Hearing Date and Time: January 19, 2012 at 11:00 a.m. (Prevailing Eastern Time)
Objection Deadline: January 12, 2012 at 4:00 p.m. (Prevailing Eastern Time)

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In re	Chapter 11
MF GLOBAL HOLDINGS LTD., *et al.*,	Case No. 11-15059 (MG)
Debtors.	(Jointly Administered)
SAPERE WEALTH MANAGEMENT LLC, GRANITE ASSET MANAGEMENT and SAPERE CTA FUND, L.P.,	
Movants,	
-against-	
STATUTORY CREDITORS' COMMITTEE OF MF GLOBAL HOLDINGS LTD., *et al.*,	
Respondents.	

OBJECTION OF STATUTORY CREDITORS' COMMITTEE OF MF GLOBAL HOLDINGS LTD., *ET AL.* TO MOTION TO DIRECT DEBTORS' ESTATE TO BE ADMINISTERED PURSUANT TO 11 U.S.C. §§ 761-767 AND 17 C.F.R. § 190

The statutory creditors' committee appointed in the chapter 11 cases of MF Global Holdings Ltd., *et al.* (the "Committee" of the "Chapter 11 Debtors," respectively), submits this objection (the "Objection") to the *Motion to Direct the Debtors' Estate to be Administered Pursuant to 11 U.S.C. §§ 761-767 and 17 C.F.R. § 190*, filed December 5, 2011, ECF No. 217,

(the "Motion"), by Sapere Wealth Management LLC, Granite Asset Management, and Sapere CTA Fund, L.P. (the "Movants"). In support of its Objection, the Committee states as follows:

SUMMARY OF ARGUMENT

1. The Motion requests that these chapter 11 cases be administered for the benefit of Movants. The Motion must be denied because Movants fail to state a claim upon which relief could be granted. In requesting that subchapter IV of chapter 7 be made applicable to these chapter 11 cases, Movants effectively ask the Court to convert these cases to chapter 7, but fail to allege the requirements for converting a case under section 1112 of title 11 of the United States Code (the "Bankruptcy Code"). If Movants wish to apply subchapter IV of chapter 7 *without* converting these cases to cases under chapter 7, that would violate section 103(a) of the Bankruptcy Code. To the extent Movants demand that MF Global Inc. ("MFGI") customers be granted priority claims against the Chapter 11 Debtors, Movants are requesting the functional equivalent of substantive consolidation of the chapter 11 and SIPA estates and simultaneous equitable subordination to commodity customer "net equity" claims (as defined below) of all other claims of the Chapter 11 Debtors' estates' creditors. And yet Movants fail to properly plead the mandatory elements for such extraordinary relief. Therefore, the Motion must be denied.

2. Movants allege a trio of immaterial "reasons" why the Court should grant their unprecedented request for relief. First, Movants claim that the Debtors became a "*de facto*" futures commodities merchant ("FCM") pursuant to the Commodities Exchange Act, 7 U.S.C. § 1 *et seq.* (the "CEA"). This claim is meaningless in the absence of conversion of the chapter 11 cases to cases under chapter 7 and, in any event, the Bankruptcy Code expressly limits the

applicability of subchapter IV of chapter 7 to FCM's that have a "customer" as that term is defined by section 761(9) Bankruptcy Code, another fact that has not been properly pled by Movants.

3. Movants then claim the Chapter 11 Debtors should be held liable for the acts of MFGI under a vicarious liability theory embedded in the CEA, or because the Court should pierce the corporate veil between the Chapter 11 Debtor and MFGI. Movants fail, however, to properly allege or substantiate even these claims, which, in any event, could lead only to *non-customer* creditor claims against the Chapter 11 Debtors, providing Movants with no priority status whatsoever. These claims serve merely to accentuate Movants' failure to state a claim upon which relief could be granted.

4. Perhaps recognizing the their requests are based on neither facts nor law, Movants have a back-up plan: they demand a Bankruptcy Rule 2004 discovery order if they lose on their primary requests for relief. By filing the Motion, Movants initiated a contested matter, and so are no longer entitled to a Rule 2004 investigation. Movants' discovery is now limited to the procedures applicable under the rules of discovery in contested matters. If Movants lose as they candidly admit they might, there will be no basis for subsequent discovery because the doctrine of *res judicata* will bar Movants' requested do-over.

BACKGROUND

5. On October 31, 2011 the Chapter 11 Debtors filed voluntary petitions for relief under chapter 11 of the Bankruptcy Code,[1] and the Securities Investor Protection

[1] On December 19, 2011, MF Global Capital LLC, MF Global FX Clear LLC, and MF Global Market Services LLC filed voluntary petitions for relief under chapter 11 of the Bankruptcy Code. The Chapter 11 Debtors' cases have been consolidated for procedural purposes only and are being jointly administered pursuant to Rule 1015(b) of the Federal Rules of Bankruptcy Procedure.

Corporation ("SIPC") commenced an adversary proceeding against MFGI pursuant to the Securities Investor Protection Act ("SIPA"). Also on that date, James W. Giddens was appointed as trustee of the estate of MFGI (the "SIPA Trustee") to conduct a liquidation of the securities broker-dealer pursuant to SIPA. To the extent consistent with the provisions of SIPA, the SIPA Trustee is subject to the same duties as a trustee in a case under chapter 7 of the Bankruptcy Code. *See* 15 U.S.C. § 78fff(b); *In re Bernard L. Madoff Inv. Securities LLC*, 445 B.R. 206, 219 n.12 (Bankr. S.D.N.Y. 2011).

6. On November 7, 2011, the United States Trustee for the Southern District of New York (the "U.S. Trustee") appointed the Committee.[2] On November 21, 2011, the Chapter 11 Debtors and the Committee filed a joint motion requesting the appointment of a chapter 11 trustee for the Chapter 11 Debtors pursuant to section 1104(a) of the Bankruptcy Code. On November 22, 2011, the Court entered an order directing the U.S. Trustee to appoint a chapter 11 trustee, and on November 25, 2011, the U.S. Trustee appointed Louis J. Freeh as chapter 11 trustee (the "Chapter 11 Trustee") and requested Court approval of the Chapter 11 Trustee's appointment. On November 28, 2011, the Court entered an order approving the Chapter 11 Trustee's appointment.[3]

7. On December 5, 2011, just one week after appointment of the Chapter 11 Trustee, and well before the Chapter 11 Trustee could have an opportunity to obtain access to,

[2] The U.S. Trustee designated the following five members to serve on the Committee: (i) Wilmington Trust, National Association, as Indenture Trustee for the (a) 6.250% Notes due August 8, 2016, (b) 3.375% Notes due August 1, 2018, (c) 1.875% Notes due February 1, 2016, and (d) 9% Notes due June 20, 2038; (ii) JP Morgan Chase Bank, N.A., as Agent under the $1,200,875,000 Revolving Credit Facility, dated as of June 15, 2007; (iii) Bank of America, N.A.; (iv) Elliott Management Corporation; and (v) Caplin Systems Ltd.

[3] On December 23, 2011 the U.S. Trustee appointed Mr. Freeh as chapter 11 trustee for MF Global Capital LLC, MF Global FX Clear LLC, and MF Global Market Services LLC, and on December 27, 2011, the Court entered an order approving the appointment.

review, and analyze the many issues implicated by this Motion, Movants filed the Motion requesting the Court "direct[] the Debtors-in-Possession, their non-debtor subsidiaries and affiliates . . . and the bankruptcy Trustee to administer the Debtors' estates pursuant to 11 U.S.C. §§ 761-767 and 17 C.F.R. § 190 . . . [thereby] providing priority status to commodities customers to the extent of their segregated accounts at . . . MFGI." Motion, at p. 1.[4]

OBJECTION

8. At its core, the Motion demands: "the Debtor's Chapter 11 case must be administered consistent [sic] 17 C.F.R. § 190.08(a)(1)(ii)(J) and in consonance with 11 U.S.C. § 766(h), with the [MFGI] commodities customers having segregated accounts[5] being treated as a customer class of the [Chapter 11] Debtors." Motion, at p. 7. The Motion must be denied for failure to state a claim upon which relief could be granted.

Conversion to Chapter 7 & Application of Subchapter IV

9. Section 766 of the Bankruptcy Code is located in subchapter IV of chapter 7. Movants request that the Court require the application of subchapter IV to the estates of the Chapter 11 Debtor case, with Movants "entitled to receive payment out of the Debtors' estate of 100% of those customers' segregated-account funds on a first priority basis." Motion, at p. 7. But section 103(d) of the Bankruptcy Code provides: "Subchapter IV of chapter 7 of this title

[4] Contemporaneously with the Motion, Movants filed an e*x parte* motion to shorten notice requesting that the Motion be heard by the Court on December 9, 2011 at 2:00 p.m., with objections due that day at 9:00 a.m. The Committee filed an objection to the motion to shorten notice, as did the Chapter 11 Trustee. The Motion has now been scheduled pursuant to the case management order filed by the Chapter 11 Trustee and is scheduled to be heard on the first omnibus hearing date in these cases on January 19, 2012.

[5] Movants misunderstand the nature of their accounts at MFGI. While Commodity Futures Trading Commission Regulation 1.20(a) indeed requires segregation of "customer funds . . . as belonging to . . . commodity or option customers," and the deposit of such funds "under an account name which clearly identifies them as such," these regulations anticipate the creation of omnibus accounts holding segregated positions of multiple customers, and permit the pooling of segregated positions for distribution purposes. *See* 17 C.F.R. § 1.20(a). Because it is essentially the "positions" of customers that are segregated, and not their "accounts," Movants claim of "segregated accounts," as if those funds were specifically identifiable property, is not meaningful.

applies *only* in a case under such chapter concerning a commodity broker," 11 U.S.C. § 103(d) (emphasis supplied), and does *not* apply in cases under chapter 11, or chapter 7 cases that do not "concern[] a commodity broker."

10. The Chapter 11 Debtors' cases are proceeding under chapter 11 of the Bankruptcy Code. Subchapter IV of chapter 7 of the Bankruptcy Code cannot apply to the Chapter 11 Debtors' estates unless (a) the cases of the Chapter 11 Debtors are converted to cases under chapter 7 *and* (b) the Chapter 11 Debtors are "commodity brokers," as defined by the Bankruptcy Code. Movants fail to properly allege facts establishing any cause for conversion or that the Chapter 11 Debtors are "commodity brokers."

a. Conversion to Chapter 7

11. Section 1112 of the Bankruptcy Code governs conversion of cases under chapter 11 to chapter 7, and provides:

> Except as provided in paragraph (2) and subsection (c), on request of a party in interest, and after notice and a hearing, the court shall convert a case under this chapter to a case under chapter 7 or dismiss a case under this chapter, whichever is in the best interests of creditors and the estate, *for cause* unless the court determines that the appointment under section 1104(a) of a trustee or an examiner is in the best interests of creditors and the estate.

11 U.S.C. § 1112(b)(1) (emphasis supplied). Section 1112(b)(4) offers sixteen grounds that constitute cause for conversion. All sixteen of these grounds, such as "gross mismanagement of the estate," "unauthorized use of cash collateral substantially harmful to 1 or more creditors," "failure to comply with an order of the court," and so on, describe in some fashion *post-petition* mismanagement of a chapter 11 estate. *See* 11 U.S.C. §§ 1112(b)(4)(A)-(P). Movants fail to establish or even allege facts that would constitute such "cause" under section 1112. Moreover,

any actions that Movants might allege as grounds for conversion pre-dated the appointment of the Chapter 11 Trustee (which the Court found was "in the best interests of creditors and the estate"), and any threat that such alleged actions might continue were cured by such appointment.

12. Even had the Chapter 11 Trustee not been appointed, conversion of these cases to chapter 7 would not be in the best interest of the creditors and estates of the Chapter 11 Debtors. Indeed, Movants' preferred outcome, "the commodities customers having segregated accounts being treated as a customer class of the Debtors . . . entitled to receive payment out of the [Chapter 11] Debtors' estate of 100% of those customers' segregated-account funds on a first priority basis, ahead of all creditors, secured and unsecured," Motion, at p. 7, would be completely inimical to the "best interests" of the creditors of the Chapter 11 Debtors, who would otherwise not even share the chapter 11 estates' assets with MFGI's customer net equity claims, let alone be subordinated to them. Under such circumstances, the Court may not convert the chapter 11 cases to cases under chapter 7. 11 U.S.C. § 1112(b).

b. Application of Subchapter IV of Chapter 7

13. Even if the chapter 11 cases of the Chapter 11 Debtors were converted to cases under chapter 7, as noted above, pursuant to section 103(d), subchapter IV of chapter 7 would not apply to Movants' claims unless the Chapter 11 Debtors constitute a "commodity broker," under the Bankruptcy Code. *See* 11 U.S.C. § 103(d). "Commodity broker" is defined in section 101(6) of the Bankruptcy Code as a "futures commission merchant . . . with respect to which there is a customer, as defined in section 761 of," the Bankruptcy Code. 11 U.S.C. § 101(6).

14. The first half of the definition of a "commodity broker" – futures commission merchant – "ha[s] the meaning[] assigned to th[at] term[] in the [Commodity Exchange] Act." 11 U.S.C. §§ 761(1), (8). The CEA defines an FCM as an entity that *presently* "*is engaged* in soliciting or accepting orders" and, "in connection with *such* solicitation or acceptance of orders, accepts any money . . . to margin, guarantee, or secure any trades or contract that result . . . therefrom." 7 U.S.C. § 1(a)(28) (emphasis supplied). The second half of the "commodity broker" definition – "a customer, as defined in section 761" – means an:

> entity for or with whom such futures commission merchant deals and that holds a claim against such futures commission merchant on account of a commodity contract made, received, acquired, or held by or through such futures commission merchant *in the ordinary course of such futures commission merchant's business as a futures commission merchant* from or for the commodity futures account of such entity.

11 U.S.C. § 761(9)(A) (emphasis supplied). Thus, even if these cases were converted to chapter 7, to be granted their requested relief, Movants would have to prove – or at a minimum, to state a claim, allege – that the Chapter 11 Debtors constituted an FCM under CEA (a "Purported FCM"), *and* (b) that the Purported FCM had a "customer" in the ordinary course, as required by section 761(9)(A) of the Bankruptcy Code.

15. Movants fail these requirements. They merely allege:

> corporate parent (Debtor Holdings) was "accept[ing]" money that FCM customers had deposited "to margin, secured, or guarantee any trades or contracts," which the parent-Holdings used in futures activities. . . . the Debtor became a *de facto* FCM the moment it accessed segregated-account funds.

Motion, at pp. 6-7.

16. Movants glibly allege that the Chapter 11 Debtors and MFGI *together* constitute one FCM under the CEA, with no factual allegation at all to sustain a claim that the *Chapter 11 Debtors* meet the CEA definition of an FCM. Equally fatal is Movants failure to allege that they constitute a "customer" of the Chapter 11 Debtors, with a claim arising against the Chapter 11 Debtors in the manner specified by section 761, that is, a claim arising from Movants' "deal[ing]" with the Chapter 11 Debtors as an FCM, "in the ordinary course" of the Chapter 11 Debtors business as an FCM (as opposed to MFGI). Thus any "*de facto*" FCM argument is ineffective in this context.

Sections 103 & 105 of the Bankruptcy Code & 28 U.S.C. § 157

17. Alternatively, if Movants wish section 766 of the Bankruptcy Code to apply to the Chapter 11 Debtors without converting these cases to chapter 7, that would directly and unequivocally violate section 103(d) of the Bankruptcy Code.

18. Movants argue that section 105 of the Bankruptcy Code authorizes this Court to issue an order directly contravening the express requirements of the Bankruptcy Code, *see* Motion, at p. 2. As the Second Circuit has made unequivocally clear, such misuse of section 105 is woefully misguided:

> Section 105(a) of the Bankruptcy Code gives the court equitable power to 'issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title.' 11 U.S.C. § 105(a). This Court has long recognized that Section 105(a) limits the bankruptcy court's equitable powers, which must and can only be exercised within the confines of the Bankruptcy Code. . . . It does not authorize the bankruptcy courts to create substantive rights that are otherwise unavailable under applicable law, or constitute a roving commission to do equity. . . . The equitable power conferred on the bankruptcy court by section 105(a) is the power to exercise equity in carrying out the provisions of the Bankruptcy Code, rather than to further the purposes of the Code

> generally, or otherwise to do the right thing. . . . th[e statutory] language suggests an exercise of section 105 power be tied to another Bankruptcy Code section and not merely to a general bankruptcy concept or objective.

In re Dairy Mart Convenience Stores, Inc., 351 F.3d 86, 91-92 (2d Cir. 2003) (citations omitted).

19. Movants fail to "tie" their requested relief to "another Bankruptcy Code section" or to cite any Bankruptcy Code section that would authorize their requests. To the contrary, such relief would "create substantive rights that are otherwise unavailable under applicable law," violate express provisions of the Bankruptcy Code, and cause this Court to use section 105 to act as a "roving commission to do equity," something it is explicitly prohibited from doing. *Dairy Mart*, 351 F.3d at 92.

20. Movants' citation to 28 U.S.C. §§ 157(b)(1) and (b)(2)(A) is baffling. Those sections provide:

> (1) Bankruptcy judges may hear and determine all cases under title 11 and all core proceedings arising under title 11, or arising in a case under title 11, referred under subsection (a) of this section, and may enter appropriate orders and judgments, subject to review under section 158 of this title.
> (2) Core proceedings include, but are not limited to—
> (A) matters concerning the administration of the estate . . . .

28 U.S.C. §§ 157(b)(1)-(B)(2)(A). While 28 U.S.C. § 157(b)(2)(B) (not cited by Movants) provides that allowance of claims constitute a "core proceeding," Movants fail to explain how 28 U.S.C. §§ 157(b)(1)-(B)(2)(A) in any way authorizes the Court to disregard express provisions of the Bankruptcy Code.

Substantive Consolidation & Equitable Subordination

21. As Movants are customers of MFGI, in asking for priority and superpriority distributions from the assets of the Chapter 11 Debtors, Movants are effectively

asking for the substantive consolidation of the estates of MFGI and the Chapter 11 Debtors and the simultaneous equitable subordination of all non-commodities customer creditors' claims that may exist against any debtor, including creditors of the Chapter 11 Debtors and residual securities customer claims against MFGI.

22. The Second Circuit has identified "two critical factors" required for substantive consolidation: "(i) whether creditors dealt with the entities as a single economic unit, . . . or (ii) whether the affairs of the debtors are so entangled that consolidation will benefit all creditors." *In re Augie/Restivo Baking Co., Ltd.*, 860 F.2d 515, 518 (2d Cir. 1988) (citations omitted). Movants fail to offer any facts whatsoever that would satisfy either prong of the *Augie/Restivo* test, and so any request for substantive consolidation, whether in form or in substance, must likewise be dismissed for failure to state a claim.

23. Movants likewise do not even allege grounds to justify subordination of other claims to their claims. "A bankruptcy court may subordinate a particular claim if it finds that the creditor's claim, while not lacking a lawful basis nonetheless results from inequitable behavior on the part of that creditor." *In re Enron Corp.*, 379 B.R. 425, 432-33 (S.D.N.Y. 2007). The basis for subordination in a bankruptcy case is section 510 of the Bankruptcy Code, which in turn relies on pre-Bankruptcy Code "existing doctrine." *Id.*

> Courts had uniformly adopted the three-pronged test set forth by the Fifth Circuit in *In re Mobile Steel Co.* for evaluating whether to equitably subordinate a claim: (1) the subordinated creditor must have engaged in some type of inequitable conduct; (2) the misconduct must have resulted in injury to the creditors of the bankrupt or conferred an unfair advantage on the claimant; and (3) equitable subordination of the claim must not be inconsistent with the provisions of the Bankruptcy Act. . . . Inequitable conduct under the first prong of the *Mobile Steel* test is generally defined as either (1) fraud, illegality, or breach of fiduciary duties; (2)

> undercapitalization; or (3) the claimant's use of the debtor as a mere instrumentality or alter ego. The second requirement is met where the general creditors are less likely to collect their debts as a result of the alleged inequitable conduct. If the misconduct results in harm to the entire creditor body, the [trustee] need not identify the injured creditors or quantify their injury, but need only show that the creditors were harmed in some general, concrete manner. The third requirement has been read as a reminder to the bankruptcy court that although it is a court of equity, it is not free to adjust the legally valid claim of an innocent party who asserts the claim in good faith merely because the court perceives that the result is inequitable.

Id. at 42-43 (citing *United States v. Noland*, 517 U.S. 535 (1996) and *In re Mobile Steel Co.*, 563 F.2d 692 (5th Cir. 1977)). Movants fail to allege inequitable conduct on the part of any creditor of the Chapter 11 Debtors or MFGI that Movants seek to subordinate, or allege facts that meet any other element required for equitable subordination.

17 C.F.R. § 190

24. Movants' reliance on 17 C.F.R. § 190 is as misplaced as their reliance on section 105, their attempts to convert this case, and their demands for substantive consolidation and subordination. C.F.R. section 190 governs distribution of property in a commodity broker liquidation and purports to allow general estate property to be allocated to customer property beyond the extent permitted by subchapter IV of chapter 7 of the Bankruptcy Code (as made applicable by SIPA), thereby diminishing the assets a commodity broker can use to pay claims of other creditors.

25. That 17 C.F.R. § 190 does not apply to the MFGI SIPA proceeding derives from its underlying statute, section 24(a) of the CEA, which provides: "*Notwithstanding title 11, the Commission may provide, with respect to a commodity broker that is a debtor under chapter 7 of title 11*, by rule or regulation - (1) that certain cash, securities, other property, or commodity

contracts are to be included in or excluded from customer property or member property." 7 U.S.C. § 24(a)(1) (emphasis supplied).

26. MFGI is not a chapter 7 debtor. It did not file a chapter 7 petition and no chapter 7 petition was filed against it. The U.S. Trustee did not appoint an interim chapter 7 trustee pursuant to section 701(a) of the Bankruptcy Code, which applies in stockbroker and commodity broker liquidations under subchapters III and IV of chapter 7. Rather, the District Court for the Sothern District of New York appointed Mr. Giddens, as SIPA trustee, in paragraph II of its order dated October 31, 2011. *See SIPA v. MF Global Inc.*, 11-cv-07750-PAE, ECF No. 3, at *1 (S.D.N.Y, October 31, 2011). The Commodity Futures Trading Commission (the "CFTC"), in its letter to the Court dated December 22, 2011, SIPA ECF No. 781, has pointed out that a SIPA trustee has duties of a chapter 7 trustee. The Committee agrees. But, the CFTC letter effectively corroborates the Committee's position that 17 C.F.R. § 190 can only apply to chapter 7 debtors, in accordance with section 24(a)(1) of the CEA, by failing to cite an iota of authority providing that because a SIPA trustee has duties of a chapter 7 trustee, section 190 applies to a non-chapter 7 case outside the bounds of section 24(a)(1) of the CEA. There is no authority whatsoever for the proposition that because the SIPA Trustee has several duties of a chapter 7 trustee, that a regulation applicable only to chapter 7 cases also applies to the MFGI SIPA proceeding.

27. Moreover, even if MFGI were a chapter 7 debtor, Movants cannot use 17 C.F.R. § 190 to grab superpriority status. In a decision that discussed extensively the customer property provisions of subchapter IV and the CFTC rules governing the liquidation of commodity brokers, the Bankruptcy Court for the Northern District of Illinois determined that 17

C.F.R. § 190.08(a)(1)(ii)(j) exceeded the CFTC's statutory authority to regulate and must be stricken. *In re Griffin Trading Co.*, 245 B.R. 291 (Bankr. N.D. Ill. 2000), vacated as moot *sub nom*. *Inskeep v. MeesPierson N.V. (In re Griffin Trading Co.)*, 270 B.R. 882 (N.D. Ill. 2001). The CFTC appealed the bankruptcy court's decision, but following a settlement among the estate's creditors, the appellate court dismissed the appeal as moot, and granted in connection therewith a request by the CFTC that the bankruptcy court's decision be vacated. The Committee's research has not disclosed even one case relying on 17 C.F.R. § 190.08(a)(1)(ii)(j) to extend a customer priority beyond the scope of Bankruptcy Code section 761(10).

Movants' Alleged Non-Customer Creditor Claims

28. Although moot in light of the failures of Movants to offer grounds on which they may be granted relief, Movants' additional "reasons" why they believe "the bankruptcy protections accorded to commodities customers' segregated accounts should apply to the administration of these Debtors' estates," Motion, at p. 6, – the Court should pierce the corporate veil of the Chapter 11 Debtors, and the Court should find the Chapter 11 Debtors vicariously liable for any failures by MFGI to comply with CEA and CFTC regulations – are without factual support and legally incorrect.

a. Piercing the Corporate Veil

29. Movants cite one decision, *United States v. Bestfoods*, 524 U.S. 51 (1998), in support of their claim that the Chapter 11 Debtors are liable for the purported misdeeds of MFGI. Movants pluck from *Bestfoods* a recitation of black-letter law "that the corporate veil may be pierced and the shareholder held liable for the corporation's conduct when, *inter alia*, the corporate form would otherwise be misused to accomplish certain wrongful purposes, most

notably fraud, on the shareholder's behalf." *Bestfoods*, 524 U.S. at 62, Motion, at p. 6. Movants then abandon this thought, failing to allege fraud or wrongful purpose.

30. *Bestfoods*, in fact, is not a case where the corporate veil was pierced. To the contrary, in *Bestfoods*, the appeals court refused to pierce the corporate veil, and the Supreme Court remanded the case for a determination whether other grounds for liability existed under Federal environmental law. *Bestfoods*, 524 U.S. at 64-65, 73. In any event, "New York courts disregard corporate form reluctantly," *Gartner v. Snyder*, 607 F.2d 582, 586 (2d Cir. 1979), and such veil-piercing must "be predicated either upon a showing of fraud or upon complete control by the dominating corporation that leads to a wrong against third parties." *Wm. Passalacqua Builders v. Resnick Developers*, 933 F.2d 131, 138 (2d Cir. 1991).

31. Movants fail to allege any such fraud, complete control, or harm to third parties, nor is there any factual record to support such drastic relief. By their own admission, Movants cannot provide the Court any evidence to support piercing of the corporate veil. All Movants have provided as "evidence" are news articles. Rather than this fatal lack of evidence giving them pause, Movants have decided it is actually further evidence they are correct! Movants allege:

> Debtor and/or its non-debtor subsidiaries and affiliates notifi[cation to] the SEC and CFTC of a shortfall in segregated-account funds and the statements of the SIPA Liquidation Trustee that $600 million up to $1.2 billion or more of customer-funds is missing are themselves sufficient to provide the legal framework for administration of claims against the Debtor's estate. (In classic, common law terms, this is at least a *res ipsa loquitur* situation.)

Motion, at p. 8.

32. Any statement to the CFTC, SEC, the SIPA Trustee, or any other person or entity concerning an apparent shortfall of customer funds "speaks" no more than what it states: that there appeared at that time to be a shortfall in the segregated accounts of MFGI. Speculation notwithstanding, such statements prove nothing more than that they were said, cannot meet the Second Circuit requirements to pierce the corporate veil, and cannot sustain Movants' attempt to shift to other parties their required burdens of pleading facts or providing evidence.

33. Even if Movants could pierce the corporate veil, they are confused about the resulting priority of their claims. Section 766 of the Bankruptcy Code (which as explained above does not apply to these chapter 11 cases) establishes a priority in favor of commodity "customers" over other claims with respect to distributions of "customer property" on the basis and to the extent of such customers' allowed "net equity" claims. *See* 11 U.S.C. § 766. Claims made by third parties under corporate veil piercing and vicarious liability (discussed below) doctrines are not included in "net equity" claims. Such claims would be general creditor claims against the Chapter 11 Debtors, not entitled to any of the protections of sections 766(h) of the Bankruptcy Code or 17 C.F.R. § 190. *See* 11 U.S.C. § 761(17). And as discussed above, Movants fail to state a claim for subordination of any other claims to their claims.

b. CEA Vicarious Liability

34. Movants alleges that "Holdings is, for the purposes of the Act and the CFTC's regulations thereunder, the 'person' charged with compliance with all of the Act's requirements," Motion, at p. 6. In support, Movants offer nothing but speculation about the

Chapter 11 Debtors operation of MFGI and a citation to section 2(a)(1)(b) of the CEA, which provides:

> The act, omission, or failure of any official, agent, or other person acting for any individual, association, partnership, corporation, or trust within the scope of his employment or office shall be deemed the act, omission, or failure of such individual, association, partnership, corporation, or trust, as well as of such official, agent, or other person.

Motion, at p. 6, citing 7 U.S.C. § 2(a)(1)(b).

35. Beginning with *Guttman v. Commodity Futures Trading Commission*, 197 F.3d 33 (2d Cir. 1999), the Second Circuit explicitly began applying what amounts to a *respondeat superior* test for vicarious liability under the CEA. *Guttman*, 197 F.3d at 39-40. *Guttman* confirmed that agency and scope of employment were requisite elements for CEA based vicarious liability. *Id.* Movants fail to offer a shred of evidence or a factual allegation to support a finding of these required elements, so their vicarious liability claim is without support.

36. Moreover, as with Movants allegation regarding piercing the corporate veil, even if Movants could establish vicarious liability, they do not allege any facts or cite any law which would yield them a priority – as opposed to a general creditor – claim, and offer no grounds to subordinate other claims to their claims.

2004 Examination

37. No doubt understanding the weakness of their arguments, Movants request that should the Court deny the Motion, it should nevertheless order a Bankruptcy Rule 2004 examination. Movants seem unaware that "once an adversary proceeding or contested matter is commenced, discovery should be pursued under the Federal Rules of Civil Procedure and not by Rule 2004." *In re Enron Corp.*, 281 B.R. 836, 840 (Bankr. S.D.N.Y. 2002). *See also*, 9

COLLIER ON BANKRUPTCY, ¶ 2004.01[1] (16th ed. 2011) ("if an adversary proceeding or contested matter is pending, the discovery devices provided for in Rules 7026-7037 . . . apply and Rule 2004 should not be used."). By filing the Motion, Movants have initiated a contested matter and lost their ability to conduct a Rule 2004 examination. Pursuant to the doctrine of *res judicata*, they do not get a do-over because of their own errors and mistakes.

CONCLUSION

WHEREFORE the Committee respectfully requests that the Court deny the Motion with prejudice for failure to state a claim upon which relief could be granted, and grant the Committee such other and further relief as is just.

Dated: January 12, 2012
New York, New York

DEWEY & LEBOEUF LLP

By: /s/ Martin J, Bienenstock

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