile: (202) 371-6728
E-Mail: jwang@sipc.org
clarosa@sipc.org
lattard@sipc.org