

# Interview With Commodity Customer Coalition Founder James Koutoulas

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*In a frank interview, industry participant James Koutoulas puts forth the facts from an interesting perspective on MF Global recovery efforts, including tales of questionable legal maneuvers as many on Wall Street and LaSalle Street circle the remains of the one-time industry flagship. Note that this interview reveals discussions that could be considered speculative and opinionated.*

**Opalesque Futures Intelligence:** We are with James Koutoulas from Typhon Capital Management in Chicago. James runs the Commodity Customer Coalition, which is recovering MF Global client funds on a pro-bono basis. James, tell me how your efforts have been received and what are some of the roadblocks you are encountering?

**James Koutoulas:** The efforts are received just very positively from the firm's customers. I cannot tell you how emails and tweets I am getting every day just thanking us for our efforts. However, members of the "bankruptcy club," I do not think are so positive. Usually, these other attorneys and banks can just rush into the bankruptcy court before anybody knows what is going on and get liens and super-priorities slapped on stuff, get money paid out to their clients, and get their legal fees accruing. So, not only are we challenging the financial industry and guys like Corzine, but we are also challenging the bankruptcy court establishment.

**OFI:** There are a few voices making claims the MF Global incident could actually bring down the futures and options model. How do you respond?

**JK:** Well, I mean, honestly there is not enough information for us to go that far – but, I think, this is a real negative for the industry. I think that the model of account segregation is a good one, but it needs to be maintained. Any system can be broken somehow, that is why we have criminal laws. If it is found that Corzine and the other MF Global Directors committed an illegal act and they violated the system then those guys need to go to jail. It's not fair to say that any time someone commits a crime, the whole system is bad. It just means that we need to actually punish those who break the existing laws that we have.

**OFI:** Great point. The system cannot eliminate criminal fraud, what it can do is to protect against it and help identify it. It is not like the regulators are sitting in the offices of MF Global watching every single trade and every single money transfer that transpires, that is irrational.

**JK:** That's right.

**OFI:** You mentioned jail. Assuming that he committed criminal acts, what do you speculate as to the odds of people going to jail?

**JK:** As long as I'm still breathing I suppose that is really high, because it is my sworn mission, if he did something illegal, to do everything I can to make sure he is prosecuted and goes to jail.

**OFI:** You share a lot of the sentiment from people I speak with in the futures and options industry. But let us talk about some of the contagion this might have. How do you see this damage spreading elsewhere, do you see any impact on the Chicago Mercantile Exchange (CME)? There has been some talk the CME may be liable for the shortfall.

**JK:** The CME could be in a lot of trouble here. They are one of the regulators in charge of watching MF Global whilst they proclaim on their website that customers never lost a penny in segregated funds and that their seg accounts are safe. They have never explained any risks of comingling or fraud or anything like that. So, they have reaped all the benefits from customers believing in the

sanctity of seg funds so it only goes to stand that if you advertise something, you benefit from it and you do not disclose all the risks then you have got liability there. There is stock price is really changing. I mean they are down something like 40 points or over two billion in market cap since the day before the bankruptcy. At the end of the day, if customers do not feel safe in segregated accounts then futures volumes are going to dry up. So, it is definitely going to hurt the CME and it is definitely going to hurt guys like us who are your commodity traders.

**OFI:** Do you see the contagion spreading past the exchanges in any other directions?

**JK:** If you look at the other end the stock price is out there. No one is really sitting pretty. You already have a tough environment for brokers with no ability to raise commissions rates and little ability to make money off the float after about three-and-a-half years with zero interest rate policy, the Fed has come out saying we are essentially Japan.

**OFI:** Fascinating because the FCM business models I have always looked at shows float (interest income) on an FCM's balance sheet often representing about a third of the income.

**JK:** Right. Zero interest rate policy that Bernanke is so enamored with has put all of the brokers in a tough position where they have to just barely get by or really chase yield aggressively.

**OFI:** It's a tough environment, and that likely lead to MF Global's move to more aggressive yield. So, let us talk about that, because there have been a number of theories floating around in the industry and so a lot of the whispers you hear that essentially trying to speculate on what happened with MF Global. I have heard one reasonably credible theory the collateralization issue that everyone was talking about so much. If you can speculate, describe to me what you think happened with the funds?

**JK:** That is really hard to say, especially on the record given that I do not really have access to the kind of information I need to make an informed statement there, so I would just stick with what I have seen from the press, which is that there are strong indications of illegal activity here. And, it is one thing to just take seg funds overnight and invest them in some way that may be a little bit more aggressive. But it's a whole different thing if you are not meeting your collateral requirement and you are shifting things around on balance sheets to give the appearance that you are better collateralized than you actually are.

**OFI:** One of the whispers that you tend to hear is that on Friday, before the bankruptcy, the money was in segregated accounts; on Monday, it had moved from a CFTC regulated segregated account into an equity's brokerage account, have you heard anything relative to that or can you comment at all?

**JK:** I have heard that rumor I have also heard conflicting rumors. I have heard rumor that it is in an OTC account. I have heard rumors that they put it on the outside of the balance sheet, and there are as many theories out there as anybody could dream of, but I'd rather wait for firm facts before we start to speculate on where exactly it went with any degree of accuracy.

**OFI:** What do you think the prospect is for people getting their money out? What is the percentage chance you think that all customers are going to be made whole on this one?

**JK:** I honestly think it is a pretty high percentage. I think before we started the CCC, it was a pretty low percentage, but I think that we are making enough noise and we have enough talented lawyers working on this, that we stand a pretty good shot to make things right for customers in court. Let us not forget that while there may possibly be a \$1.2 billion shortfall on MF Global customer Seg accounts, there are about \$40 billion in assets in the MF Global Holdings estate. There are people still buying MF Global stock, and think the shareholders are going to get paid, and for shareholders to get paid, customers have to get paid and so do all the secured and unsecured creditors.

**OFI:** In terms of liquidating MF Global assets in a bankruptcy, clients invested in segregated accounts would be at the top of the list and shareholders would be at the bottom?

**JK:** That is right.

**OFI:** Using simple logic, it seems to me as long as the lawyers do not get in there with their \$800 an hour hands and eliminate the \$40 billion in assets, it might be reasonable to assume there is an extremely good chance investors get their seg funds back,

particularly when you throw the CME guarantee on top. What kind of timeframe do you think a customer would be getting their capital back?

**JK:** It really depends. There are a lot of interests represented in this case that are adverse to customers, and the Trustee gets paid hourly and is thus incentivized to make the process take as long as possible. We have raised a lot of these issues and advised the Trustee on technologically-based solutions. The judge has been very receptive to that. I think my read on the judge is he is a honorable man, he cares about the customers, he wants the customers to get paid as soon as possible. I think we are going to see everybody get a at least 60% of their money back by early December, and I think with the CME upping their guarantee to \$550 million, 75% is reasonable before Christmas. I think that is a good start and now the rest of it is going to depend on really how the court plays out the next couple of weeks. We are creating an ad hoc committee to give a voice to customers in the bankruptcy proceedings and we will continue to advocate that I be added to the creditors committee in the holding company case. If the judge allows me on the committee, then customers will have an advocate to stand up to the guys like JP Morgan, Bank of America and Elliot Systems, all three of whom are buying investors claims. They give investors money upfront in order to get paid in full once the customers are paid out of the estate. The numbers we're being offered right now are about 85 cents on the dollar.

**OFI:** Interesting. Now, I have heard that JP Morgan is asking for some priority treatment here. What's going on?

**JK:** The first thing we filed in this case was an objection to JP Morgan's order for the use of cash collateral, which on its face seems to be a pretty innocuous order. But, if you read it really carefully, basically what they are trying to do is say in order to concede to an extension of an \$8 million credit line for the holding company to continue to operate during the transfer process, they potentially get super-priority rights slapped on all sorts of things, including assets that go behind the holding company case. They created a new definition of the word "Company", which is generally just used like an abbreviation, where they snuck in language that would allow them to include the broker dealer entity into this definition. This was not defined anywhere else in the motion and if you include the broker there then that would essentially allow them to cut in line ahead of customers.

**OFI:** Is that common in such legal cases for that to occur?

**JK:** I honestly do not know how common it is, but I have heard that this particular lawyer who drafted the motion, does this all the time. Our co-counsel had worked with him in the past and knows to be on the look out for something tricky, so we are fortunate enough to have an attorney who knew what he was looking for or we probably would have missed it along with everybody else.

**OFI:** Is there any news I should be watching or what should I be paying attention to here that is going to kind of indicate which way this thing is going to break?

**JK:** Honestly, I think probably our recaps from tomorrow. Tomorrow is looking like it is going to be a big showdown, you have got the Trustee who does not want us to be involved in the process. I have the feeling that I think the judge does. I think the judge senses that I am working pro bono, we are doing this for the right reasons, we are trying to make the customers whole, so if the judge lets us on the committee the next day in court and if they want a customer voice in the claims process that will be a huge win for the customers.

**OFI:** Fascinating James. Best of luck with all your efforts.