

Testimony of James B. Kobak, Jr.
Counsel for the Trustee for the Securities Investor Protection Act Liquidation of
MF Global Inc.
U.S. House of Representatives Committee on Agriculture
December 8, 2011

Chairman Lucas, Ranking Member Peterson, and Members of the Committee: Thank you for inviting me to testify today about efforts to identify, preserve and return assets to former customers of MF Global Inc. My name is James Kobak. I am a partner at the law firm Hughes Hubbard and Reed and lead counsel to James Giddens, the court-appointed Trustee for the Securities Investor Protection Act (SIPA) liquidation of the failed broker-dealer, MF Global Inc. On behalf of the Trustee, I would like to provide an update on the actions his office is taking to protect MF Global Inc. customers.

Introduction

On October 31st, Mr. Giddens was appointed as the independent Trustee for the liquidation of MF Global Inc. by the United States District Court for the Southern District of New York, on recommendation from the Securities Investor Protection Corporation, or SIPC. As empowered by the Securities Investor Protection Act of 1970, when a brokerage firm must be liquidated due to bankruptcy or other financial difficulties, SIPC uses a court-appointed Trustee to, within certain limits, return customers' property as quickly as possible.

A different Trustee has been appointed to oversee the bankruptcy proceedings of MF Global Holdings Ltd. As counsel for the Trustee liquidating MF Global Inc., I do not have obligations to the MF Global holding company, nor do I have firsthand knowledge about the events that transpired prior to MF Global's bankruptcy.

The Trustee is the customers' advocate. His statutory mandate is to preserve and recover MF Global Inc. customer assets so that they can be returned to the rightful owners and to maximize the estate for all stakeholders. The Trustee's staff, which includes legal experts, consultants and forensic accountants, is singularly focused on looking after the interests of customers and returning assets to them as quickly as possible and in a way that is fair and consistent with the law.

The Trustee appreciates the interest of this Committee and other Members of Congress and has been working closely and continuously with SIPC, Commissioner Jill Sommers and the Commodity Futures Trading Commission, Chairperson Mary Schapiro and the Securities and Exchange Commission, along with the staffs of their respective organizations, and the Chicago Mercantile Exchange.

Distributions to nearly all former MF Global Inc. retail customers, whether farmers, day traders, or institutional investors, have been made within weeks of the bankruptcy filing. Through already approved expedited court filings and additional court filings that will be heard by the Bankruptcy Court tomorrow, we have laid the ground work for up to \$4.1 billion in customer distributions. The customer claims process, which we asked the Bankruptcy Court to authorize us to establish on an expedited basis, is also up and running, with claims forms on the Trustee's website and also sent by mail.

The goal of the Trustee remains to pay MF Global Inc.'s former retail commodities and securities customers 100% of the amounts in their accounts as promptly as permitted by governing regulations. Ultimate distributions are, of course, dependent upon assets available and there is no assurance of a 100% return.

Exhaustive efforts to collect funds from US depositories continue. However, complicating matters, assets located in foreign depositories for customers that traded in foreign futures are now under the control of foreign bankruptcy trustees or administrators. While the Trustee will pursue them vigorously, experience dictates that recovery of these foreign assets may be more uncertain and may take more time.

The Office of the Trustee has made every effort to communicate directly and frequently with customers. The Trustee's website includes updates, court filings, claims forms and claims filing instructions, including a section addressing the common questions being asked by customers in calls or other communications to the Trustee's staff. The Trustee's staff is answering customer calls and emails and holding meetings with customer groups and counsel. In the month of November, the Trustee's call center handled more than 8,500 calls, and more than 60,000 individuals accessed the Trustee's detailed website on more than 222,000 occasions.

If your constituents have any questions, we encourage them to visit the Trustee's website at MFGlobalTrustee.com, e-mail the Trustee's staff at MFGITrustee@hugheshubbard.com, or call our call center at 1-888-236-0808.

The Trustee and everyone working with him understands the frustration of many former MF Global Inc. customers, some of whom you may have heard from directly. When a broker-dealer fails under the unprecedented circumstances surrounding MF Global's demise, the liquidation is necessarily complex. The Office of the Trustee has been working tirelessly with speed and diligence to identify ways to return assets to customers to the full extent of our ability under the applicable provisions of SIPA, the Bankruptcy Code and CFTC regulations.

Customer Distributions

Commodities Accounts

Returning assets to former MF Global Inc. retail commodities customers has been accomplished thus far through two Bankruptcy Court-approved bulk transfers. The Trustee has filed a motion for an additional bulk transfer for commodities accounts that will be before the Bankruptcy Court for approval at a hearing tomorrow morning.

Approximately \$2 billion has already been distributed to former MF Global Inc. retail commodities customers through the first two bulk transfers. The first transfer was approved by the Court just two days after the appointment of the Trustee and implementation began immediately.

The approval of the third bulk transfer will allow the distribution of an additional \$2.1 billion, which will restore approximately two-thirds or more of US segregated customer property pro rata to all former MF Global Inc. retail commodities customers with US positions.

Once approved by the Court, the Trustee expects that the process to implement the third bulk transfer can start immediately on a rolling basis working with the CME and other derivative clearing organizations and industry participants, who estimate the transfers will take them two to four weeks to complete in most cases.

The Trustee appreciates the exhaustive efforts of the CME and other derivative clearing organizations, which have made the bulk transfers possible. The Trustee also appreciates the CME's offer of a \$550 million guarantee, which will be available for the benefit of commodity customers should it ultimately be determined that any customer has received more than a pro rata share of the final distribution.

Securities Accounts

Last week, the Trustee filed an expedited motion with the Bankruptcy Court seeking authorization to sell and transfer substantially all retail securities accounts to Perrin, Holden & Davenport Capital Corp. If successfully implemented, this transfer of approximately 300 accounts will allow former MF Global Inc. retail securities customers to receive all or a majority of the net equity in their accounts. This motion will also be heard by the Bankruptcy Court tomorrow.

The Trustee appreciates the ongoing support and partnership of SIPC. The staff of SIPC have been an invaluable resource for the Trustee's office as both groups work to protect customers and return assets as quickly as possible. SIPC will play a vital role in the return of securities customer assets.

Claims Process

The Bankruptcy Court approved the Trustee's customer claims process on an expedited basis on November 22, 2011. Consistent with SIPA principles and in the interest of an orderly and efficient claims process, separate, parallel customer claims processes have been established for MF Global Inc.'s commodity futures customers, securities customers, and general creditors, respectively.

Former MF Global Inc. commodity futures customers will file their claims against the commodity account estate. They will receive an equal, prorated distribution from two subsets in that estate: one for US positions traded through US clearing houses (so-called Rule 4(d) segregated funds), and another for foreign positions (so-called Rule 30.7 secured funds). The foreign secured funds are now largely under the control of foreign bankruptcy trustees or administrators, and the Trustee will use all means available to gain control of those assets held by foreign entities for the return to US customers. At this time, the Trustee does not have control of most of these assets and it is not known when, or if, the assets will become available to the Trustee. If commodity customer claims are not satisfied from the segregated commodity account estate, the remaining claim will automatically go against the general creditors' estate.

Security customers will file their claims against the separate fund of customer property segregated for security customers under SEC rules. Deficiencies will be covered to the limit of SIPC, which is \$500,000 for the valid claims of each securities customer, including up to \$250,000 for claims for cash deposited for the purpose of purchasing securities. Remaining deficiencies in security customer claims, if they exist, will automatically go against the general creditors' estate.

General creditors cannot receive distributions from the customer estates and can only recover claims from the general creditors' estate.

The clear regulatory intent of SIPA is the protection of customer property. Consistent with SIPA, the Trustee has the authority to seek recovery of assets removed from customer property funds to the extent a cause of action exists against those who wrongfully removed the funds. In addition, the Trustee may also seek Bankruptcy Court approval to allocate existing funds from the general creditors' estate for distribution to customers to the extent of regulatory shortfalls and under certain conditions and circumstances.

Claims have already started to be filed and reviewed, and the Trustee's office is committed to processing them promptly and to supporting a customer-friendly claims process. More than 75,000 claims forms were mailed to customers last week, and PDF claims forms have been available on the Trustee's website since November 23, 2011. The Trustee has also provided detailed instructions and deadlines on the website and has been meeting with customer groups and counsel about the process.

Investigation and “Shortfall”

As part of his statutorily-mandated duty, the Trustee is investigating the extent of and reasons for the shortfall in customer funds. The Trustee’s investigative team, consisting of counsel experienced in broker-dealer liquidations and expert consultants and forensic accountants from both Deloitte and Ernst & Young, continues in close coordination with the Department of Justice, the CFTC, the SEC, SIPC, and others.

The investigation is ongoing, and the Trustee is not yet in a position to make any definitive conclusions. However, he has determined that even if he could recover everything that is at US depositories, there will be a significant shortfall in what MF Global management should have segregated at US depositories for the benefit of customers. At present, the Trustee believes this shortfall may be as much as \$1.2 billion or more. These are preliminary numbers that may well change, and the Trustee will update these numbers as appropriate. The Trustee felt obligated to share these preliminary numbers and their uncertainty with the public to dampen assumptions that some smaller amount of the shortfall was known with certainty and could not be larger. It is the Trustee’s hope that, for the benefit of customers, the number will come down. No matter the exact size of the shortfall, however, its probable size is significant and will substantially affect the Trustee’s ability to make a 100% distribution to former MF Global Inc. customers.

The investigation will also address broader topics, including the demise of MF Global Inc. and the events and transactions that preceded it. The Trustee has requested and has been granted subpoena power to aid the investigation. The Bankruptcy Court has written an opinion supporting the Trustee’s view of the importance of maintaining the independence of that investigation and denying participation in it by the representatives of the holding company or former management whose conduct of course is an important subject of the investigation. At the same time, the Trustee is coordinating his investigation with those being conducted for law enforcement purposes by the SEC, the CFTC, and US Attorneys. It is expected that the Trustee will make an interim report on the investigation to the Court at an appropriate time, and that on completion of the investigation, the final report will be made public.

Conclusion

Thank you Chairman Lucas, Ranking Member Peterson and other Members of the Committee for the opportunity to be here on behalf of the Trustee and to submit this testimony for the full record of the hearing. You can be assured that the Trustee and his staff are fully committed to returning customers’ property as quickly as possible in a fair and equitable manner that complies with the law.

APPENDIX – TIMELINE OF TRUSTEE’S MOTIONS ON BEHALF OF CUSTOMERS AND COURT APPROVALS

- **October 31, 2011** – Court appointment of the Trustee for the SIPA Liquidation of MF Global Inc. at approximately 5:00 pm EST.
- **November 2, 2011** – Trustee files emergency motion seeking approval of the bulk transfer of customer commodity open positions and a percentage of the collateral associated with those positions.
- **November 2, 2011** – Court holds a hearing and approves Trustee’s motion for the bulk transfer of open positions and collateral.
- **November 4, 2011** – Court holds a hearing on an expedited basis and confirms Trustee’s authority to issue subpoenas as part of his duty to conduct an investigation. The Court denies a motion to participate in the investigation by representatives of the holding company and subsequently issues an opinion emphasizing the importance of the independence of the Trustee’s investigation.
- **November 7, 2011** – Trustee files motion seeking establishment of procedures to return misdirected wires.
- **November 15, 2011** – Trustee files application seeking approval of an expedited claims process.
- **November 15, 2011** – Trustee files motion seeking approval of the bulk transfer of 60% of the cash attributable to commodities accounts holding only unencumbered cash, or cash equivalents, on October 31, 2011.
- **November 17, 2011** – Court holds a hearing and approves Trustee’s motion for the bulk transfer of cash-only accounts.
- **November 22, 2011** – Court holds a hearing and approves Trustee’s expedited claims process.
- **November 22, 2011** – Court holds a hearing and approves procedures for return of post-bankruptcy misdirected wires.
- **November 29, 2011** – Trustee files motion seeking approval of the bulk transfer of up to an additional \$2.1 billion to restore approximately two-thirds or more of US segregated customer property pro rata to all former MF Global Inc. commodities customers with US positions. The motion is scheduled for hearing on December 9.
- **November 30, 2011** – Trustee files motion seeking authorization to sell and transfer substantially all retail securities accounts to Perrin, Holden & Davenport Capital Corp. The motion is scheduled for hearing on December 9.