

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

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In re	:	Chapter 11
	:	
	:	Case No. 11-15059 (MG)
MF GLOBAL HOLDINGS LTD., <u>et al.</u> ,	:	
	:	
	:	Jointly Administered
Debtors.	:	
	:	
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**RESPONSE OF THE UNITED STATES TRUSTEE TO
CHAPTER 11 TRUSTEE’S BRIEF IN SUPPORT OF THE
RETENTION AND EMPLOYMENT OF FREEH GROUP
INTERNATIONAL SOLUTIONS, LLC AS ACCOUNTANTS
TO THE TRUSTEE *NUNC PRO TUNC* TO THE APPOINTMENT DATE**

TO: THE HONORABLE MARTIN GLENN,
UNITED STATES BANKRUPTCY JUDGE:

Tracy Hope Davis, the United States Trustee for Region 2 (the “United States Trustee”), in furtherance of the duties and responsibilities set forth in 28 U.S.C. §§ 586(a)(3) and (5), hereby files her response (the “Response”), as requested by the Court at the hearing on February 9, 2012, to the Chapter 11 Trustee’s Brief filed on March 5, 2012 in support of the retention and employment of Freeh Group International Solutions, LLC (“FGIS”) as his accountants (the “Chapter 11 Trustee’s Brief”).¹ ECF Docket No. 517.

I. INTRODUCTION

This Response is written to address the applicability of the Second Circuit’s holding in In re Palm Coast, Matanza Shores Limited Partnership, 101 F.3d 253 (2d Cir. 1996) to the Chapter 11 Trustee’s application to retain FGIS (the “FGIS Retention

¹ While the Chapter 11 Trustee’s Brief labels FGIS’s retention as “accountants” for the Chapter 11 Trustee, the FGIS Retention Application (as defined herein) labels FGIS’s retention as that of “advisors.”

Application”). The Court requested additional briefing on this and several related issues at the hearing on February 9, 2012 on the FGIS Retention Application.

If a trustee retains himself as a professional, the trustee acquires an interest potentially adverse to the estate, thereby impairing his independence and disinterestedness. Thus, the appointment of FGIS must fall within one of the exceptions of Section 327, in this case, subsection 327(d).

In Palm Coast, the Second Circuit stated that a bankruptcy trustee can hire his own law or accounting firm because those two occupations are specifically exempted by subsection 327(d) of the Bankruptcy Code. Therefore, FGIS may not be retained unless the Court finds that FGIS is being retained as an “accountant;” that is, that FGIS meets the statutory definition of an “accountant” set forth in section 101(1) of the Bankruptcy Code and that its proposed duties are those that would typically be performed by an accountant.

II. FACTS

A. General Background

1. On October 31, 2011, MF Global Holdings Ltd. (“Holdings”) and MF Global Finance USA Inc. (together with Holdings, the “Initial Debtors”), each commenced a voluntary case under Chapter 11 of the Bankruptcy Code.

2. On November 7, 2011, the United States Trustee appointed an Official Committee of Unsecured Creditors (the “Committee”) pursuant to section 1102(a) of the Bankruptcy Code.

3. On November 21, 2011, the Initial Debtors and the Committee filed the Joint Emergency Motion for Order Pursuant to 11 U.S.C. § 1104 and Fed. R. Bankr. P. 2007.1 Directing Appointment of Chapter 11 Trustee. ECF Docket No. 131.

4. By Order dated November 22, 2011, ECF Doc. No. 156, the Court directed that the United States Trustee appoint a Chapter 11 trustee in these cases. On November 25, 2011, the United States Trustee filed the Notice of Appointment of Chapter 11 Trustee, ECF Doc. No. 168, which appointed Louis J. Freeh as the trustee of the Initial Debtors' estates (the "Chapter 11 Trustee") and the Application for Order Approving Appointment of Chapter 11 Trustee (the "Trustee Application"). ECF Doc. No. 169.

5. On November 28, 2011 (the "Appointment Date"), the Court entered an order granting the Trustee Application. ECF Doc. No. 170.

6. On December 19, 2011, MF Global Capital LLC, MF Global Market Services LLC, and MF Global FX Clear LLC (the "Additional Debtors," and together with the "Initial Debtors," and MF Global Holdings USA Inc., the "Debtors") also filed for relief under chapter 11 of the Bankruptcy Code. Subsequently, on March 2, 2012, MF Global Holdings USA Inc., also filed a voluntary petition for relief under Chapter 11 of the Bankruptcy Code.

7. On December 23, 2011 and March 8, 2012, respectively, the Court approved the appointment of Louis J. Freeh as the Chapter 11 Trustee of the Chapter 11 cases of the Additional Debtors and MF Global Holdings USA Inc.

B. FGIS Retention Application

8. On January 23, 2012, the Chapter 11 Trustee filed applications seeking to employ (a) Freeh Sporkin & Sullivan, LLP ("FSS") as his investigative counsel and (b)

FGIS as his advisors (the “FGIS Retention Application”), both *nunc pro tunc* to the Appointment Date. ECF Docket Nos. 388 and 390. Both retention applications rely on 11 U.S.C. § 327(a) for statutory authority.

9. The Chapter 11 Trustee is the founder and Chairman of FGIS and is also the founder and the Senior Managing Partner of FSS. See Declaration of Disinterestedness by Louis J. Freeh at ¶¶ 1 and 2, ECF Docket No. 390.

10. The FGIS Retention Application does not represent that FGIS, as a firm, is a licensed accountant in any jurisdiction. On information and belief, various employees of FGIS are individually licensed as accountants or attorneys.

10. The FGIS Retention Application contemplates that the services for which FGIS would be employed are as follows:

- (a) managing the facilitation and coordination of information and data exchange between the various worldwide administrations including, but not limited to, the SIPA proceeding: *SIPC v. MF Global Inc. (In re MF Global Inc.)*, Case No. 11-2790 and the United Kingdom Administration of MF Global Overseas Limited;
- (b) coordinating the workflow administration between the Trustee’s professionals, the Committee and its professionals, and the various worldwide administrations including, but not limited to, the SIPA proceeding: *SIPC v. MF Global Inc. (In re MF Global Inc.)*, Case No. 11-2790) and the United Kingdom Administration of MF Global Overseas Limited;
- (c) assisting the Trustee with the day-to-day, short-term and long-term management of the bankruptcy process, including evaluation of strategic and tactical options with respect to the SIPA proceeding and various insolvency administrations throughout the world, as well as management of the wind down of the debtors operations; and
- (d) assisting the Trustee in undertaking additional tasks that the Court may direct, to the extent those tasks are consistent with those set forth *infra*.

See FGIS Retention Application at ¶ 11.

11. Pursuant to the Court's request at the February 9, 2012 hearing, on March 5, 2012, the Chapter 11 Trustee filed the Chapter 11 Trustee's Brief in essence making the following two arguments:

- (a) Section 327(d) of the Bankruptcy Code is not implicated and the retention of FGIS is properly requested pursuant to Section 327(a) because the Chapter 11 Trustee himself will not be providing services to the estates as a member of FGIS; rather, he will be providing services solely as a member of FSS.
- (b) The services for which FGIS is being retained to provide are accounting-type services, accordingly, the FGIS Retention Application does not run afoul of the holding in Palm Coast.

See Chapter 11 Trustee's Brief at p. 2.

12. In the Chapter 11 Trustee's Brief, the Trustee sets forth the scope of services to be provided by FGIS as the following:

- Provide forensic accounting support and leadership of the 11 U.S.C. § 1106(a)(3) investigation, and as required in any subsequent litigation.
- Assist in the development of tax-friendly strategies with the Trustee's professionals to recapture funds from foreign subsidiaries in liquidation proceedings.
- Formulate for the Trustee strategies for the cost-effective utilization of existing company personnel and the integration of the company's staff with the financial advisory team, and other professionals retained in these cases.
- Participate in the negotiation, reconciliation and resolution of claims asserted by the Debtors against MF Global foreign affiliates and assess the distributable value that will flow from those entities to the chapter 11 estates.
- Participate in strategy calls and negotiations with the administrators for the various MF Global foreign affiliates, primarily KPMG and Deloitte & Touche LLP, the advisors for

those affiliates, to aid the Trustee in maximizing recovery for these estates.

- Serve as a member of the creditors' committees of (I) MF Global Overseas Limited and (ii) MF Global Holdings UK Limited, foreign non-debtor subsidiaries in wind-down proceedings, on behalf of the Debtors in order to monitor the financial positions of those debtor entities and report to the Trustee.
- Conduct meetings with the SIPA Trustee in order to:
 - (I) Close the Debtors' books and records;
 - (ii) Coordinate the sharing of information necessary to respond to the audits and complete the tax returns of the various Debtors;
 - (iii) Develop strategies to assess the movement of funds between the Debtors and MFGI; and
 - (iv) Oversee the calculation of inter-company claims related to trading and borrowing under the bank facility.
- The development and drafting, calculation and formulation of the customer claims filed on behalf of the chapter 11 estates and their subsidiaries in the SIPA case.
- Determine appropriate employee and professional retention levels, including review of professional's billing, and provide high-level cost-benefit analysis on such matters, for the purpose of maximizing efficient use of the estates' resources.
- Communicate with the Statutory Creditors' Committee and the bank group regarding efforts to maximize value to the estate.

See Chapter 11 Trustee's Brief at pp. 10-11.²

III. RESPONSE

A. Retention of FGIS Must Fall Within the Exception of Subsection 327(d)

The Chapter 11 Trustee argues that he will not be providing the estates' services through FGIS. Instead, he asserts that those services will be provided by him solely as a member of FSS. See Chapter 11 Trustee's Brief at pp. 2, 9. As a result, the Chapter 11

² The revised scope of services delineated in the Chapter 11 Trustee's Brief overlaps, to a certain extent, with the services that FTI Consulting Inc. was retained by the Chapter 11 Trustee to perform. See ECF Docket No. 438. Should the Court determine that FGIS may be retained under 327(a) & (d), the scope of services to be performed by FGIS should be carefully delineated so as to avoid any duplication with those to be performed by FTI Consulting.

Trustee argues that subsection 327(d) does not apply. Such argument misinterprets the “disinterestedness” requirements of Section 327 and the narrow exceptions set forth therein.

Pursuant to Section 327(a) of the Bankruptcy Code:

Except as otherwise provided in this section, the trustee, with the court’s approval, may employ one or more attorneys, accountants, appraisers, auctioneers, or other professional persons, that do not hold or represent an interest adverse to the estate, and that are disinterested persons, to represent or assist the trustee in carrying out the trustee’s duties under this title.

11 U.S.C. § 327(a). The Bankruptcy Code includes as a “disinterested person,” someone who

(a) is not a creditor, an equity security holder, or an insider,

(b) is not and was not, within 2 years before the date of the filing of the petition, a director, officer, or employee of the debtor, and

(c) does not have an interest materially adverse to the interest of the estate or of any class of creditors or equity security holders, by reason of any direct or indirect relationship to, connection with, or interest in, the debtor, or for any other reason.

11 U.S.C. § 101(14).

The standards of subsection 327(a) make *per se* invalid a trustee’s appointment of him or herself, as well as his or her firm, to serve in any professional capacity; accordingly, anytime that a trustee attempts to hire his or her firm, Section 327(d) is implicated, because the trustee would thereby acquire an interest adverse to the estate, which would render the trustee not disinterested. The Court in Palm Coast reached that conclusion and noted:

A trustee who hires his own professional firm to assist him cannot be a “disinterested person” who has no interest adverse to the estate. Once the

trustee's firm is hired by the estate, the trustee's personal interests are implicated. At that point, the trustee's independence and disinterestedness are compromised by a potential conflict of interest. The trustee may be placed in a position where it would be to his benefit to harm the reorganization or dissolution of the estate. Because "[e]quity tolerates in bankruptcy trustees no interest adverse to the trust," we hold that a trustee is not permitted to hire his own firm in a non-lawyer or non-accountant capacity. In certain situations, a bankruptcy trustee can hire his own law or accounting firm, but only because those two occupations are specifically exempted by subsection 327(d) of the Bankruptcy Code.

Pam Coast, 101 F.3d at 258 (citations omitted). Accordingly, the Chapter 11 Trustee may retain FGIS only if the firm falls within the exception in Section 327(d).

The fact that the Chapter 11 Trustee will not be providing services to the Debtors' estate through FGIS is not relevant. Section 327(d) does not apply solely when a trustee himself will be providing services through the firm being retained. Rather, it applies any time a trustee retains his or her own firm – which is the case here. See 3 Collier on Bankruptcy ¶327.04[1] (16th Ed.) (“Under section 327(d), trustees may retain their own law firms as attorneys for the trustee, but any applications for compensation and reimbursement of expenses must clearly distinguish between the trustee's administrative activities and the legal services rendered by the law firm.”). Moreover, the holding in Palm Coast was in no way premised on the fact that the trustee in that case was providing services as a member of the firm. Palm Coast, 101 F.3d at 258. Accordingly, the fact that the Chapter 11 Trustee in this case will provide services as a member of FSS cannot be used as a distinguishing factor from the holding in Palm Coast.

II. While Section 327(d) Applies With Respect to the FGIS Retention Application, FGIS May Only be Retained if FGIS Meets the Statutory Definition of “Accountant”

The Chapter 11 Trustee is correct in arguing that the Second Circuit in Palm Coast held that the Chapter 11 trustee in that case could not hire his real estate firm

because “a bankruptcy trustee may not hire his or her firm in a non-lawyer or non-accounting capacity.” Palm Coast, 101 F.3d at 258. The Second Circuit explained that “[i]n certain situations, a bankruptcy trustee can hire his own law or accounting firm, but only because those two occupations are specifically exempted by subsection 327(d) of the Bankruptcy Code.” Id. at 258 (emphasis added). Given that the real estate firm at issue fell squarely outside of the realm of the Section 327(d) exceptions, the Second Circuit was not asked to apply its holding that “a trustee is not permitted to hire his own firm in a non-lawyer or non-accounting capacity” to facts similar to those before this Court. Id. at 258. This is therefore a question of statutory construction not addressed by Palm Coast.

Section 327(d) provides that “[t]he court may authorize the trustee to act as attorney or accountant for the estate if such authorization is in the best interest of the estate.” 11 U.S.C. §327(d). In turn, Section 101(1) defines “accountant” as “accountant authorized under applicable law to practice public accounting, and includes professional accounting association, corporation or partnership, if so authorized.” 11 U.S.C. §101(1). Moreover, Section 101(4) defines “attorney” as “attorney, professional law association, corporation, or partnership, authorized under applicable law to practice law.” 11 U.S.C. § 101(4).³

FGIS is not licensed as an accounting firm and therefore is not eligible to be retained under the section 327(d) exception as it does not satisfy the statutory definition of an accountant. Moreover, even if it were an accounting firm, it appears that it is not

³ For example, in New York State, a firm that is established for the business purpose of lawfully engaging in the practice of public accountancy must register with the state board for public accountancy. NY Education Law §§ 7403, 7408(3)(a).

being retained to perform “accounting capacity” services. While “accounting capacity” is not defined by the Second Circuit in Palm Coast, it appears that the initial scope of retention which has not been formally revised seeks to retain FGIS to perform duties that are not traditional accounting duties. Moreover, even as revised, the retention of FGIS still contemplates that FGIS will be performing duties that are outside the scope of traditional accounting services. For example, the Chapter 11 Trustee proposes that FGIS will serve as a member of the creditors’ committees in MF Global Overseas Limited and MF Global Holdings UK Limited, on behalf of the Debtors. FGIS will also be requested to communicate with the Statutory Creditors’ Committee and the bank group regarding efforts to maximize value to the estate. See Chapter 11 Trustee’s Brief at pp. 10-11. These are not traditional accounting services.

IV. CONCLUSION

The FGIS retention application in its present form is not consistent with section 327(a) or (d) of the Bankruptcy Code, however, such inconsistency may be curable should FGIS be able to demonstrate that it is an accounting firm authorized under applicable law to practice public accounting. To the extent that FGIS can establish that it is an “accountant” under section 101(1), its retention would be permissible so long as its proposed duties are limited to duties that are generally performed by persons acting in the capacity of an accountant. If FGIS cannot be so retained, the Trustee should be afforded a reasonable opportunity to explore alternative mechanisms for obtaining the services of professionals necessary to a successful reorganization of these cases.

WHEREFORE, the United States Trustee requests that the Court grant such relief
as is just or proper.

Dated: New York, New York
March 19, 2012

Respectfully submitted,

TRACY HOPE DAVIS
UNITED STATES TRUSTEE

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