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

In re

MF GLOBAL INC.,

Debtor.

Case No. 11-2790 (MG) SIPA

**TRUSTEE'S PRELIMINARY REPORT ON STATUS OF HIS INVESTIGATION AND  
INTERIM STATUS REPORT ON CLAIMS PROCESS AND ACCOUNT TRANSFERS**

1. James W. Giddens (the “Trustee”) as trustee for the liquidation of MF Global Inc. (“MFGI”), respectfully submits this preliminary report on the progress of his investigation and interim status report on the claims process and account transfers, in accordance with his duties under sections 78fff-1(c) and (d) of the Securities Investor Protection Act (“SIPA”), 15 U.S.C. §§ 78aaa *et seq.*, and in accordance with the suggestion of the Court that the Trustee prepare reports on a more frequent basis than a six-month formal reporting period (Hr’g Tr., Nov. 22, 2011, ECF No. 423).

2. As the Court is aware, on October 31, 2011, the Honorable Paul A. Engelmayer, United States District Court Judge for the Southern District of New York, entered an Order (the “MFGI Liquidation Order”) commencing liquidation of MFGI pursuant to the provisions of SIPA in the case captioned *Securities Investor Protection Corp. v. MF Global Inc.*, Case No. 11-CIV-7750 (PAE).

3. The MFGI Liquidation Order, *inter alia*: (i) appointed James W. Giddens as Trustee for the liquidation of the business of MFGI pursuant to SIPA section 78eee(b)(3); (ii) appointed Hughes Hubbard & Reed LLP counsel to the Trustee pursuant to SIPA section 78eee(b)(3); and (iii) removed the case to this Court as required for SIPA cases by SIPA section 78eee(b)(4).

### **INVESTIGATION**

4. The Trustee’s investigation has preliminarily determined that MFGI had a shortfall in commodities customer segregated funds beginning on Wednesday, October 26, 2011,

and that the shortfall continued to grow in size until the bankruptcy filing on Monday, October 31, 2011.<sup>1</sup>

5. The Trustee's investigators have now traced a majority of the cash transactions, totaling more than \$105 billion, made in and out of MFGI in the last week before bankruptcy and are completing the process of tracing the remaining transactions. MF Global also executed securities transactions totaling more than \$100 billion during its final week of operations. These included liquidation of customer securities, proprietary positions and other items. The securities included complex instruments, such as off-balance sheet repurchase transactions involving sovereign debt securities and derivative structures.

6. For three months the Trustee's investigative team has worked to understand what happened during the final days of MF Global when cash and related securities movements were not always accurately and promptly recorded due to the chaotic situation and the complexity of the transactions. With these preliminary investigative conclusions in hand, the Trustee's investigative team will analyze where the property wired out of bank accounts established to hold segregated and secured property ultimately ended up. The Trustee will then determine whether there is a sound and legal basis for recoveries against third parties that will help make customers whole. These will be very complex legal and factual determinations, which the Trustee will make consistent with his duty as the advocate for the former customers of MFGI.

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<sup>1</sup> This preliminary report on the progress of the Trustee's investigation is supplemented by slides that are annexed as Appendix A.

7. The investigation to date has found that transactions regularly moved between accounts and that funds believed to be in excess of segregation requirements in the commodities segregated accounts were used to fund other daily activities of MF Global. In the past, such transfers were in amounts of less than \$50 million, but as liquidity demands increased and could not be met from internal sources, much larger amounts were used, apparently with the assumption that funds would be restored by the end of the day. By Wednesday, October 26th, as the result of increasing demands for funds or collateral throughout MF Global, funds did not return as anticipated. As these withdrawals occurred, a lack of intraday accounting visibility existed, caused in part by the volume of transactions being executed, and the 4(d) U.S. segregated commodity customer account appears to have reached a deficit condition on Wednesday, October 26th that continued through to MF Global's bankruptcy.

8. The Trustee has identified most of the parties that were the immediate recipients of transfers from MFGI during the final days and weeks of operation. These transfers were largely effected through the clearing banks acting on behalf of MFGI. The ultimate recipients of these transfers included banks, exchanges and clearing houses, MFGI affiliates, counterparties, and customers of the futures commission merchant and the broker-dealer.

9. The number of transactions executed by MF Global during the last week prior to the initiation of insolvency proceedings escalated to unprecedented volumes. The rush to meet funding needs for collateral, margin and customer liquidations led to billions of dollars in securities sales, draws on credit facilities, and a web of inter-company loans across affiliates, some foreign. The company's computer systems and employees had difficulty keeping up with the unprecedented volume of transactions. A number of transactions were recorded erroneously or not at all. So called "fail" transactions—where either the buyer or seller fails to deliver the

cash or the security, respectively—were five times the normal volume during the firm’s final week.

10. The investigation has revealed that a confluence of factors contributed to the deterioration of MF Global’s liquidity position. The exposure to European sovereign debt, coupled with the announcement of disappointing quarterly results, triggered credit downgrades by Moody’s, Fitch and S&P. This escalation in credit risk mandated substantial margin calls and increased demands from counterparties and exchanges for collateral. As an example, the additional margin paid to support only the sovereign debt positions exceeded \$200 million during the final week of operations. This was a significant drain on available cash and securities. The sovereign debt investments undertaken on a repo to maturity basis allowed some immediate gains to be booked, but these were purely paper profits generating negligible cash while the underlying transactions resulted in calls for substantial additional margin.

11. The heightened risk and apparent loss of confidence drove customers to close their accounts and withdraw funds, resulting in even greater demands on a relatively limited amount of available cash. The Trustee’s investigation has revealed that, while personnel may not have been immediately aware of it, MFGI experienced a shortfall in 4(d) customer funds beginning during the day on Wednesday, October 26th. MF Global Holdings Ltd., the MF Global parent company, struggled to continue to operate and even to sell the business, but MFGI appears to have remained in a shortfall of commodity customer segregated funds virtually continuously until its parent filed for Chapter XI protection on Monday, October 31st and the SIPA proceeding was commenced against MFGI later that afternoon.

12. The Trustee’s investigators, including the legal and forensic accounting teams, have conducted over 50 witness interviews, preserved secure access to thousands of boxes

of hard copy documents, imaged over 800 computer drives, and are maintaining over 100 terabytes of data.

13. To understand where the funds went during October 2011, the analysis conducted by the Trustee's professionals has included 840 cash transactions in excess of \$10 million that total \$327 billion, and an ongoing analysis of related securities transactions involving a value of over \$100 billion. These large cash transactions alone span 47 bank accounts across eight financial institutions. An additional 20,000 cash transfers that total \$9 billion involve transfers of less than \$10 million.

14. The Trustee's investigation is continuing to correlate cash transfers to relevant movements of securities used as collateral or loaned to counterparties. To that end, the Trustee is now working with various third parties to further define these securities transactions and obtain more complete information about the extent and basis for transfers to select parties. The Trustee continues to investigate the complex factual and legal questions to determine how best to pursue possible recoveries and the extent to which applicable law would support claims against particular recipients of funds, affiliates, and possibly to other parties, including employees of MF Global.

15. The Trustee's investigation will continue, in coordination with the regulatory and law enforcement investigations that are being conducted by the Department of Justice, the Commodity Futures Trading Commission, and the Securities Exchange Commission on an ongoing basis. The Trustee will seek to release additional information related to his investigation in the future, but cannot prematurely release information that might compromise the integrity of those investigations or the Trustee's own efforts to recover funds for customers and the estate.

## **CLAIMS PROCESS AND ACCOUNT TRANSFERS**

16. The Trustee's staff is continuing its analysis of customer claims after the claims filing period for commodities customers closed on January 31, 2012.

17. Once a claim is reviewed by the Trustee's staff on as expedited a basis as possible, a determination letter will be issued to the claimant. These determination letters are being issued on a rolling basis. The determination letter will acknowledge the claim and provide a determination as to whether the claim has been allowed, denied, reclassified, or is subject to further reconciliation or information requests.

18. The Trustee is eager to make additional distributions to former MFGI customers as soon as possible. However, the Trustee is required by law to hold an appropriate reserve of funds until disputed claims are resolved either through negotiation or by the Court. At this time, the Trustee anticipates significant disputed claims against the MFGI estate by MF Global Holdings Ltd., MF Global UK Limited, and other entities. The Trustee will move to attempt to resolve these claims as quickly as possible, but it is uncertain how long resolution will take. Therefore, it is not known at this time when the Trustee will be legally able to make additional distributions.

19. The Trustee has already distributed nearly \$4 billion to former MFGI retail commodities customers with U.S. futures positions via three bulk transfers:

- Within days of the bankruptcy, the Trustee received Court approval for the transfer of 10,000 commodities customer accounts with three million open positions, along with approximately \$1.5 billion in collateral associated with those positions at the time of the bankruptcy. These open positions had a notional value of \$100 billion. It is estimated that 40% of all commodity futures exchange activity in U.S. markets came from MFGI trades and a serious disruption in markets was avoided by the transfer.

- A transfer of 60% of the cash attributable to approximately 15,000 customer commodity accounts with cash only in the accounts, totaling approximately \$500 million, was completed in November.
- In December and January a third transfer occurred that moved approximately \$2 billion to restore 72% of U.S. segregated customer property to all former MFGI retail commodities customers with U.S. futures positions.

20. In addition, the Trustee has received Court approval to sell and transfer approximately 318 active retail securities accounts, which is substantially all of the securities accounts at MFGI. Nearly all securities customers have received 60% or more of their account value and already 194 of former MFGI securities customers have received the entirety of their account balances because of a Securities Investor Protection Corporation guarantee.

Dated: New York, New York  
February 6, 2012

Respectfully submitted,

HUGHES HUBBARD & REED LLP

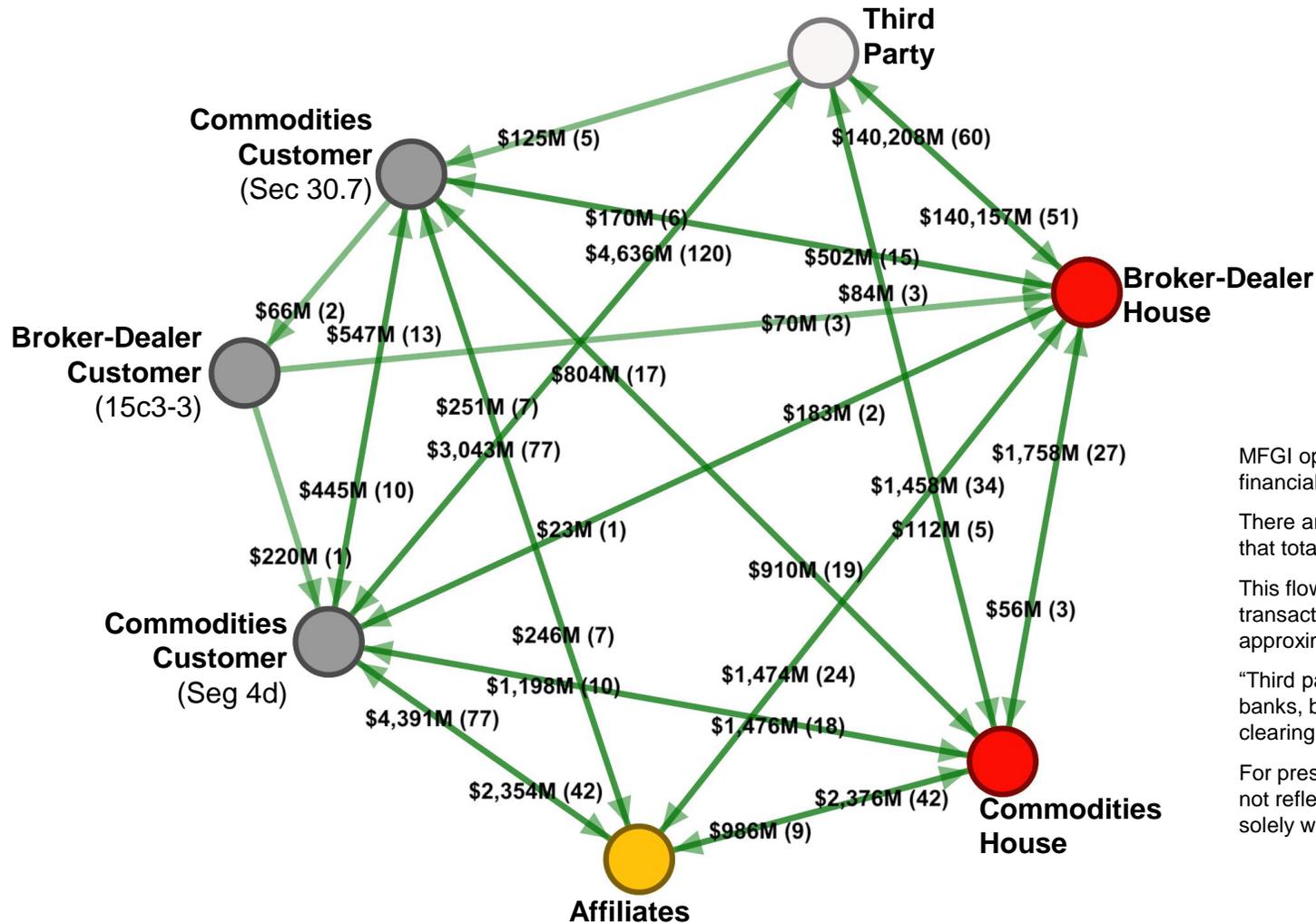
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# **Appendix A**

# Consolidated Overview of Cash Movement MF Global Inc. 10/1 – 10/31



MFGI operated 47 bank accounts held at 8 financial institutions.

There are 840 transactions > \$10 million that total approximately \$327 billion.

This flowchart excludes roughly 20,000 transactions < \$10 million that total approximately \$9 billion.

“Third party” includes customers, lending banks, brokerage firms, exchanges, and clearing agents.

For presentation purposes, this chart does not reflect certain transactions that occurred solely within a related grouping of accounts.

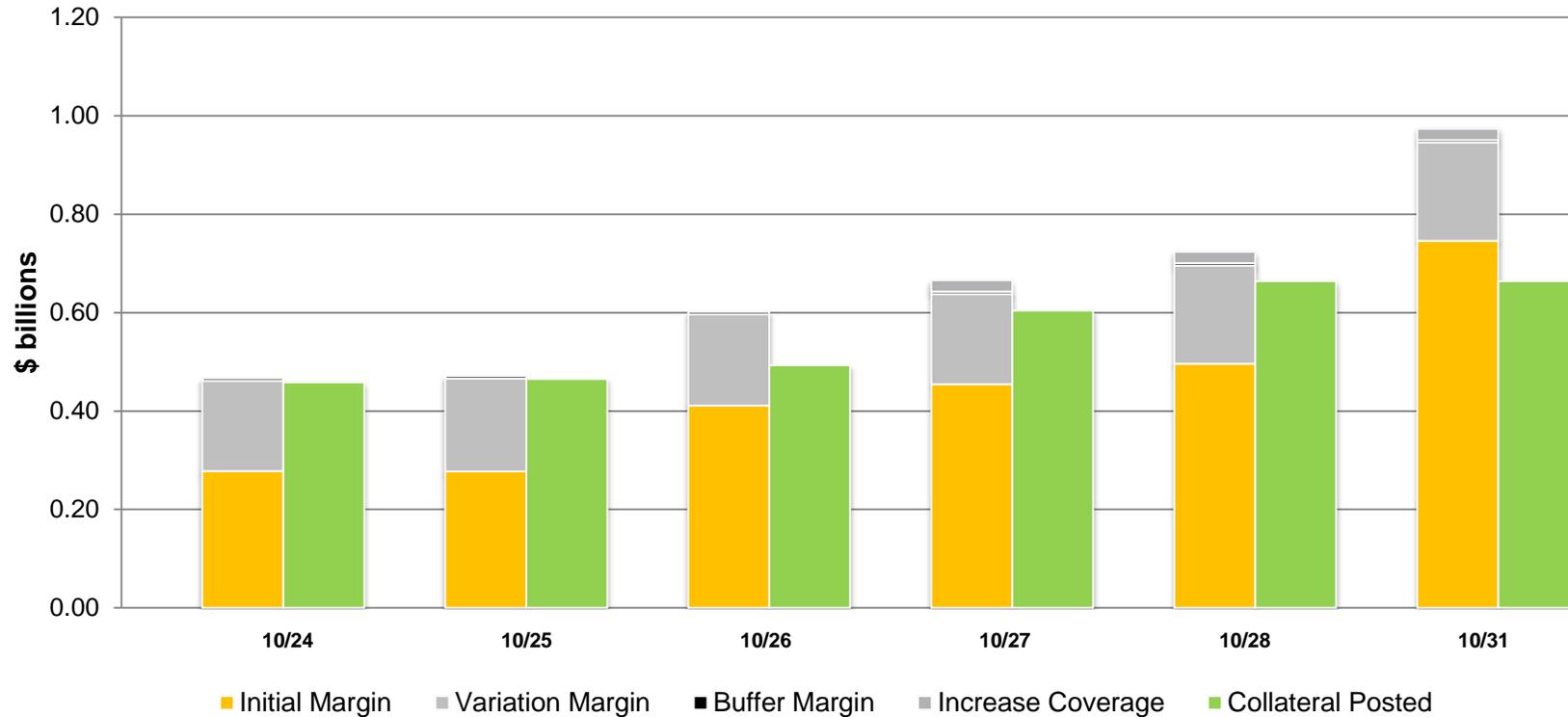
This reflects cash movement only. Investigation is ongoing to trace correlated securities, collateral and other assets.

## Pertinent Liquidity Events 10/24 – 10/31

- ▶ Credit rating downgrade
- ▶ Increased margin calls
- ▶ Funds in segregation: excess turns into deficit
- ▶ Customer liquidations / withdrawals
- ▶ Bonds borrowed program unwind creates liquidity gap of approx \$450 - 500 million
- ▶ Increased draws on both credit facilities:
  - ▶ Unsecured Revolving Credit Facility nearly fully drawn on 10/28 at \$1.17 billion of the \$1.2 billion
  - ▶ Secured facility balance of at least \$130 million of the \$300 million.

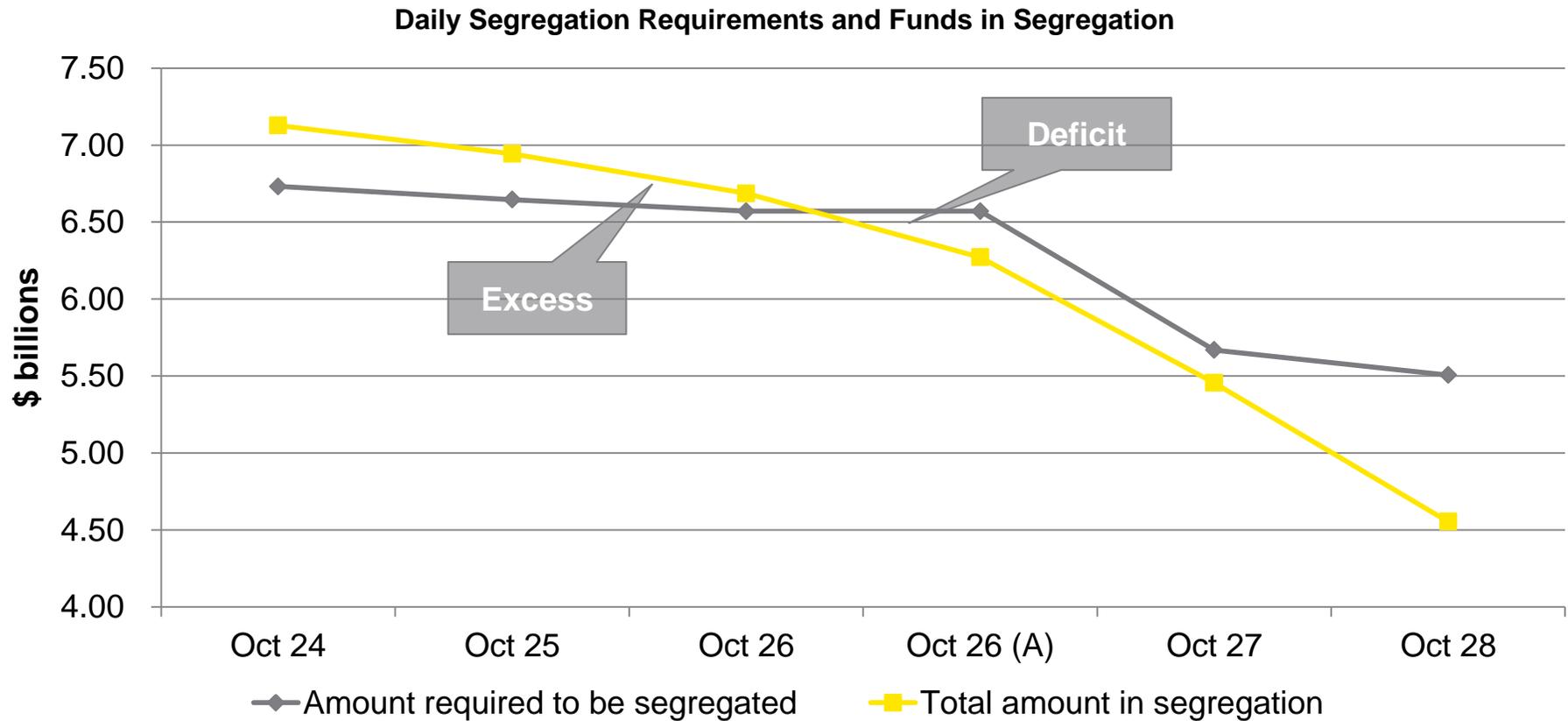
# Increased margin calls

Sovereign Debt Repo To Maturity - Margin Call Trend



<u>Date</u>	<b>Initial Margin</b>	<b>Variation Margin</b>	<b>Buffer Margin</b>	<b>Increase Coverage</b>	<b>Total Margin</b>	<b>Collateral Posted</b>	<b>Margin Call</b>
10/24	278,049,205	182,979,874	5,000,000		466,029,079	457,962,898	8,066,181
10/25	277,302,875	188,277,470	5,000,000		470,580,345	464,694,118	5,886,227
10/26	410,963,534	185,592,415	5,000,000		601,555,949	492,732,015	108,823,934
10/27	454,624,390	182,811,558	5,000,000	23,280,469	665,716,417	604,003,047	61,713,370
10/28	495,975,763	199,344,353	5,000,000	23,219,740	723,539,856	663,925,523	59,614,333
10/31	745,975,763	199,344,353	5,000,000	23,219,740	973,539,856	663,925,523	309,614,333

# Customer funds in segregation: excess turns into deficit



(A) A shortfall in segregated customer funds occurred during 10/26. The calculation originally prepared by MFGI contained an error. Cash deposits in segregated funds bank accounts were erroneously overstated.