

**STATEMENT OF DIANE GENOVA
BEFORE THE UNITED STATES HOUSE OF REPRESENTATIVES
COMMITTEE ON FINANCIAL SERVICES
OVERSIGHT AND INVESTIGATIONS SUBCOMMITTEE**

MARCH 28, 2012

Chairman Neugebauer, Ranking Member Capuano, and Members of the Subcommittee, good afternoon. My name is Diane Genova. I am the Deputy General Counsel for the investment bank of JPMorgan Chase & Co. I am pleased to appear this afternoon on behalf of J.P. Morgan in order to describe for you certain of the interactions J.P. Morgan had with MF Global before MF Global filed for bankruptcy protection on October 31, 2011. I appreciate the opportunity to appear before the Subcommittee.

As I will describe in more detail, J.P. Morgan professionals worked very hard throughout the week of October 24 to accomplish two main goals: first, we took what we believed were appropriate and prudent steps, as part of maintaining safe and sound banking operations, to ensure that we did not wind up in a position where we had extended credit to MF Global without proper collateral and security protections; and, second, our professionals simultaneously worked very hard that week to provide first-rate operational clearing and settlement support and services to MF Global. With those goals in mind, J.P. Morgan also sought to collect as much information as we could from MF Global about its liquidity situation under what were very difficult, rapidly changing circumstances. We were always mindful that despite our best efforts, there was a lot going on inside MF Global during that week that we were not seeing and could not see.

BACKGROUND

To understand what we were trying to accomplish that week, it may be helpful to describe briefly the banking services that J.P. Morgan (along with numerous other financial institutions)

provided to MF Global. These are fairly standard services that clearing banks typically provide to support the day-to-day broker-dealer and futures commission merchant (“FCM”) operations of firms like MF Global.

First, MF Global maintained a large number of cash demand deposit accounts (much like a retail checking account) both at J.P. Morgan and at several other banks to support its operations in the United States, Europe and Asia. Four of the accounts MF Global maintained with J.P. Morgan in the United States were designated as customer segregated accounts, and these accounts generally contained funds belonging to customers as well as funds belonging to MF Global itself, as permitted by the relevant CFTC regulations.

Second, MF Global used both J.P. Morgan and Bank of New York Mellon (“BONY”) for clearing services. When MF Global cleared U.S. Treasury securities, it did so through BONY. It cleared Federal Government Agency securities (*e.g.*, Federal Home Loan Bank securities) through J.P. Morgan.

Third, well before the week of October 24, MF Global had negotiated for and put in place two committed revolving credit facilities in which J.P. Morgan was the administrative agent for two large groups of other banks. The first of these was a \$1.2 billion committed line of credit that MF Global was entitled to draw upon without having to post any collateral — in other words, it was unsecured. And, as I noted, J.P. Morgan was the administrative agent for a total of 22 other banks, with Citibank and Bank of America serving as the syndication agents for the bank group. The other revolving credit facility was a \$300 million committed line that MF Global was entitled to draw upon, but only if it first properly posted certain eligible securities (*e.g.*, U.S. Treasuries and Federal Government Agency bonds) as collateral for the loan. J.P. Morgan served as administrative agent for a syndicate of nine other banks, including Harris Bank, Citibank and Bank of America.

With regard to the \$1.2 billion unsecured facility, MF Global had drawn down, prior to the week of October 24, a total of \$367 million from that facility, and then, during the week of October 24, MF Global drew down an additional \$805 million, for a total outstanding loan balance of approximately \$1.17 billion. J.P. Morgan had promptly funded these draw requests by MF Global to the full extent of its individual commitment (which was \$73.5 million); during that week, however, certain other financial institutions who were members of the bank group either delayed their funding or did not provide funding at all to MF Global.

Finally, long before the week of October 24, MF Global had entered into securities lending and repurchase arrangements with J.P. Morgan, the largest of which involved MF Global borrowing U.S. Treasuries from J.P. Morgan's securities lending clients in exchange for posting U.S. Government Agency securities as collateral. Shortly before MF Global filed for bankruptcy, it had been borrowing approximately \$5.3 billion worth of U.S. Treasuries every night through this securities lending arrangement.

WEEK OF OCTOBER 24

With that brief background, let me now turn back to the events of the week of October 24, 2011. Early that week, it became clear that MF Global was in some degree of distress and there had been a number of negative public announcements about the company — for example, on Monday, October 24, Moody's downgraded MF Global's credit rating to the lowest investment-grade level, and on Tuesday, October 25, MF Global announced a large quarterly loss and suffered a sharp drop in its stock price thereafter. Despite those developments, J.P. Morgan continued to provide to MF Global the standard array of banking and financial services described earlier.

On Thursday evening, October 27, Moody's publicly announced that it was downgrading MF Global by two notches to below investment grade. As a result, late on Thursday evening, J.P. Morgan professionals began the process of putting all MF Global accounts on what is called "debit alert" and advising personnel at MF Global that we were doing so. A debit alert is a standard step that banks take when a customer is in financial distress. It mandates that no transfers of funds requested by the customer will be executed unless the bank determines that there are "good funds" present in the account to be debited that are adequate to support the requested transfer. As part of this debit alert process, J.P. Morgan also suspended all of MF Global's uncommitted intra-day credit lines.

That same evening, we agreed with MF Global to send a J.P. Morgan team to MF Global's New York City offices on Friday, October 28, to assist MF Global with its ongoing efforts to unwind its securities lending arrangements, including the unwinding of numerous repurchase transactions and the sale and purchase of large amounts of securities held by MF Global. We understood that these activities were being done by MF Global to generate as much liquidity as possible, in order to meet requests for more margin from various clearing houses, requests from its customers to withdraw funds (in circumstances where such funds were being held by MF Global in permissible securities investments), and requests for more collateral from MF Global counterparties. By unwinding its securities lending arrangements, MF Global was able to regain access to the securities it had posted as collateral, and thus was able to sell those securities and thereby generate additional liquidity and deleverage its balance sheet.

Separately, on the morning of Friday, October 28, as a result of the heightened level of attention to MF Global transfers and balances dictated by the debit alert, J.P. Morgan determined that there were overdrafts in certain of the foreign-exchange clearing accounts maintained by MF Global's U.K.-based affiliates. We promptly advised the Chairman and CEO of MF Global Holdings Ltd., Jon

Corzine, and others at MF Global of these overdrafts and were assured that any overdraft would be covered. It was especially important to both MF Global and J.P. Morgan that the overdrafts be covered because J.P. Morgan had agreed to facilitate a broad auction to multiple market participants of approximately \$4.9 billion in government agency and corporate bonds as a way to assist MF Global in its ongoing effort to generate liquidity. J.P. Morgan had offered, as part of its ongoing support for MF Global, to take the unusual step of providing same-day liquidity as to any such sales in which J.P. Morgan acted as agent on MF Global's behalf with respect to securities actually custodied at J.P. Morgan. This measure would provide MF Global with liquidity on the fastest possible basis, and certainly far faster than the typical one to two business days for regular way settlement of such securities trades. However, as MF Global understood, J.P. Morgan was unwilling to take this unusual step if MF Global's overdrafts were not addressed. Thus, when this was raised with Mr. Corzine on Friday morning, he readily agreed that it was important for MF Global to cover the overdrafts, and he assured J.P. Morgan executives that MF Global had ample funds to cover the overdrafts and that they would be covered promptly.

J.P. Morgan management was able to confirm by about 11:00 AM on Friday, October 28, that MF Global had transferred sufficient funds to its U.K. affiliate to cover the London overdrafts. J.P. Morgan also noticed that MF Global had done so through a series of two transfers. The first was a transfer of \$200 million from an MF Global account in the U.S. designated as a customer segregated account to an MF Global account in the U.S. designated for MF Global's own funds. The second was a transfer of \$175 million from that MF Global account in the U.S. to another MF Global account in London also designated for MF Global's own funds. The customer segregated account from which MF Global had withdrawn \$200 million had an opening balance on Friday of approximately \$1.32 billion. After further internal review and discussion, J.P. Morgan determined that under the circumstances, including the financial stress facing MF Global and the fact that the transfers had been made to cover

overdrafts in MF Global accounts maintained at J.P. Morgan in the U.K., it would be prudent and appropriate to ask MF Global to confirm that these transfers had been made in compliance with the CFTC rules governing customer segregated accounts.

It is important to note that in seeking such assurances and as background to making this request, J.P. Morgan understood it is common industry practice for FCM firms such as MF Global to maintain substantial amounts of their own funds within their customer segregated accounts. This is typically done by FCM firms in order to serve as a cushion and ensure that adequate funds are always maintained in such accounts and to facilitate day-to-day operations. J.P. Morgan also understood that the relevant CFTC rule — CFTC Rule 1.23 — permits an FCM firm to add its own funds to customer segregated accounts to ensure that such accounts do not become “undersegregated.” Rule 1.23 also expressly permits an FCM firm to “draw upon such segregated funds to its own order” and do so to the full extent of the FCM firm’s “actual interest therein.” Indeed, when the CFTC amended these rules in August 1997, it specifically explained the reasons for this common industry practice:

[M]aintaining an adequate cushion of its own in segregation is a part of routine FCM funds management operations. FCM operational funding needs often dictate that any unneeded excess funds in segregation be moved so that they can be used in other aspects of the firm’s operations. Therefore, prudent and efficient funds management typically requires an FCM to make frequent transfers of funds into and out of segregation.

Securities Representing Investment of Customer Funds Held in Segregated Accounts by Futures Commission Merchants, 62 Fed. Reg. 42398 (Aug. 7, 1997).

We also understood that FCM firms such as MF Global are required each day to calculate the amount of actual customer funds they are holding and the total amount of such funds on deposit in segregated accounts, and if they determine at any point they are undersegregated, they must

promptly notify their designated self-regulatory organization (*i.e.*, the CME) and the CFTC. J.P. Morgan and other depository institutions do not receive these FCM calculations or regulatory notifications.

Thus, around early to mid-afternoon on Friday, October 28, J.P. Morgan reached out to Mr. Corzine to explain J.P. Morgan's understanding of how the London overdrafts had been covered by a series of transfers originating with a withdrawal of funds from a customer segregated account, and to ask that MF Global confirm in writing that the funds it had transferred represented its own funds and thus that it was entitled to withdraw them pursuant to CFTC Rule 1.23. Mr. Corzine said he understood the request and would have someone within his organization review it. J.P. Morgan thereafter e-mailed a proposed draft letter to Mr. Corzine. That initial draft asked MF Global to confirm that all transfers made at any time from its customer segregated accounts to any of its own accounts represented MF Global's "actual interest in such funds according to CFTC Regulation 1.23." Knowing it had been a busy week for MF Global, we thought that our request would help to focus the attention of appropriately senior MF Global officials. In retrospect, events appear to have overtaken MF Global during the weekend before it filed for bankruptcy, and, as a result, the letter was not signed. Nevertheless, our request did result in our receiving multiple clear oral assurances from senior MF Global officials that MF Global was in compliance with its obligations under the CFTC rules.

Later on Friday, after not hearing back about the letter, we placed a call to the office of Laurie Ferber, the General Counsel of MF Global, but we wound up speaking with Ms. Ferber's deputy general counsel, Dennis Klejna. We understood Mr. Klejna to be a former Head of the Enforcement Division of the CFTC and someone who had a reputation in the FCM industry as an expert in the relevant CFTC rules and regulations. We explained to Mr. Klejna that we hoped to get the letter sent earlier that day signed and were calling to check on the status of the letter. In response, Mr. Klejna told us that the transfers made that day by MF Global out of its customer segregated account had been done in

compliance with the CFTC rules and represented excess funds belonging to MF Global. Mr. Klejna stated that his only concern about the letter was that our proposed draft appeared to him to be overly broad in that it referred to all transfers that had ever been made out of these accounts, which, as he pointed out, would have necessitated a time-consuming administrative burden to review all such transactions. He therefore asked that we narrow the letter to focus solely on the transfers executed on October 28. Mr. Klejna closed by saying that he needed to consult with Ms. Ferber about getting a narrowed form of the letter signed. A revised version of the letter — focusing only, as Mr. Klejna had suggested, on the transfers from October 28 — was e-mailed to Mr. Klejna around 6:30 PM that evening.

The next day, Saturday, October 29, we arranged to speak by telephone at around 2:30 PM with both Ms. Ferber and Mr. Klejna. Much as we had done the evening before, we began this call by saying that we were calling to check on the status of the (now revised) letter. Among other things, Ms. Ferber assured us in substance that MF Global understood the relevant CFTC rules, that MF Global knew how to properly maintain customer segregated accounts, that the transfers on Friday, October 28 that we had inquired about represented a withdrawal of MF Global's own funds held in a customer segregated account, and that we therefore did not need to be concerned. After some further discussion about how we could more specifically focus the draft letter on the series of transfers on the morning of Friday, October 28 that had initially triggered J.P. Morgan's request for assurances from MF Global, Ms. Ferber told us that she would arrange to have such a revised letter signed. Ms. Ferber was known by J.P. Morgan to have an outstanding reputation for expertise in the securities and FCM industry.

In accordance with this 2:30 PM telephone conversation on Saturday afternoon, my colleagues sent a further revised version of the letter to Mr. Klejna a little after 5:00 PM that day. As the Committee is already aware, we never received the executed letter back from MF Global. Neither I nor to the best of my knowledge anyone else from J.P. Morgan ever had any further communications with

anyone at MF Global about the letter. But we certainly were never told that any MF Global personnel were refusing to sign the letter or that MF Global would not provide us with a signed letter. As I noted earlier, we fully expected to receive a signed letter after we spoke with Ms. Ferber. When the letter did not arrive on Sunday, October 30, our belief was that, given all that was happening at MF Global that day, they simply had numerous pressing matters to attend to that prevented them from turning their attention back to our letter. We had no reason to doubt the clear oral assurances we had been given on Friday and Saturday.

CONCLUSION


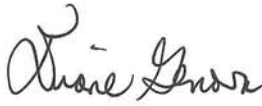
J.P. Morgan sought to support the clearing and settlement operations of MF Global during a very challenging and difficult week, and to do so in a prudent manner so that J.P. Morgan did not inadvertently extend credit to MF Global without adequate and appropriate protections and MF Global could continue to serve its customers.

Thank you again for the opportunity to make this statement. I hope it has been helpful and I would be happy to answer any questions the Subcommittee may have.

United States House of Representatives
Committee on Financial Services

“TRUTH IN TESTIMONY” DISCLOSURE FORM

Clause 2(g) of rule XI of the Rules of the House of Representatives and the Rules of the Committee on Financial Services require the disclosure of the following information. A copy of this form should be attached to your written testimony.

1. Name: Diane Genova	2. Organization or organizations you are representing: J.P. Morgan
3. Business Address and telephone number: 	
4. Have <u>you</u> received any Federal grants or contracts (including any subgrants and subcontracts) since October 1, 2008 related to the subject on which you have been invited to testify? <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No	5. Have any of the <u>organizations you are representing</u> received any Federal grants or contracts (including any subgrants and subcontracts) since October 1, 2008 related to the subject on which you have been invited to testify? <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No
6. If you answered .yes. to either item 4 or 5, please list the source and amount of each grant or contract, and indicate whether the recipient of such grant was you or the organization(s) you are representing. You may list additional grants or contracts on additional sheets. 	
7. Signature: 	

Please attach a copy of this form to your written testimony.