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MF Global Customers Have Few Options, Can't Get Cash or Answers

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By Tiffany Kary

Nov. 11 (Bloomberg) -- Ted Monjure, a 48-year-old Manhattan trader who has \$27,252 frozen in a former MF Global Inc. account, said he is considering pulling his money out of his three other trading accounts.

"I'm a high net-worth person, and I don't want to see \$1 million get smoked by another misunderstanding," Monjure said, recounting how he'd thought the Securities Investor Protection Corp. covered any losses due to a meltdown such as that at MF Global. He's now been told SIPC may not cover the money because it was in a futures account and faces months of uncertainty as he files a claim seeking recoveries.

Monjure is one of many customers who can't access cash in the segregated accounts they once thought were safer than bank deposits and just as accessible. Frustrated by a lack of legal options to reclaim frozen funds and dead-end inquiries to call centers and hotlines since MF Global's Oct. 31 bankruptcy, many are not able to trade and say they've lost faith in retail brokerages and the regulatory system.

More than 150,000 customer accounts were frozen Oct. 31, with \$5.45 billion affected, the day after a unit of the New York-based brokerage reported a "material shortfall" in customer funds that are required to be segregated under rules of the U.S. Commodity Futures Trading Commission.

Collapse

MF Global listed \$39.7 billion in debt and \$41 billion in assets and said it has about \$26 million in cash in its Oct. 31 filing. Jon Corzine, the former co-chief executive officer of Goldman Sachs Group Inc., quit as MF Global's CEO on Nov. 4. CFTC Chairman Gary Gensler has recused himself from the agency's investigation.

About \$593 million of MF customer funds are unaccounted for, according to a person with knowledge of regulatory probes into the firm's collapse.

SIPC is a private, government-sponsored company that insures brokerage accounts for up to \$500,000 in securities with \$100,000 for cash in case the brokerage firm goes bankrupt. While SIPC covers losses in stocks and bonds, it doesn't cover commodity futures contracts unless defined as specific property under certain conditions.

While the brokerage's parent, MF Global Holdings Inc., filed for bankruptcy to apportion returns to creditors, a trustee, James W. Giddens, took over to liquidate the brokerage.

Mayhem

MF Global's bankruptcy, the eighth largest ever, is causing mayhem for customers that may exceed that suffered by Lehman Brothers Holdings Inc.'s brokerage customers. Though Lehman's bankruptcy, the largest in U.S. history, sent the world financial system into a tailspin, at least its brokerage customers benefitted from Barclays Plc's takeover of its accounts on Lehman's second day in court.

A transfer of MF Global's accounts to qualified clearing firms began almost immediately, with a lawyer for Giddens saying accounts with open positions would be moved with 60 percent of their collateral, leaving 40 percent to MF Global or other parties who might have legal claim to it. As of Nov. 10, dozens of customers had said they still hadn't gotten their funds, and ICE, or IntercontinentalExchange Inc. had written a letter to the bankruptcy court asking for immediate release of customer cash.

"We didn't think we were just customers," said David Rosen, a 32-year-old energy broker who works at the New York Mercantile Exchange. "We're the ones in the pits providing liquidity so everyone around the world can trade these products."

Organizing

Rosen is organizing exchange members to consider their legal options, and said his group will look to recover money from the bankrupt estate before considering who else they might be able to sue.

The CME said in court papers it has \$2.5 billion of MF Global's total \$5.45 billion in customer segregated funds on deposit. The effect of frozen collateral has already been felt; Volume for agricultural futures contracts traded on the CME and CBOT was 705,273 on Oct. 31, less than the 867,591 30-day average, and down 71,106 from the prior day.

"Though many of the decisions going forward are beyond our control we are working very closely with the regulators and the Trustee to represent our

customers' interests," said CME spokesman Michael Shore.

A stampede to pull funds out of collateral accounts or a boycott of the exchanges could ripple through the markets, affecting farmers as well as hedge funds, said Ashmead Pringle, president of Grain Service Corp., an introducing broker for grain elevator operators who are looking to hedge against price fluctuations with futures contracts. Grain Service Corp. has filed court papers seeking information about MF Global's liquidation on behalf of its clients.

Judge Glenn

Butler has requested that U.S. Bankruptcy Judge Martin Glenn in Manhattan lift the so-called stay that protects companies in bankruptcy from lawsuits and other actions that can let one creditor withdraw money before another. Butler said customers of the brokerage unit should come before all other creditors, as their money was held in supposedly segregated accounts. Butler's request will be heard Nov. 22.

James L. Koutoulas, chief executive of Typhon Capital Management in Chicago, said his fund has lost one client who wasn't a customer of MF Global, and most others are in limbo because their funds -- totaling \$55 million -- are tied up. Koutoulas, a lawyer, is working with Northwestern University law professor J. Samuel Tenenbaum on behalf of any MF Global clients and hopes to put together a group that can seek representation on the five-person creditors committee along with JPMorgan Chase & Co., Wilmington Trust and Elliott Management Corp., all of whom have interests are averse to those of customers.

No, Wait

"If there's a dispute as to whether it's house or client money and five people are saying it's the house's money, we need someone there to say 'No, wait. Maybe it's the client's money and our money is at risk,'" Koutoulas said.

Timothy Butler, a lawyer whose firm filed a lawsuit on behalf of three commodities traders seeking the return of 85 percent of their \$2.5 million in combined frozen funds, said he's taking on new clients and hopes if his suit is successful it will recover that amount for all customers with all-cash accounts. Because the \$593 million shortfall is about 11 percent, customers should be able to get 85 percent back up front, he said.

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Shortfall

Giddens has said he can't release funds immediately because the trustee's job is to distribute assets equally among all customers. Kent Jarrell, a spokesman for Giddens, said the trustee simply doesn't have the authority to make transfers until its teams of forensic accountants have confirmed whether the shortfall is greater or less than \$593 million.

Even when forensic accountants have located money, there may still be disputes among clearinghouses and banks about whose it rightfully is, Jarrell said.

"We can't give out money we won't have at the end of the game," he said.

Legal obstacles to quick recovery of the frozen cash could also include concern about whether some customers aren't entitled to be repaid as much as others, and customers who transferred money out of their accounts prior to the bankruptcy could be subject to clawback rules, Butler noted.

Cash Locked Up

Those like Monjure who liquidated their positions on the day of the Oct. 31 bankruptcy to avoid a drawn-out recovery process, said they feel aggrieved because they had to sell at a loss and can't get any of their cash. Customers who still had open positions have been transferred to new brokerages with about 60 percent of their cash collateral, and now FACE margin calls for the rest, which is locked up at the MF Global accounts.

Jarrell said customers with open accounts were transferred while those with all cash accounts were not because, "moving the open positions could avoid market disruptions and allow customers to have some sort of choice of what to do with the positions."

"We can't distribute cash because we have to know what the amount of segregated cash held for customers is and verify the claims against that pool of segregated cash," he said.

Legal options are less clear for those who have not just frozen cash, but margin calls, Butler said; "people can't understand how the new margin is being calculated. Some people say they're getting less than 60 percent transferred, others say they're getting 80 percent," he said.

Prudence Doesn't Pay

The people who were most prudent are being hurt the worst, said Don Miller, 50, a member of the CME since 2004 who works remotely from his home in the area Boston and has more than \$2 million at risk, including his business and retirement accounts.

"Some people put a little in for margin, those of us who don't believe in excessive leverage put more in for our activity in the course of providing market liquidity than we need," Miller said. "Because of the segregated aspect, that money is supposed to be safer than with a bank."

"My trading business and my life have come to a complete stop," said Miller, who has a \$30,000 college bill for his daughter coming due.

Sacred Cow

The CME reviewed MF Global's accounts the week of Oct. 24, and found them to be in compliance. MF Global didn't report any transfers until early morning Oct. 31, suggesting the firm "made subsequent transfers of customer segregated funds in a manner that may have been designed to avoid detection," said Shore, the CME spokesman.

"The clock's ticking," said Kurt Schacht, managing director in the market integrity division of the CFA Institute, the largest association of investment professionals. "Whether there's a crisis of confidence depends on how this one turns out -- a lot of people in this country view their money in a money market account, at a depository institution as safe and protected."

Schacht, 57, who said he lost money with MF Global, called the experience "humbling" given his role, and his 25 years of trading with MF Global and its predecessor.

Schacht said he hasn't been able to find out what exactly SIPC will guarantee. "There's no one you can actually talk to get it figured out," said Schacht, who described finally getting through to a live person on a hotline only to find they could answer only pre-set questions.

Even with his role in developing ethical standards for investors, Schacht says he doesn't see an easy explanation of what went wrong or how to prevent it from happening again. "I think we need to figure out what happened before we come up with a safeguard against this."

The bankruptcy case is MF Global Holdings Ltd., 11-bk- 15059, U.S. Bankruptcy Court, Southern District of New York (Manhattan). The brokerage case is In re MF Global Inc., 11-ap- 2790, U.S. Bankruptcy Court, Southern District of New York (Manhattan).

--With assistance from Linda Sandler and Matthew Leising in New York. Editors: John Pickering, David E. Rovella

To contact the reporter on this story: Tiffany Kary in New York at tkary@bloomberg.net;

To contact the editor responsible for this story: John Pickering at jpickering@bloomberg.net

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