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UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In re:	Chapter 11
MF GLOBAL HOLDINGS LTD., *et al.*,	Case No. 11-15059 (MG)
Debtors.	(Jointly Administered)
MF GLOBAL HOLDINGS USA INC., by and through MF GLOBAL HOLDINGS LTD., as Plan Administrator,	
Plaintiff,	
-against-	
HEARTLAND CO-OP,	Adversary Proceeding No.: 17-01000 (MG)
Defendant.	

MF GLOBAL HOLDINGS USA INC.'S MEMORANDUM OF LAW
IN OPPOSITION TO DEFENDANT HEARTLAND CO-OP'S MOTION TO DISMISS

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Plaintiff MF Global Holdings USA Inc. ("MF Global USA"), by and through MF Global Holdings Ltd., as Plan Administrator ("MF Global" or "Plan Administrator"), respectfully submits this memorandum of law in opposition to the motion to dismiss ("Motion") submitted by Defendant Heartland Co-Op ("Heartland"), dated February 20, 2017, in the above-captioned action.

PRELIMINARY STATEMENT

Heartland argues that the Second Amended and Restated Joint Plan of Liquidation (the "Plan") for the Debtors[1] did not specifically preserve a breach of contract claim against Heartland, and that the Plan's preservation of "any claims, demands, rights and Causes of Action that any Debtor or Estate may hold against any Person or Entity to the extent not released otherwise" was an inadequate substitute. This purported deficiency, Heartland contends, resulted in a forfeiture of the Debtors' contractual right to receive nearly $2 million owed under the early termination provisions of a 1992 ISDA Master Agreement, providing Heartland a windfall equal to that amount.

Bankruptcy law does not favor such a windfall, and the Motion must be denied. The clear weight of authority in this District is that general preservation of claims language of the type contained in the Plan preserves all claims not specifically released under the plan. In a section titled "Preservation of Causes of Action," the Plan expressly provided that the Plan Administrator could pursue any claims against any Person or Entity. Plan [Dkt No. 1382] at 37. The Plan also made clear that "the Plan Proponents' inclusion or failure to include any right of action or claim on [a nonexclusive list of potential claims] shall not be deemed an admission, denial or waiver of

[1] The Debtors include MF Global, MF Global USA, MF Global Market Services, LLC, and various of their affiliates in these jointly administered cases. The Plan was proposed by the Debtors' Chapter 11 Trustee and various Creditor Co-Proponents.

any claims, demands, rights or Causes of Action that any Debtor or Estate may hold against any Person or Entity. The Plan Proponents intend to preserve all such claims, demands, rights or Causes of Action (except to the extent any such claim is specifically released herein)." *Id.*at 38. The Chapter 11 Trustee and the Plan's Creditor Co-Proponents thus made clear that they intended to preserve causes of action, which would be pursued for the benefit of creditors.

In addition to the unmistakable intent of the Plan proponents, the Motion to Dismiss should be denied on *res judicata* grounds. This Court's order confirming the Plan specifically approved the Plan's "preservation of Causes of Action" and provided that "[i]n accordance with § 1123(b)(3) of the Bankruptcy Code, Article IV.G of the Plan provides for the Plan Administrator, on behalf of each Debtor, to retain and enforce all claims, demands, rights and Causes of Action that every Debtor and Estate may hold against any Person or Entity to the extent not otherwise released."[2] Heartland received notice of the confirmation hearing, but raised no objection to the Plan.[3] As Heartland itself admits, confirmation orders are *res judicata* and binding on all parties receiving notice thereof, and that includes Heartland.

Nor is there any basis for Heartland to claim surprise. The Debtors and Plan proponents provided extensive disclosures regarding the potential existence of unknown assets and liabilities associated with the close-out of Debtor MF Global Market Services, LLC's ("MFGMS") more than 90 ISDA Master Agreements—including disclosures in the Plan itself, the Disclosure

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[2] Order Confirming Amended And Restated Joint Plan Of Liquidation Pursuant To Chapter 11 Of The Bankruptcy Code For MF Global Holdings Ltd., MF Global Finance USA Inc., MF Global Capital LLC, MF Global FX Clear LLC, MF Global Market Services LLC, And MF Global Holdings USA Inc [Dkt No. 1288] (the "Confirmation Order") at 11 & 14. The Plan proponents made nonmaterial modifications to the Plan after the Confirmation Order was entered, which this Court approved. *See* Dkt. Nos. 1351 & 1376.

[3] *See* Affidavit Of Service [Dkt No. 1148] at 241.

Statement[4] accompanying the Plan, and the Debtors' Schedules of Assets and Liabilities and Statements of Financial Affairs. But even without these disclosures, Heartland and other creditors were on notice that claims might be pursued post-confirmation. The introduction to the Disclosure Statement made clear (in bolded type) that:

> **No reliance should be placed on the fact that a particular Claim or Interest or potential objection to a particular Claim or Interest is, or is not, identified in this Disclosure Statement. The Plan Administrator may investigate, file, and prosecute claims or Causes of Action against other Entities, including Holders of Claims or Interests and may object to or assert counterclaims against Holders of Claims or Interests after the Effective Date irrespective of whether this Disclosure Statement identifies any such Claims or Interests or objections to or counterclaims against any such Claims or Interests**

Disclosure Statement [Dkt No. 1111-1] at p. 4 (emphasis in original).

Finally, Heartland's argument ignores the fact that Heartland itself contributed to the Debtors and their Chapter 11 Trustee lacking the specific details of the MFGMS's claim against Heartland. Heartland knowingly breached its contractual obligation to deliver a valuation statement of amounts owed to MFGMS until well after the effective date of the Plan and deliberately dodged numerous pre- and post-effective date efforts by MF Global personnel and the post-effective date Plan Administrator to obtain compliance. Heartland was fully aware of its exposure prior to Plan confirmation and for years afterward, and must not be rewarded for hiding the ball in breach of its obligation. For these reasons, as set forth in greater detail below, Heartland's Motion to Dismiss should be denied.

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[4] Disclosure Statement For The Amended Joint Plan Of Liquidation Pursuant To Chapter 11 Of The Bankruptcy Code For MF Global Holdings Ltd., MF Global Finance USA Inc., MF Global Capital LLC, MF Global FX Clear LLC, MF Global Market Services LLC, And MF Global Holdings USA Inc. [Docket No. 1111-1].

BACKGROUND

I. DEBTOR MFGMS'S ISDA MASTER AGREEMENT WITH HEARTLAND

On April 9, 2010, MFGMS and Heartland entered into a standard-form 1992 ISDA Master, which is attached as Exhibit A to the Complaint (the "Heartland Master Agreement"). Complaint ¶ 15. Section 5(a)(vii) of the Heartland Master Agreement provides that an Event of Default occurs when, among other things, either party to the contract or any Credit Support Provider (in this case, MF Global) files for bankruptcy. *Id.* ¶ 16. In the schedule to the Heartland Master Agreement, MFGMS and Heartland agreed that, in the case of such an Event of Default the party that had not defaulted (the "Non-defaulting Party") would have the right to terminate the parties' transactions by designating an Early Termination Date. *See* Heartland Master Agreement § 6(a) & Schedule Part 1(g).

The parties further agreed that, in the case of such an early termination, the amount payable would be determined by the "Loss" method, which provides:

> [W]ith respect to this Agreement . . . and a party, the Termination Currency Equivalent of an amount that party reasonably determines in good faith to be its total losses and costs (or gain, in which case expressed as a negative number) in connection with this Agreement . . . including any loss of bargain, cost of funding or, at the election of such party but without duplication, loss or cost incurred as a result of its terminating, liquidating, obtaining or reestablishing any hedge or related trading position (or any gain resulting from any of them).

Heartland Master Agreement § 14 at 15 (definition of "Loss"). The Heartland Master Agreement requires that the Non-defaulting Party determine Loss "as of the Early Termination Date"—a date chosen by the Non-defaulting Party, *see id.* § 6(a)—"or, if that is not reasonably practicable, as of the earliest date thereafter as is reasonably practicable," *id.* § 14 at 15. Through the Loss mechanism, the Non-defaulting Party has either a right to collect its total losses and costs or an obligation to pay to the Defaulting Party its gains associated with the termination of transactions under the Heartland Master Agreement, as of the Early Termination Date. Complaint ¶ 17.

Critically, upon designation of the Early Termination Date, the Heartland Master Agreement requires the Non-defaulting Party to "provide to the other party a statement [the 'Statement'] (1) showing in reasonable detail, such calculations (including all relevant quotations and specifying any amount payable under Section 6(e)) and (2) giving details of the relevant account to which any amount payable to it is to be paid." *Id.* § 6(d)(i); *see also* 1992 User's Guide § 4(c)(iv) ("The Non-defaulting Party is the party that makes the relevant determination in this case."). The Statement must be delivered "[o]n or as soon as reasonably practicable following the occurrence of an Early Termination Date . . . ." *Id.*

II. THE IMPACT OF MF GLOBAL'S BANKRUPTCY ON MFGMS'S LARGE DERIVATIVES PORTFOLIO

MF Global filed for chapter 11 protection on October 31, 2011, Complaint ¶ 30, and Louis J. Freeh was appointed as its Chapter 11 Trustee soon thereafter. MFGMS filed for chapter 11 on December 19, 2011, *id.*, and Mr. Freeh became its Chapter 11 Trustee as well.

At the time of MF Global's bankruptcy filing, MFGMS had more than 90 separate ISDA Master Agreements with a similar number of counterparties, primarily governing trading portfolios focused on commodity derivatives. *See* MFGMS Schedules of Assets & Liabilities [Dkt. No. 700], Schedule G at 30-31 ("MFGMS Schedules"). Each of these Master Agreements, in turn, governed dozens, and in many cases hundreds, of underlying derivatives trades. *See* Complaint ¶ 19 n.3 (noting that Heartland and MFGMS engaged in "280 transactions" under the Heartland Master Agreement that were "memorialized in 534 trade confirmations," because many were package trades). Thus, at the time of MF Global's bankruptcy, MFGMS was a party to Master Agreements governing thousands of derivatives transactions. Moreover, other MF Global affiliates had hundreds more ISDA Master Agreements or similar counterparty arrangements that governed trades subject to early termination procedures. *See* MF Global Capital LLC Schedules of Assets

& Liabilities [Dkt. No. 699], Schedule G3 at 33-34; MF Global FX Clear LLC Schedules of Assets & Liabilities [Dkt. No. 701], Schedule G3 at 34-35.

MF Global's bankruptcy petition triggered an Event of Default under the overwhelming majority of MFGMS's ISDA Master Agreements. *See* MFGMS Schedules [Dkt. No. 700] § V(5) at 7. This Event of Default, in turn, triggered the right of MFGMS's contractual counterparties to designate an Early Termination Date on or after the date of the Event of Default and their corresponding obligations to (1) calculate the amounts owed upon Early Termination and (2) submit a valuation statement to MFGMS showing in reasonable detail the Non-defaulting party's calculations and providing payment instructions. *See, e.g.*, Heartland Master Agreement § 6(d)(i). Because the amounts owed upon early termination are required to be calculated by the Non-defaulting Party (Heartland), the defaulting party (MFGMS) is reliant, at least in the first instance, on the Non-defaulting Party's compliance with the terms of the ISDA Master Agreement and delivery of a close-out calculation that comports with the requirements of the Master Agreement.

The obligation to calculate the amounts owed on early termination is imposed on Heartland as the Non-defaulting Party for good reason; unlike their defaulted counterparty, the Non-defaulting Party is able to continue operating its business post-default, with the full benefit of its key personnel and access to its trading data and pricing sources. MFGMS, by contrast, was not in this position. As disclosed in MFGMS's Statement of Financial Affairs, "[t]he circumstances surrounding the commencement of the Debtors' cases were extraordinary and have materially impacted the Debtors' ability to access and marshal information about their businesses." MFGMS Statement of Financial Affairs [Dkt. No. 695] § 1 at 2 ("MFGMS SOFA"). Specifically, "[o]n or about the commencement of MFG's bankruptcy, many of the non-Debtor MFG entities around the

world became subject to various proceedings, in which administrators or trustees were appointed by the requisite authorities to oversee, manage, and administer the affairs of those affiliates going forward," and "Debtors were significantly and adversely affected by these proceedings because they lost full, direct access to certain personnel, a portion of their books and records, certain back office systems and document repositories" and "were no longer able to communicate directly with the employees of the non-Debtor MFG entities." *Id.* Of particular relevance, "the majority of the operational accounting functions, including day-to-day maintenance of the Debtors' books and records, were fulfilled by an accounting function . . . employed by a non-Debtor MFG entity" controlled by the SIPA appointed Trustee. *Id.* Moreover, the Debtors were under the control of the Chapter 11 Trustee, and their personnel was reduced from well over 1,000 employees to only 30 employees in the first two months after MF Global's bankruptcy filing, and was further reduced to only 13 by the time the Plan and Disclosure Statement were submitted to the Court. *See* Disclosure Statement [Dkt. No. 1111-1] § 3(J) at 49.

The logistical and administrative impediments described in the prior paragraph were particularly acute in MFGMS's derivatives trading operation. As disclosed in its Statement of Financial Affairs, under the title "Derivatives and Other Contractual Agreements":

> The Debtors do not have full access to all of their documents and contracts because these are held in document repositories controlled by non-Debtor MFG entities. Additionally, the Debtors do not have full access to personnel familiar with this information because they are employed by non-Debtor MFG entities or had their employment terminated by non-Debtor MFG entities after October 31, 2011. As a result, currently the Debtors do not have a complete listing of their contractual agreements.

MFGMS SOFA [Dkt. No. 695] § V(5) at 7. In spite of these severe impediments, as explained in the following sections, MFGMS and the Chapter 11 Trustee were careful to make fulsome disclosures regarding MFGMS' derivatives assets and liabilities and pursue liquidation of outstanding contracts such as the Heartland Master Agreement.

III. DISCLOSURE OF MFGMS's OUTSTANDING MASTER AGREEMENTS AND SPECIFIC DISCLOSURES RELATED TO HEARTLAND

On May 18, 2012, MFGMS filed its Schedules of Assets and Liabilities and Statement of Financial Affairs. *See* Dkt. Nos. 695, 700. In Schedule G of MFGMS's Schedules of Assets and Liabilities, MFGMS disclosed more than 90 ISDA Master Agreements, including the Master Agreement at issue in this case, dated on or about April 9, 2010, by and among MFGMS and Heartland. MFGMS Schedules [Dkt. No. 700], Schedule G at 30.

The Statement of Financial Affairs accompanying the Schedules specifically highlighted the existence of the outstanding Master Agreements and the potential assets and liabilities associated with the termination of trades under those agreements:

> **Derivatives and Other Contractual Agreements.** The Debtors have attempted to list on Schedule G all of the derivative contracts that they were party to as of the Petition Date . . . [A] large number of the contracts listed on Schedule G may have been terminated before or subsequent to the Petition Date. Finally, assets and liabilities that may result, or may have resulted from the termination of derivative contracts are not included on the Debtors' Schedules B, D, or F, as may be applicable. Potential additional assets and/or liabilities associated with the Debtors' derivative contracts will not be disclosed until the Debtors have completed their analysis of their books and records and the numerous derivative transactions.

MFGMS SOFA [Dkt. No. 695] § V(5) at 7.[5] The Statement of Financial Affairs further provided that "[t]he Debtors and the Chapter 11 Trustee reserve all of their rights, claims, and causes of action with respect to the contracts and agreements listed on Schedule G . . . ." *Id.* § VI(5)(iv) at 10. As noted above, the Heartland Master Agreement is listed on Schedule G.[6]

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[5] As noted in the prior Section, the same paragraph disclosed that MFGMS's lack of access to documents, contracts, and personnel at non-Debtor MFG entities severely impaired its ability to provide complete details about its derivative contracts.

[6] In addition, MFGMS disclosed that Heartland owed it $306,288.54 at the time MF Global's bankruptcy filing. MFGMS Schedules [Dkt. No. 700], Attachment B16 at 19. This amount reflects a receivable associated with Heartland's failure to deliver collateral under the parties' Credit Support Annex during the week prior to October 31, 2011. However, as disclosed in

The Disclosure Statement contained additional disclosures related to assets and liabilities associated with MFGMS's ISDA Master Agreements. Under the section of the Disclosure Statement titled "Other Potential Sources of Recovery," the first potential source of recovery listed is "Recovery of Trading Close-Out Valuation Under Certain Derivative Transactions." Disclosure Statement [Dkt. No. 1111-1] § V(A) at 78. It further discloses that "[t]he Chapter 11 Trustee has recovered in excess of $25 million for the Unregulated Debtors from the termination of certain master derivatives agreements and the related underlying transactions." *Id.* Thus, any Master Agreement counterparty with MFGMS was on notice that MFGMS's estate was seeking to recover monies it was owed upon termination of its derivative transactions.

Finally, the Disclosure Statement makes abundantly clear that it "has been prepared based on a preliminary review of certain Proofs of Claims and the ***Schedules***," *id.* at 18 (emphasis added)—*i.e.*, the very same Schedules quoted above—and the Plan specifically refers the reader to those Schedules in the definitions section, *id.* at 22; *see also id.* 51 n.18.

IV. THE PLAN AND ITS CLAIM PRESERVATION CLAUSE

The Plan was proposed jointly by the Chapter 11 Trustee and various Creditor Co-Proponents. The Plan includes a "Preservation of Causes of Action" clause, which provides in pertinent part:

> Except as provided in this Plan, the Confirmation Order, or in any contract, instrument, release or other agreement or document entered into or delivered in connection with this Plan, in accordance with § 1123(b)(3)(B) of the Bankruptcy Code, the Plan Administrator, on behalf of each Debtor, shall have and retain and may enforce any claims, demands, rights and Causes of Action that any Debtor or Estate may hold against any Person or Entity to the extent not released otherwise, all of which are included within the Property of the Estate . . . . The Plan Administrator may pursue such claims, demands, rights or Causes of Action . . . ,

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the excerpt above, this amount was not reflective of—and, in fact, diverged from—the Loss amount owed by Heartland to MFGMS upon the Early Termination Date, which Heartland designated as November 8, 2011, at which point the market had moved significantly.

> as appropriate, in accordance with the best interests of the beneficiaries of the Estates.

Plan [Dkt. No. 1382], Article IV(G) at 37-38.[7] The Plan goes on to provide "[a] nonexclusive schedule of currently pending actions and claims brought by one or more Debtors or the Chapter 11 Trustee," but is clear that the specifically named actions "shall not be deemed an admission, denial or waiver of any claims, demands, rights or Causes of Action that any Debtor or Estate may hold against any Person or Entity," and that "[t]he Plan Proponents intend to preserve all such claims, demands, rights or Causes of Action (except to the extent any such claim is specifically released herein)." *Id.* at 38.[8]

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[7] The Plan defines "Causes of Action" as including, "without limitation, any and all actions, causes of action, controversies, liabilities, obligations, rights, suits, damages, judgments, claims, and demands whatsoever, whether known or unknown, reduced to judgment, liquidated or unliquidated, fixed or contingent, matured or unmatured, disputed or undisputed, secured or unsecured, assertable directly or derivatively, existing or hereafter arising, in law, equity, or otherwise, based in whole or in part upon any act or omission or other event occurring prior to the Effective Date, including without limitation . . . any other litigation claims." *Id.*, Article I(A)(18) at 4.

[8] The nonexclusive list also makes clear (in all caps text):

> ARTICLE IV.G. OF THE PLAN PRESERVES AND RETAINS FOR THE PLAN ADMINISTRATOR, ON BEHALF OF EACH DEBTOR, ANY CLAIMS, DEMANDS, RIGHTS AND/OR CAUSES OF ACTION THAT ANY DEBTOR OR ESTATE (OR THE CHAPTER 11 TRUSTEE ON THEIR BEHALF) MAY HOLD AGAINST ANY PERSON OR ENTITY TO THE EXTENT NOT OTHERWISE RELEASED. THE BELOW LIST IS A NONEXCLUSIVE LIST OF CAUSES OF ACTION AND CLAIMS THE PLAN ADMINISTRATOR SHALL RETAIN. THE PLAN PROPONENTS' INCLUSION OF OR FAILURE TO INCLUDE ANY RIGHT OF ACTION OR CLAIM ON SUCH LIST SHALL NOT BE DEEMED AN ADMISSION, DENIAL, OR WAIVER OF ANY CLAIMS, DEMANDS, RIGHTS OR CAUSES OF ACTION THAT ANY DEBTOR OR ESTATE MAY HOLD AGAINST ANY PERSON OR ENTITY. THE PLAN PROPONENTS INTEND TO PRESERVE ALL SUCH CLAIMS, DEMANDS, RIGHTS OR CAUSES OF ACTION (EXCEPT TO THE EXTENT ANY SUCH CLAIM IS SPECIFICALLY RELEASED IN THE PLAN).
>
> Amended Plan Supplement [Dkt No. 1283], Ex. IV.G (emphasis in original).

The Disclosure Statement accompanying the Plan emphasizes its preservation of claims language, noting that "**[t]he Plan Administrator may investigate, file, and prosecute claims or Causes of Action against other Entities . . . after the Effective Date irrespective of whether this Disclosure Statement identifies any such Claims or Interests or objections to or counterclaims . . .**" Disclosure Statement [Dkt. No. 1111-1] at 4 (emphasis in original). The Plan Administrator is specifically authorized to "review, reconcile, enforce, collect, compromise, settle, or elect not to pursue any and all Causes of Action or similar actions, free of any restrictions of the Bankruptcy Code or the Bankruptcy Rules" and "maintain, conserve, supervise, prosecute, collect, settle and protect the Property of the Estate (subject to the limitations described herein)." *Id.* at 94-95. Finally, the Disclosure Statement warns that "[d]ue to uncertainty and litigation risk, no recovery value has been attributed to avoidance actions and other litigation." *Id.* at 174.

There can be no doubt that the Plan and Disclosure Statement intended to preserve for the benefit of the stakeholders of the Debtors' estates all claims, including those that were similar in nature to the derivative transaction close-out recoveries that had already produced meaningful value. Indeed, the inclusion in the Disclosure Statement of "Recovery of Trading Close-Out Valuation Under Certain Derivative Transactions" as first among "Other ***Potential*** Sources of Recovery" makes clear that the Plan proponents intended to preserve the Plan Administrator's ability to enforce MFGMS's rights under the Master Agreements and contemplated the Plan Administrator obtaining additional recoveries in doing so.

Nor is there any evidence that the Debtors, the Chapter 11 Trustee, or his Creditor Co-Proponents intended to release the estate's claims against Heartland. Indeed, there would have been no consideration for such a release, as Heartland was not contributing anything to the estates or their creditors in return for MFGMS purportedly giving up its valuable contractual rights. There

is no plausible explanation for why the Plan's proponents would have released Heartland, or as to how Heartland could have expected such a release.

V. HEARTLAND RECEIVED NOTICE OF THE BANKRUPTCY AND THE PLAN

Heartland received multiple notices from the Debtors' claims administrator regarding the bankruptcy, including of the continued section 341(a) meeting of creditors [Dkt No. 709 at 204], bar date [Dkt No. 742 at 134], confirmation hearing [Dkt No. 1148 at 241], and Plan's effective date [Dkt No. 1496 at 143].[9] Despite these repeated notices, Heartland did not object to the Plan or Disclosure Statement, nor to the preservation of causes of action provisions contained therein. Nor did Heartland ever request additional information about the potential claims against it.

VI. THE PRESENT DISPUTE AND HEARTLAND'S FAILURE TO PERFORM UNDER THE MASTER AGREEMENT

MF Global's voluntary petition for relief under chapter 11 of the Bankruptcy Code triggered an Event of Default under the Heartland Master Agreement because MF Global was a guarantor of MFGMS's obligations and a designated Credit Support Provider under the ISDA Master. Complaint ¶ 30. As the Non-defaulting Party, Heartland exercised its right to select November 8, 2011 as the Early Termination Date. *Id.* ¶ 31. Following designation of the Early Termination Date, Heartland was contractually obligated to calculate in good faith a commercially reasonable Loss amount, *see* Heartland Master Agreement § 14 at 15, and "provide to the other party a statement [the 'Statement'] (1) showing in reasonable detail, such calculations (including all relevant quotations and specifying any amount payable under Section 6(e)) and (2) giving details of the relevant account to which any amount payable to it is to be paid." *Id.* § 6(d)(i); *see also* 1992 User's Guide § 4(c)(iv) ("The Non-defaulting Party is the party that makes the relevant

[9] Heartland was scheduled as a potential creditor in both the MGFMS and MF Global cases.

determination in this case."). The Statement must be delivered "[o]n or as soon as reasonably practicable following the occurrence of an Early Termination Date . . . ." *Id.* In the letter designating November 8, 2011 as the Early Termination Date, Heartland expressly acknowledged its obligation, "[a]s soon as reasonably practicable following the Early Termination Date," to "provide [MFGMS] with a statement in accordance with Section 6(d) ('*Calculations*') (i) ('*Statement*') of the Agreement specifying the payments due in relation to the Early Termination Date." *See* Complaint, Ex. C.

Notwithstanding Heartland's recognition of its obligation to deliver a valuation statement to MFGMS "as soon as reasonably practicable" after the Early Termination date, Heartland failed to do so ***for over four years***. *Id.* ¶ 36. Indeed, while the Complaint alleges that Heartland ignored requests between October 2014 and October 2015 for delivery of the valuation statement, *id.*, a further investigation of the record reveals that Heartland was repeatedly approached about its obligation to calculate the Loss amount not just in 2014 and 2015, but also as early as 2012, *see* Declaration of Blair A. Adams, Exs. A & B. In response to each of these efforts, Heartland used delay and obfuscation to avoid disclosing that it owed MFGMS nearly two million dollars in Loss, plus significant amounts of interest. *Id.*

Without any valuation statement from Heartland, and with Heartland ignoring requests to fulfill its contractual obligations, MF Global, on behalf of MFGMS, was finally forced to perform its own calculation of Loss. Complaint ¶ 37. Using market-standard valuation techniques that employ the same methods used by MFGMS to determine daily margining of its trades with Heartland prior to the bankruptcy filing, the Plan Administrator determined that Heartland owed MFGMS approximately $1.7 million as of the Early Termination Date. *Id.* ¶¶ 37-38.

Only after MF Global provided its calculation of Loss did Heartland finally produce its own valuation statement, claiming that Heartland owed only $47,614.96, based on a flawed valuation approach that cherry-picks trades that were favorable to Heartland, ignores numerous trades that were favorable to MFGMS, and ignores key features of the parties' transactions. *Id.* ¶ 39. That valuation statement, provided for the first time in October 2015, after four years of effort by the MFGMS to coax, cajole, and ultimately compel Heartland to perform its basic contractual obligations, finally instigated some limited discussions among the parties, which made little progress and ultimately led to the present Adversary Proceeding. *See id.* ¶¶ 39-44. Delivery of the valuation statement was also a tacit admission by Heartland that MFGMS's contract rights under the Heartland Master Agreement remained enforceable notwithstanding the Confirmation Order.

The Plan Administrator commenced this Adversary Proceeding on behalf of Debtor MF Global USA on January 3, 2017. MF Global USA is the assignee of all remaining assets of MFGMS, including its claims against Heartland. Complaint ¶ 46.

ARGUMENT

I. THE ESTATE'S CLAIMS AGAINST HEARTLAND WERE ADEQUATELY PRESERVED BY THE BANKRUPTCY PLAN

Heartland's motion artfully ignores the weight of authority in the Southern District of New York, which provides that a general reservation of post-confirmation claims suffices to preserve those claims for the bankrupt estate. The law was succinctly explained by Judge Gerber in *In re Perry H. Koplik & Sons, Inc.*:

> Courts differ on how specific the language of retention and enforcement must be under section 1123(b)(3)(B). Despite this conflict among the courts, it has been held in this Court, as affirmed by the district court and the Second Circuit, that a debtor's plan of reorganization may reserve postconfirmation claims in general terms. In [*In re*] *I. Appel* [*Corp.*, 300 B.R. 564 (S.D.N.Y. 2003) (Marrero, J.)], the district court and subsequently the Second Circuit, found a chapter 11 debtor's

> general reservation of rights to litigate postconfirmation claims to be satisfactory, and rejected the notion that specific causes of action had to be preserved in a plan of reorganization. The *I Appel* court found persuasive the [*In re*] *Ampace* [*Corp.*], 279 B.R. 145 (Bankr. D. Del. 2002)] line of cases, which rejected the requirement of the specificity of claims in the plan of reorganization.

357 B.R. 231, 246 (S.D.N.Y. 2006) (finding that "a general statement on the court's retention of jurisdiction . . . satisfactorily reserved this Court's retention of jurisdiction in this proceeding."); *see also In re I. Appel Corp.*, 300 B.R. at 568 (adopting the rule that a "general reservation of claims in a plan or disclosure statement is sufficient to avoid res judicata"). This approach conforms to "the plain language of Section 1123(b)(3)(B)" which "does not require a plan to specify every claim," instead "provid[ing] that the plan *may* do so." *In re Perry H. Koplik & Sons, Inc.*, 357 B.R. at 247 (emphasis in original).

There is good reason for the rule adopted in *Appel* and *Koplik*, particularly in cases like this one, which was initiated in chaotic fashion and involved the liquidation of a large and globally integrated company with thousands—perhaps even tens of thousands—of contracts and potential claims. As District Judge Marrero explained in *Appel*, "[i]t is neither reasonable nor practical to expect a debtor to identify in its plan of reorganization or disclosure schedules every outstanding claim it intends to pursue with the degree of specificity that the [defendants] would require" because "mandating a specific description of every claim the debtor intends to pursue could entail months or years of investigation and a corresponding delay in the confirmation of the plan or reorganization." 300 B.R. at 569. This unnecessary delay would be bad for creditors because it would "either delay recovery for creditors or would induce the debtor to abandon valid claims in order to expedite the confirmation process." *Id.* The result would therefore conflict with "the purpose of the Bankruptcy Code … to 'achieve the maximum distribution in the minimum time with all creditors of the same class sharing ratably.'" *Id.* (quoting *In re Amarex, Inc.*, 74 B.R. 378, 380 (Bank. W.D. Okla. 1987)).

These concerns are cogently illustrated in the present case. As disclosed in Schedule G of MFGMS's Schedules of Asset and Liabilities, MFGMS had ISDA Master Agreements with over 90 counterparties as of the Debtors' chapter 11 filings, which governed thousands of individual over-the-counter derivative transactions. *See* MFGMS Schedules [Dkt. No. 700], Schedule G at 30-31. The thousands of individual transactions under MFGMS's ISDA Master Agreements, the overwhelming majority of which became subject to early termination upon the bankruptcy of MF Global, but were not automatically terminated. *See* MFGMS Schedules [Dkt. No. 700] § V(5) at 7. As such, MFGMS faced close-outs occurring "as of" a variety of dates, based on calculations performed by numerous different non-defaulting counterparties. Moreover, in several instances—including this one—MFGMS's counterparty breached the Master Agreement by failing to provide a valuation statement, forcing MFGMS to perform an investigation to determine the appropriate valuation of the terminated transactions long after the fact. Even with a fully staffed team of experienced individuals, this investigation can take months, or even years, particularly where, as here, the Determining Party's personnel with expertise in the complex derivatives transactions governed by the Master Agreements are no longer employed by the debtor following the bankruptcy filing. In these circumstances, any benefits of specific preservation language cannot justify the "months or years of investigation and a corresponding delay in the confirmation of the plan of reorganization" that such disclosure could require. *In re I. Appel Corp.*, 300 B.R. at 568.

Heartland's attempts to evade the law of this jurisdiction are unavailing. All of the cases Heartland relies upon are either distinguishable or inconsistent with the weight of authority in this jurisdiction, described above. For example, in *In re Kelley*, 199 B.R. 698 (9th Cir. B.A.P. 1996), the debtors had negotiated a creditor's specific treatment under the plan—payment in full over five years—in exchange for the creditor's support. *Id.* at 701. After the plan was confirmed, the

debtors objected to the creditor's claim, contending that they owed it nothing. *Id.* The court held that a general reservation of rights in the plan was not sufficient to overcome the debtors' express agreement to pay the creditor in full. *Id.* at 705. *Kelley* is distinguishable from the present case, in which there was no agreement with Heartland whatsoever regarding its treatment under the Plan or whether it could be sued post-confirmation. Indeed, Heartland could not have had any reasonable expectation that it was receiving a release under the Plan for no consideration.

In re American Preferred Prescription, Inc., 266 B.R. 273 (E.D.N.Y. 2000), is similarly distinguishable because it involved a post-confirmation objection to a claim that had been partially allowed under a plan. As explained in *In re Futter Lumber Corp., American Preferred Prescription* "dealt with a reservation of right to object to a claim as opposed to reservation of causes of action post-confirmation and the [claim at issue] had already been allowed as part of the plan and there was no specific notice given that the Debtor or the Trustee reserved any rights to pursue a further objection to the" claim. 2011 WL 5417094, at *6 (Bankr. E.D.N.Y. Nov. 8, 2011), *aff'd* 473 B.R. 20, 33 (E.D.N.Y. 2012).

In *Rosenshein v. Kleban*, 918 F. Supp. 98 (S.D.N.Y. 1996), the court found that the debtor and its affiliates knew about the debtor's potential claims but deliberately concealed them from the court and creditors. The court found sufficient evidence to "infer an intent to mislead the bankruptcy court" and a "knowing nondisclosure of the claims." *Id.* at 105. Nor was there any indication that the debtor's creditors would receive any benefit from the prosecution of the lawsuit. *Id.* at 103. By contrast, here there is no evidence that the Debtors or the Chapter 11 Trustee attempted to conceal any asset from anyone. *Id.* (acknowledging that "courts are in agreement that creditors, trustees and debtors in possession may pursue undisclosed claims following confirmation of a plan of reorganization by methods that ensure that the creditors receive the

benefit of any recovery"). To the contrary, it was Heartland that delayed for years in informing the Debtors and the Chapter 11 Trustee what it owed to them—and to this day has failed to provide a good faith valuation—in direct violation of the Heartland Master Agreement. *See* Complaint ¶ 36. And even if there had been a knowing failure by the Debtors or the Chapter 11 Trustee to disclose (which there was not), the only parties that would have been harmed by it are the very same creditors who benefit from any recovery in this litigation.

In any event, those cases which hold that confirmation of a plan is *res judicata* as to any potential claim the debtor might have against a third party are inconsistent with the plain language of the Bankruptcy Code, misconstrue the role of a plan confirmation hearing, and often end up harming the same creditor interests that they purport to protect. *See In re I. Appel Corp.*, 300 B.R. at 569 (noting that "mandating a specific description of every claim the debtor intends to pursue" would be bad for creditors because it would "either delay recovery for creditors or would induce the debtor to abandon valid claims in order to expedite the confirmation process"). It is thus with good reason that they are not followed in this jurisdiction. Bankruptcy Code section 1141 provides that all property of the estate vests in the debtor upon confirmation, unless the plan provides otherwise. 11 U.S.C. § 1141. There is no requirement that the plan itemize each and every asset that will so vest, and to impose such a rule in a large chapter 11 case would be commercially impractical and detrimental to the bankruptcy estate. Nor did Congress provide that litigation assets are to be treated differently than any other estate assets. To the contrary, Bankruptcy Code section 1123(b)(3)(B) makes clear that a plan may provide for "the retention and enforcement by the debtor, by the trustee, or by a representative of the estate appointed for such purpose, of any such claim or interest." 11 U.S.C. § 1123(b)(3)(B).

Although confirmation of a plan is a very significant event for a debtor and its creditors, it is not the forum in which to resolve every matter relating to the debtor. Congress established very specific criteria for plan confirmation in Bankruptcy Code section 1129, and none of those criteria includes the resolution of claims by the estate against third parties. 11 U.S.C. § 1129(a). *Res judicata* and collateral estoppel bar parties from relitigating issues that either were litigated or could have been litigated in a prior proceeding. *See Federated Dep't Stores, Inc. v. Moitie*, 452 U.S. 394, 398 (1981). Those doctrines simply are not applicable to the estate's claims against third parties, which generally could not be litigated at a confirmation hearing. And while valuation of the debtor's assets may be relevant at confirmation, there is no requirement that every asset be individually appraised for purposes of confirmation. In this case, whether the Debtors did or did not have a $2 million claim against Heartland would not have altered the Plan or the outcome of the confirmation hearing. *See* 11 U.S.C. § 1125(a)(1) ("adequate information" for a disclosure statement means information that would enable a creditor "to make an informed judgment about the plan"). Even if the Debtors' claims against Heartland were material to creditors' votes on the Plan, it would be absurd to hold that the same creditors are now barred from recovering on account of those claims simply because the claims were not disclosed to them. The Bankruptcy Code's disclosure requirements are designed to protect creditors, not to harm them.

Indeed, to the extent that *res judicata* applies here, it is Heartland that should be bound by it. Heartland received multiple notices of the bankruptcy, including the confirmation hearing. *See* Background § V, *supra*. Yet, Heartland raised no objection as to the breadth of the reservation of rights provisions in the Plan. Nor did Heartland appeal, and the Confirmation Order is final. The Plan and Confirmation Order are binding on Heartland, including the provisions that authorize "the Plan Administrator, on behalf of each Debtor, to retain and enforce all claims, demands, rights

and Causes of Action that every Debtor and Estate may hold against any Person or Entity to the extent not otherwise released." Confirmation Order [Dkt. No. 1288] at p. 14. Heartland may not collaterally attack this provision now.

II. EVEN IF THE PRESERVATION CLAUSE WAS INADEQUATE TO PRESERVE EVERY UNDISCLOSED CLAIMS, THE POTENTIAL CLAIMS AGAINST HEARTLAND WERE ADEQUATELY DISCLOSED

"[E]ven if a blanket reservation in the plan itself is insufficient, if the disclosure statement expressly reserves causes of action, then there is no *res judicata* bar." *In re Futter Lumber Corp.*, 473 B.R. 20, 33 (E.D.N.Y. 2012). Here, there can be no question that the existence of derivatives claims are adequately disclosed. Under the section of the Disclosure Statement titled "Other Potential Sources of Recovery," the very first potential source of recovery listed is "Recovery of Trading Close-Out Valuation Under Certain Derivative Transactions." Disclosure Statement [Dkt. No. 1111-1] § V(A) at 78. There is little else the Chapter 11 Trustee could have done in terms of disclosure. Additional detail regarding potential recoveries (or liabilities) on the specific close-out of the Heartland Master Agreement was not available at the time of the Disclosure Statement, because Heartland—in breach of its obligations under the Heartland Master Agreement—had failed to deliver a valuation statement. *See* Complaint ¶ 36.

The Disclosure Statement is further supplemented by disclosures in the Schedules and Statements of Financial Affairs filed by the Debtors, which are specifically referenced throughout the Disclosure Statement and the Plan. *See, e.g.*, Disclosure Statement [Dkt. No. 1111-1] § XV(A) at 131 ("This Disclosure Statement has been prepared based on a preliminary review of certain Proofs of Claim and the Schedules."). Schedule G of MFGMS's Schedules of Assets and Liabilities specifically lists each and every one of MFGMS's more than 90 ISDA Master Agreements with derivative counterparties, including the Heartland Master Agreement. MFGMS Schedules [Dkt. No. 700], Schedule G at 30. Moreover, the Statement of Financial Affairs filed

by MFGMS disclosed in no less than two places that MFGMS was continuing to investigate claims under the Master Agreements and reserved all rights in respect of those potential claims and assets. *See* MFGMS SOFA [Dkt. No. 695] § V(5) at 7 ("**Derivatives and Other Contractual Agreements** …[A] large number of the contracts listed on Schedule G may have been terminated before or subsequent to the Petition Date . . . Potential additional assets and/or liabilities associated with the Debtors' derivative contracts will not be disclosed until the Debtors have completed their analysis of their books and records and the numerous derivative transactions."); *id.* § VI(5)(iv) at 10 ("The Debtors and the Chapter 11 Trustee reserve all of their rights, claims, and causes of action with respect to the contracts and agreements listed on Schedule G …"). In light of these disclosures, all contract counterparties, including Heartland, were on notice of the potential existence of unknown assets and liabilities associated with the close-out of MFGMS's Master Agreements. As such, the Complaint is not barred by *res judicata*.

III. MF GLOBAL USA HAS STANDING TO PROSECUTE ITS BREACH OF CONTRACT CLAIMS AGAINST HEARTLAND

Heartland's last-ditch argument that MF Global USA lacks standing to bring its breach of contract claim against Heartland fails for many of the same reasons as its prior two theories. While "[c]ourts have held that . . . an unscheduled claim remains the property of the bankruptcy estate" and therefore "the debtor lacks standing to pursue the claims after emerging from the bankruptcy," *Kotbi v. Hilton Worldwide, Inc.*, 2012 WL 914951, at *2 (S.D.N.Y. 2012), those circumstances are not presented here.

First, the claims against Heartland were clearly included on MFGMS's Schedules of Assets and Liabilities and Statement of Financial Affairs, with as much detail as was available at the time. As noted above, MFGMS's Schedule G specifically listed the Heartland Master Agreement. Moreover, MFGMS's Statement of Financial Affairs was clear that "assets and liabilities that may

result, or may have resulted from the termination of derivative contracts, are not included on the Debtors' Schedules B, D, or F, as may be applicable" and "will not be disclosed until the Debtors have completed their analysis of their books and records and the numerous derivative transactions." MFGMS SOFA [Dkt. No. 695] § V(5) at 7. It further provided that "[t]he Debtors and the Chapter 11 Trustee reserve all of their rights, claims, and causes of action with respect to the contracts and agreements listed on Schedule G . . . ," *id.* § VI(5)(iv). Because these statements adequately disclosed the claims at issue in this case, the consequences of non-disclosure do not come into play.

Second, the Plan Administrator brings this claim on behalf of a current debtor, MF Global Holdings USA Inc., as assignee of MFGMS, thus preserving the value of these claims for the estates and their creditors. Thus, there is no risk of a debtor, having emerged from bankruptcy cleansed of its liabilities *via* discharge, profiting from an undisclosed claim; the recoveries from this case will go to the benefit of MF Global USA's creditors—the very entities that the bankruptcy laws are structured to protect. In such circumstances, the law is clear that claims are allowed to proceed. *See Rosenshein*, 918 F. Supp. at 102 ("The courts are in agreement that creditors, trustees and debtors in possession may pursue undisclosed claims following confirmation of a plan of reorganization by methods that ensure that the creditors receive the benefit of any recovery.").

CONCLUSION

For the foregoing reasons, Plaintiff respectfully submits that Heartland's Motion to Dismiss should be denied.

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Respectfully submitted,

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