The Restructuring Review of the Americas 2019

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Global Restructuring Review is a leading source of news and insight on cross-border restructuring and insolvency law and practice, read by international lawyers, insolvency practitioners and accountants, judges, corporate counsel, investors and academics.

We deliver on-point daily news, surveys and features that give our subscribers the most readable updates and analysis of all the cross-border developments that matter, allowing them to stay on top of their game even more so than they already are.

In the past couple of years, we have published exclusive interviews with bankruptcy judges around the world, unearthed nuggets from court hearings that other news services missed, released several original surveys – including on the experiences of female professionals working in restructuring – and features such as a comparative study looking at current restructuring strategies in the retail sector. Our newly introduced Worked Out series, profiling key jurisdictions around the world, has so far published profiles on Singapore, Ukraine and Delaware, with the Cayman Islands, Hong Kong and China still to come. Our book-length *Art of the Ad Hoc* guide gathers the wisdom and perspectives of some of the leading practitioners in the area of ad hoc committees in restructurings.

Complementing our news and magazine coverage, *The Restructuring Review of the Americas* provides exclusive thought leadership, direct from pre-eminent practitioners. The *Review* gathers the expertise of 19 leading figures from 12 different firms in eight jurisdictions. Contributors are vetted for international standing and knowledge of complex issues before being approached.

In this volume we have expanded our coverage in the United States. In addition to an overview of Chapter 11 of the US Bankruptcy Code, our expert panel also reviews hedge fund and private equity fund participation and some of the investment strategies that funds continue to adopt to maximise their returns. Chapter 15 is discussed in two chapters: first, a full review of Chapter 15 as a tool providing effective mechanisms for dealing with cross-border insolvency cases and looking at whether it remains a welcoming destination for foreign debtors; second, a look at the limits of Chapter 15 with specific consideration to the high burden parties must overcome to invoke section 1506 of the Bankruptcy Code, which allows courts to refuse to take action on public policy grounds.

Furthermore, our panel provides an overview of the bankruptcy law in Argentina and considers criticisms made against Brazil's restructuring legislation and the proposed amendments suggested in May 2018 to revamp corporate restructuring in the country. We also review the broad and flexible restructuring options available in Canada; offshore restructuring in the Bahamas; and the Concurso Law in Mexico, explaining why it has not provided a feasible and efficient restructuring procedure for companies in financial distress. Additionally, our experts in Chile consider the flaws of the local regime, while our panel in Venezuela assesses the current regime, which lacks a statutory concept of insolvency, in the face of widespread economic instability.

The *Review* is annual and will expand with each edition. If you have a suggestion for a topic to cover or would just like to find out how to contribute please contact mahnaz.arta@globalrestructuringreview.com.

GRR would like to thank all our contributors for their time and effort.

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US – How Foreign is Too Foreign? Extraterritorial Limits on the Recovery of Fraudulent Transfers

Timothy Graulich and Elliot Moskowitz*
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Introduction

Section 550(a)(2) of the US Bankruptcy Code allows a trustee to recover property that is the subject of an avoided transfer from 'any immediate or mediate transferee' of an initial transferee. Whether this power to recover extends to property that was transferred from a foreign initial transferee to a foreign subsequent transferee has long been an unresolved question. In recent years, several courts have weighed in on the question, clarifying and refining the framework for answering it with respect to individual transfers in specific cases. While the recent case law has provided more guidance to litigants, several open questions remain. In this chapter, we discuss the current landscape with respect to the application of section 550(a)(2) to foreign-to-foreign transfers, how a recent Second Circuit decision has altered the terrain, and the questions that remain unanswered.

The basic question: how do Code sections 550(a)(2) and 541 interact?

Under Code section 541, 'property of the estate' is defined expansively to include certain categories of property 'wherever located and by whomever held'. These categories of property include '[a]ny interest in property that the trustee recovers under [section 550]'. Section 550(a)(2) allows a trustee to 'recover, for the benefit of the estate', property transferred to 'any immediate or mediate transferee' of an initial transferee, 'to the extent that [the] transfer is avoided' under one of several avoidance sections provided elsewhere in the Code.

Trustees in a number of bankruptcy proceedings have argued that their recovery powers under section 550(a)(2) extend to property that was the subject of an overseas (or foreign-to-foreign) transaction. To support this argument, these trustees have generally either relied on the broad definition of 'property of the estate' in section 541, or on the notion that this type of transaction, in certain instances, should be considered 'domestic', so that recovery of the assets transferred would not require extraterritorial application of the Code section in the first place.

The pre-Madoff framework: Maxwell, French and Morrison

In re Maxwell[1]

The seminal *Maxwell* case cemented comity and a presumption against extraterritoriality as the twin principles guiding US courts addressing the extraterritorial reach of US insolvency law. The case involved an English debtor corporation, and centred on a series of transfers by foreign transferors to foreign recipients that were otherwise avoidable under section 547. The Bankruptcy Court for the Southern District of New York declined to permit recovery of these transfers, reasoning that 'neither the language nor legislative history of section 547 or the bankruptcy code as a whole evinced Congress's intent to apply section 547 to conduct occurring outside the borders of the U.S.' On appeal, the district court endorsed the bankruptcy court's analysis, but held that, separate and apart from the presumption against extraterritoriality, principles of international comity counselled against extraterritorial application of the US Bankruptcy Code.

The district court began by recognising that the presumption against extraterritoriality 'is a longstanding principle of American law that legislation of Congress, unless a contrary intent appears, is meant to apply only within the territorial jurisdiction of the United States'. The presumption 'serves to protect against unintended clashes between our laws and those of other nations which could result in international discord'. The court articulated a 'two-fold inquiry' for application of the presumption: '[f]irst, a court must determine if the presumption applies at all'; in other words, the court must determine whether the 'conduct [at issue] occurred outside of the borders of the U.S.' If the court determines that the presumption applies, it then must determine whether 'Congress intended to extend the coverage of the relevant statute to such extraterritorial conduct'.

The court determined that the transactions at issue 'clearly' occurred overseas, but it declined to rest this decision solely on the basis that the transfers were made from and to bank accounts located outside of the United States. It noted that 'such a limited conception of "transfer" for purposes of an extraterritoriality analysis would have potentially dangerous implications', because a creditor seeking to have a transfer characterised as extraterritorial 'could simply arrange to have the transfer made overseas'. Instead, the court noted, the analysis requires a consideration of 'all component events of the transfers'.

In performing the analysis, the court determined that the transferors and transferees were all foreign entities, whose relationships were 'centered in England'. The debts underlying the payments had been made and maintained in England, and were governed by English law. The only connection to the US was that the payments represented proceeds from a sale of US assets, a sale that depleted the bankruptcy estate. The court dismissed the importance of this connection, however, holding that the sale was 'more appropriately characterized as a preparatory step to the transfers'.

The court implicitly left open the possibility that the presumption might not apply to foreign defendants who subjected themselves to the equitable claims adjustment process by submitting a proof of claim. It declined to make such a finding in this case because, although the foreign defendants had submitted proofs of claim, they had done so only in a parallel proceeding in England.

Having determined that the transfers at issue were extraterritorial, the court turned to the second step of its inquiry: whether Congress intended section 547 of the Bankruptcy Code to apply extraterritorially. It stated that a statute will not be applied extraterritorially 'unless the affirmative intention of the Congress to apply the law extraterritorially is clearly expressed in the statute' and that 'any ambiguity in the statute must be resolved in favor of refusing to apply the law to events occurring outside U.S. territory'.

The court declined to find Congressional intent to apply section 547 of the Bankruptcy Code extraterritorially. First, it rejected an argument that extraterritoriality was implied by the words 'any transfer' in section 547, explaining that this type of 'boilerplate language' is 'insufficient to overcome the presumption against extraterritoriality' and noting that the parties had not pointed to any legislative history

that would alter this conclusion. Next, it rejected an argument that the definition of 'property of the estate' in section 541 (to include property 'wherever located') mandated extraterritorial application, reasoning that property is not 'property of the estate' until after it has been recovered.

Having concluded that section 547 could not be applied extraterritorially, the court offered comity as a separate and independent ground to block recovery of the transfers at issue in the case. It noted that '[c]omity is wholly independent of the presumption against extraterritoriality and applies even if the presumption has been overcome or is otherwise inapplicable'. Since the transfers at issue 'occurred in England on account of debt incurred there', and 'most creditors [of the overseas transferor] are English', the court held that 'the effect on U.S. creditors of the transfers is outweighed by the effects of the transactions in England'.

In re French[2]

A decade later, the Court of Appeals for the Fourth Circuit in *In re French* applied the analysis laid out in *Maxwell* to the transfer of real estate located in the Bahamas, but reached the opposite conclusion:

- recovery of the property at issue, although its transfer took place abroad, did not require extraterritorial application of the recovery statute;
- in any event, Congress intended the recovery statute to be applied extraterritorially; and
- comity did not bar recovery of the transferred property.

The subject property was a house in the Bahamas that had been transferred by the debtor to her children, as a gift, at a time that the debtor was already insolvent.[3] The court noted that both the debtor and her children were located in the United States; that the decisions to transfer the property and to make the transfer a gift had also been made there; and that recordation of the deed in the Bahamas was 'at most incidental' to the conduct regulated by the fraudulent-transfer statute. The court concluded that the transfer of the house was therefore a domestic transfer, so that its recovery did not require extraterritorial application of any Bankruptcy Code section.

The court did recognise that the Bahamas had a 'powerful interest' in real property within its boundaries – an interest that 'perhaps merits special weight in the balancing test'. However, the court determined that it did not need to 'resolve this slippery question' because even if recovery of the property required extraterritorial application of the Bankruptcy Code, there was sufficient evidence of congressional intent favouring such application that the presumption against extraterritoriality was rebutted. Acknowledging the existence of a circuit split regarding the question, the court sided with Fifth Circuit precedent to hold that the 'property of the estate' includes property that would have been property of the estate but for the fraudulent transfer. It then reasoned that the definition of 'property of the estate' in section 541 (which includes property 'wherever located') 'demonstrated an affirmative intention [by Congress] to allow avoidance of transfers of foreign property that, but for a fraudulent transfer would have been property of the debtor's estate'.

Finally, the court determined that comity would not block recovery of the Bahamian property. It rested this decision on a determination that it would be more appropriate to apply US law to the transfer than Bahamian law: most activity surrounding the transfer took place in the US, almost all the parties with an interest were located in the US, and the debtor had a strong connection to the US. In addition, because no parallel insolvency proceedings were taking place in the Bahamas, there was no risk of conflicting judicial opinions. The court concluded that 'applying Bahamian law here would undercut the purpose of the United States Bankruptcy Code by withdrawing its protections from those it is intended to cover, while simultaneously failing to protect any Bahamian residents'

Morrison, Nabisco and WesternGeco

The extraterritoriality question reached the US Supreme Court in 2010. In *Morrison v. National Australia Bank*,[4] a securities fraud case, the Supreme Court proceeded from the principle that there exists a presumption against extraterritorial application of statutes. It outlined a two-step approach for determining whether in a given case this presumption blocks recovery of property involved in an avoided foreign-to-foreign transfer. First, the court is to determine whether the presumption has been rebutted, by examining whether Congress intended the statute to apply extraterritorially. Second, if the presumption against extraterritoriality has not been rebutted, the court is to determine whether the litigation involves extraterritorial application of the statute.[5] The Court emphasised that the presumption against extraterritoriality is not a 'clear statement rule'—a court can look beyond the words of the statute and review the statute in context—but made clear that in seeking to overcome the presumption, 'uncertain indications do not suffice'.

In the subsequent *Nabisco* decision, in which the Supreme Court was called upon to apply the *Morrison* test in a RICO[6] context,[7] the first step of this inquiry was phrased as follows: 'If the statute is not extraterritorial then at the second step we determine whether the case involves a domestic application of the statute, and we do this by looking to the statute's "focus".'

In the recent *WesternGeco* decision,[8] discussed below, the Supreme Court further elucidated that the 'focus' of a statute is '"the object of its solicitude," which can include the conduct it "seeks to regulate," as well as the parties and interest it "seeks to protect" or vindicate'. The Supreme Court advised that analysis of a statute's focus should not occur 'in a vacuum' but should assess the statute 'in concert with other provisions' with which it works 'in tandem', and with a view to determining 'how the statute has actually been applied'.

The Madoff cases: divergent application of the Morrison test to section 550

Two of the first opinions applying the *Morrison* test to recovery of fraudulent transfers reached diametrically opposite conclusions. Both opinions were rendered in adversary proceedings arising out of the Bernard Madoff Ponzi scheme, and involved offshore 'feeder funds' that pooled capital from investors worldwide for investment in Madoff Securities. The feeder funds had received distributions from Madoff Securities, which they transferred to their foreign customers.

BLI[9]

In what is commonly referred to as the *BLI* matter, the trustee for the Madoff Securities estate sought to recover certain transfers received by foreign entities, including the Taiwanese Bureau of Labour Insurance (BLI), via one of the largest feeder funds for Madoff Securities.

The US Bankruptcy Court for the Southern District of New York applied the *Morrison* steps in reverse order.[10] First, it determined that the 'focus' of the avoidance and recovery sections in the Bankruptcy Code is on the initial transfer, from the bankruptcy estate to an initial transferee, since it is this initial transfer that depletes the estate. The court explained that 'if the acts or objects upon which the statute focuses are located in the United States, application of the statute is domestic and the presumption against extraterritoriality is not implicated, even if other activities or parties are located outside the United States'. Because Madoff Securities was located in New York, the court held that the relevant transfers were domestic and application of section 550 to recover transferred assets would not be extraterritorial, even if the recovery involved a subsequent transferee located abroad.

Second, although the court found that recovery of the transferred assets in this case did not call for extraterritorial application of the

avoidance provisions, it determined that the statutory context showed Congress's intent to allow such application. Congress demonstrated this intent through 'interweaving terminology and cross-references' by:
- defining 'property of the estate' in section 541 to include all property worldwide;
- incorporating the language 'interest of the debtor in property' in avoidance sections 544, 547, and 548; and
- explicitly authorising recovery of all avoided transfers in section 550.

The court added that disallowing recovery of assets fraudulently transferred abroad would 'render hollow the avoidance and recovery provisions of the Code, an outcome clearly unintended by Congress'. It distinguished the SDNY's findings in *Maxwell* on the basis that the *Maxwell* debtor was located outside the United States, so that depletion of the estate in that case occurred abroad.

Finally, the court held that considerations of comity did not bar recovery of the transferred assets, distinguishing the *Maxwell* court's comity decision as having 'no applicability to the instant case', because BLI was not involved in parallel liquidation proceedings in a foreign country.

ET – District Court[11]

In a different adversary proceeding emanating from the Madoff Securities bankruptcy, the District Court for the Southern District of New York reached the opposite conclusion from the *BLI* court.

Applying a *Morrison/Nabisco* analysis, the court first determined that recovery of the transfers at issue would require extraterritorial application of section 550. The 'focus' of the section, according to the court, was on 'the property transferred and the fact of its transfer', not on the debtor. Applying the 'component events' test articulated in *Maxwell*, the court observed that the transfers and transferees involved in the proceeding were predominantly foreign, and that the funds' origination at Madoff Securities in New York was insufficient to render them domestic. The court also rejected the argument that the use of correspondent banks in the US to execute the transfers would render the transfers domestic.

The court next concluded that Congress did not evince 'clear intent' to permit extraterritorial application of section 550. It rejected the relevance of section 541's definition of 'property of the estate', citing Second Circuit precedent for the proposition that 'preferential transfers do not become property of the estate until recovered.'[12] On the basis of this precedent, the court declined to follow *In re French*. In doing so, it noted that *In re French* was distinguishable in any event, since it involved transfer activity that took place in the US as well as parties based in the US. The court brushed aside an argument (endorsed by the *Maxwell* court) that barring extraterritorial application of section 550 would allow debtors and creditors to avoid recovery by arranging for their transfers to occur abroad, reasoning that 'the desire to avoid such loopholes in the law must be balanced against the presumption against extraterritoriality'.

Finally, the court cited comity as an independent ground for disallowing recovery from the foreign transferees. It reasoned that, since many of the feeder funds were involved in foreign liquidation proceedings, investors in foreign funds 'had no reason to expect that U.S. law would apply to their relationships with the feeder funds'. The court added that given the 'indirect relationship between Madoff Securities and the transfers . . . foreign jurisdictions have a greater interest in applying their own law than does the United States'.

The court did not dismiss any of the pending claims, instead remanding the case to the bankruptcy court, to determine which claims should be dismissed for being 'purely foreign transfers'.

ET – on remand[13]

Before the bankruptcy court could address the issues left on remand, parties to more than 80 parallel adversary proceedings filed motions to dismiss on, among other things, extraterritoriality grounds, relying on the district court's decision. The court issued an omnibus decision addressing the motions together.

The judge[14] noted the stark differences between the *BLI* and *ET* decisions, and construed his task narrowly: to review the allegations 'to determine whether they survive dismissal under the extraterritoriality or comity principles enunciated in the *ET* decision'.

The court first examined the claims under principles of comity. Most claims based on transfers originating in feeder funds that were subject to a foreign liquidation proceeding were dismissed on the basis of comity.[15] Although the court noted that a finding of 'comity among nations does not require parallel proceedings', it did not engage in a comity analysis for the remaining transfers.

The court next performed a detailed extraterritoriality analysis, painstakingly analysing the numerous claims one by one to determine 'the critical factor—where the transfer occurred'. The court stated that the *ET* decision 'identifie[d] only four possibly relevant facts to consider in determining whether the Trustee has rebutted the presumption against extraterritoriality: (i) the location of the account from which the transfer was made, (ii) the location of the account to which the transfer was made; (iii) the location or residence of the subsequent transferor and (iv) the location or residence of the subsequent transfer'. Applying these criteria, the court dismissed a 'substantial number' of the remaining claims on the basis of extraterritoriality, as they did not allege a relevant nexus with the United States.

Madoff appeal

The Madoff Securities trustee filed a petition for leave to appeal the *ET* district court decision and the subsequent decision on remand to the Court of Appeals for the Second Circuit,[16] presenting the court with two questions:
- whether the Bankruptcy Code and the Securities Investor Protection Act 'permit the recovery of property fraudulently transferred by the debtor when it has been subsequently transferred in transactions with allegedly extraterritorial components'; and
- '[w]hether the comity of nations independently bars recovery of such property'.

The petition was granted on 27 September 2017.[17]

In re Picard[18]

In a carefully written opinion that confined itself to the specific facts presented, the Second Circuit in *In re Picard* resolved the split between the Madoff district court decisions by finding that the Madoff trustee could recover for alleged fraudulent transfers that occurred between foreign initial and subsequent transferees.

The Second Circuit reached its conclusion through a novel analysis and a narrower ruling in comparison to that of the lower courts. Instead of announcing a bright-line rule on the extraterritorial application of section 550(a) under the first step of *Morrison*, the *Picard* court proposed a new conceptual framework under the second step of *Morrison* for analysing whether, in a given case, section 550(a) involves domestic or extraterritorial conduct.

The *Picard* court determined that, taken together, sections 548(a)(1)(A) and 550(a) focus on the initial transfer of the debtor, and that, as a result, the transactions at issue in the Madoff cases should be considered domestic applications of the statute, notwithstanding the fact that subsequent transfers may have occurred entirely between foreign entities. The court also determined that, based on the facts before it, comity concerns did not bar the Madoff trustee from seeking to recover fraudulent transfers from foreign initial or subsequent transferees. The Second Circuit vacated the judgments of the *ET* bankruptcy

court dismissing the Madoff trustee's actions and remanded the case for further proceedings.

Morrison/Nabisco/WesternGeco analysis

The *Picard* court began by reviewing the operative provisions of the Bankruptcy Code that the Madoff trustee relied upon: sections 548(a)(1)(A)and 550(a).[19] The Madoff trustee alleged that Madoff Securities' initial transfers to feeder funds were avoidable as fraudulent under section 548(a)(1)(A). Section 548(a)(1(A) provides, in relevant part, that '[t]he trustee may avoid any transfer . . . of an interest of the debtor in property, or any obligation . . . incurred by the debtor', provided the debtor 'voluntarily or involuntarily . . . made such transfer . . . with actual intent to hinder, delay, or defraud . . . .'[20] The Madoff trustee sought to reclaim such fraudulent transfers under the recovery provisions of section 550(a), in particular from foreign subsequent transferees of the foreign feeder funds.

The lower court in *ET* had dismissed the Madoff trustee's action after finding under *Morrison/Nabisco* that Congress did not evince a 'clearly expressed' intent that section 550(a) should have extraterritorial reach and the transactions did not involve a domestic application of the statute. The *Picard* court reviewed these determinations *de novo*.

Rather than analyse the Morrison questions in the order posed by the Supreme Court, the Picard court found this 'an appropriate case for beginning with the latter question' – whether the case involved a domestic application of the statute. The court first assessed whether, per *Nabisco*, 'the conduct relevant to the statute's focus occurred in the United States'.[21] The court's approach to analysing the 'focus' of section 550(a) was influenced by the Supreme Court's recent decision in *WesternGeco*, which examined the extraterritorial application of provisions of the Patent Act. According to *WesternGeco*, courts must not 'analyze the provision at issue in a vacuum' when determining a statute's focus. Instead, '[i]f the statutory provision at issue works in tandem with other provisions, it must be assessed in concert with those other provisions'. Courts must also consider the conduct that a statute 'seeks to regulate' and the 'parties and interests it seeks to protect or vindicate'.

The *Picard* court took the teachings of *WesternGeco* to heart in fashioning a new framework for analysing the 'focus' of section 550(a). First, the court found that in order to properly assess the focus of section 550(a), it must not consider the provision 'in a vacuum'. Because section 550(a) is a recovery provision that can apply 'only to the extent that a transfer is avoided' pursuant to an avoidance provision of the Bankruptcy Code, the two provisions necessarily work 'in tandem'. The *Picard* court accordingly held that 'to determine § 550(a)'s focus in a given action, a court must also look to the relevant avoidance provision', whether that is section 548(a)(1(A) or another provision identified in section 550(a).

Second, the court found that when section 550(a) is considered in tandem with section 548(a)(1(A), section 550(a) should be read as regulating the debtor's fraudulent transfer of property. Section 548(a)(1(A) allows a trustee to 'avoid any transfer . . . of an interest of the debtor in property' that the debtor 'made . . . with actual intent to hinder, delay, or defraud'. The court found the purpose of this provision to be 'plain: it allows a trustee, for the protection of an estate and its creditors, to avoid a debtor's fraudulent . . . transfer that depletes the estate'. Quoting bankruptcy expert Edward Morrison, the *Picard* court stated that section 550(a) is a 'utility provision, helping execute the policy of § 548[(a)(1)(A)]' by 'tracing the fraudulent transfer to its ultimate resting place (the initial or subsequent transferee)'.

On this basis, the *Picard* court held that 'in recovery actions where a trustee alleges a debtor's transfers are avoidable as fraudulent under § 548(a)(1)(A), § 550(a) regulates the fraudulent transfer of property depleting the estate', and thus regulates the debtor's initial transfer. Therefore the focus of section 550(a) is on the initial transfer from Madoff Securities to the feeder funds, and not on subsequent overseas transfers made by the feeder funds. The court found that the lower courts, which held that section 550(a) regulated only the subsequent transfer of property, had erred by failing to consider how '§ 548(a)(1)(A) shape[d] the focus of § 550(a)'.

Finally, the *Picard* court analysed the initial transfers of debtor Madoff Securities and determined that they involved a domestic application of the statute. Madoff Securities was a domestic debtor based in New York and the alleged fraud occurred when the debtor transferred property from US bank accounts. On this basis the court held that the transfers were 'domestic activity for the purposes of §§ 548(a)(1)(A) and 550(a)', and that 'the presumption against extraterritoriality therefore does not prohibit the debtor's trustee from recovering such property using § 550(a), regardless of where any initial or subsequent transferee is located'.

The *Picard* court also indicated that its resolution of the case provided the best policy outcome. The court noted that if the approach in *ET* were followed and the court focused on the transferee's receipt of property, instead of the debtor's transfer, this would 'open a loophole' for persons on the verge of bankruptcy to transfer assets outside the reach of the Bankruptcy Code and its creditor-protection provisions. The court refused to read *Morrison* and the Bankruptcy Code in this 'self-defeating way'.

Because the *Picard* court found that the case involved a domestic application of section 550(a), it declined to opine on whether section 550(a) indicates its extraterritorial application under *Morrison* step one.

Comity

The *Picard* court then assessed whether the lower courts' dismissal of the Madoff trustee's actions on international comity grounds was proper. The lower courts had found that comity principles required a 'choice-of-law analysis to determine whether the application of US law would be reasonable under the circumstances, comparing the interests of the United States and the relevant foreign state'.[22] Applying this analysis, the lower courts found that comity barred the application of US law here. The *Picard* court interpreted this question as one of 'prescriptive' comity, which requires the court to determine whether, as a matter of statutory interpretation, it should presume that Congress limited the application of domestic law in certain situations out of respect for foreign sovereigns.[23] The court reviewed the comity question *de novo*, and found that the lower courts had erred.

The *Picard* court applied the choice-of-law test from the *Maxwell* case, which 'takes into account the interests of the United States, the interests of the foreign state, and those mutual interests the family of nations have in just and efficiently functioning rules of international law'.[24] First, the *Picard* court noted that the 'United States has a compelling interest in allowing domestic estates to recover fraudulently transferred property'. When a debtor in American courts is also in foreign liquidation proceedings, the foreign state 'has at least some interest in adjudicating property disputes', which '[i]n appropriate cases . . . will trump our own'. The court noted that there were no such parallel proceedings in this case, because only the feeder funds, not Madoff Securities, had filed as debtors in foreign courts. The court found that 'the absence of such [parallel] proceedings seriously diminishes the interest of any foreign state' in how the matters were resolved.

The court did recognise that foreign states adjudicating the feeder funds' liquidations would have an interest in the Madoff trustee's actions, since if the Madoff trustee succeeded in his recovery attempts, it might 'frustrate' the efforts of the feeder funds' trustees to recover

the same property. But the court determined that those interests did not implicate 'the comity concerns our precedent discusses in explaining when and why the Bankruptcy Code should give way to foreign law', because the proceedings in question were not duplicative of the US action.[25] The court therefore concluded that, under the *Maxwell* test, the United States' interest in applying its law outweighed that of any foreign state and that under the facts presented, prescriptive comity posed 'no bar to recovery' of property under section 550(a) from a foreign subsequent transferee, 'even if the initial transferee is in liquidation in a foreign nation'.

As with the extraterritoriality analysis, the *Picard* court found that the lower courts erred in their comity analysis by focusing on the subsequent transfers to foreign transferees, as opposed to the debtor's initial transfer, which was domestic in nature and implicated the United States' interests.

Result and effects

The *Picard* court permitted the Madoff trustee to seek avoidance and recovery of alleged fraudulent transfers involving foreign transferees, in alignment with the outcomes in the *BLI* and *In re French* cases. But given the narrow ruling in *Picard*, it remains to be seen just how much the decision will affect the litigation landscape concerning this issue.

On the one hand, and in contrast to *BLI* and *In re French*, the *Picard* decision declined to reach the larger question of section 550(a)'s extraterritorial application under the first step of Morrison. Such a ruling might have encouraged litigation against foreign recipients of fraudulently transferred assets. As it is, the *Picard* decision sets out an analytical framework for litigants to argue that an application of section 550(a) involves domestic conduct under *Morrison* step two. But the outcome of that analysis in the context of other fact patterns, and under other avoidance provisions of the Bankruptcy Code, is uncertain.

On the other hand, the *Picard* decision can be read to suggest that permitting domestic trustees to reach assets of foreign transferees is not only the right policy outcome, but also permissible under, and intended by, the Bankruptcy Code. This may lead plaintiffs to believe that the Second Circuit would be inclined to find that section 550(a) has extraterritorial effect, if made to confront the issue in a future case.

Unresolved questions

The *Picard* court ruled narrowly on the issues raised by the Madoff trustee, leaving many open questions. First and foremost, while numerous observers had hoped for a conclusive resolution of the extraterritorial application of section 550(a), the court pointedly declined to render an opinion on it. Within the Second Circuit this issue remains subject to the contrasting opinions of the *BLI* and *ET* courts.

In lieu of addressing extraterritoriality under the first step of *Morrison*, the *Picard* court provided a framework for analysing whether, in a given case, section 550(a) involves foreign or domestic conduct. But the court's analysis was confined to the specific case of fraudulent transfers avoided under 548(a)(1)(A) and recovered under section 550(a), where the transfers were made by a domestic debtor from banks located in the United States. It is therefore unclear, for instance, whether the outcome would be the same for a domestic debtor whose transfers were made from foreign banks, or a foreign debtor making transfers from US banks. The court declined to discuss how such changes might affect its ruling.[26]

Finally, it remains unclear how the *Picard/Morrison* analysis will play out for transfers avoided under the six other avoidance provisions listed in section 550(a). Although guidance can be gleaned from the *Picard* court's analysis under section 548(a)(1)(A), it will fall to future litigants and courts to grapple with those issues.

* *The authors express appreciation to Drew Dean for his significant assistance in the preparation of this chapter.*

Notes

1 *In re Maxwell Commc'n Corp plc*, 186 BR 807 (SDNY 1995), aff'd sub nom. *In re Maxwell Commc'n Corp plc*, 93 F3d 1036 (2d Cir 1996).
2 440 F3d 145 (4th Cir 2006).
3 Unlike the transfers at issue in *Maxwell* and the other recovery cases discussed in this chapter, the transfer in *In re French* was an 'initial transfer', made directly by the debtor to a transferee, and recoverable under section 550(a)(1) of the Bankruptcy Code.
4 561 US 247 (2010)..
5 As described below, the two-step Morrison test is often applied in reverse order.
6 Racketeer Influenced and Corrupt Organizations Act.
7 *RJR Nabisco, Inc. v. European Cmty*, 136 S Ct 2090 (2016).
8 *WesternGeco LLC v ION Geophysical Corp*, 138 S Ct 2129 (2018).
9 *Sec Inv'r Prot Corp v Bernard L Madoff Inv Sec LLC*, 480 BR 501 (Bankr. SDNY 2012) (BLI).
10 Before performing the *Morrison* analysis, the court determined that it had personal jurisdiction over BLI through a 'minimum contacts' analysis.
11 *Sec Inv'r Prot Corp v Bernard L Madoff Inv Sec LLC*, 513 BR 222 (SDNY 2014) (ET).
12 *ET*, 513 BR at 228–230, citing *In re Colonial Realty Co*, 980 F2d 125, 131 (2d Cir 1992).
13 *Sec Inv'r Prot Corp v Bernard L Madoff Inv Sec LLC*, No. AP 08-01789 (SMB), 2016 WL 6900689 (Bankr. SDNY November 22, 2016), petition for direct appeal docketed, No. 17-1341 (2d Cir 28 April 2017).
14 The omnibus decision on remand from ET was written by Judge Bernstein. The *BLI* decision was written by Judge Lifland.
15 Claims against three of these defendants were upheld because the court had not received sufficient information about the foreign liquidation proceedings to reach a conclusion.
16 *Pet. of Appellant Irving H Picard for Permission to Appeal Pursuant to 28 USC Section 158(d)(2)(A)*, Case No. 17-1341 (2d Cir 28 April 2017).
17 Docket No. 388 (Order), Case No. 17-1294 (2d Cir 27 September 2017).
18 917 F3d 85 (2d Cir 2019).
19 The Madoff trustee was appointed pursuant to the Securities Investor Protection Act (SIPA) and argued that certain provisions of SIPA provided additional reasons for the court to find that section 550(a) focused on domestic conduct. Because the court reached its holding without relying on SIPA, it 'express[ed] no opinion on whether SIPA is relevant to the focus of the Bankruptcy Code's avoidance and recovery provisions in cases where SIPA trustees seek to use them'. *Picard*, 917 F3d at 100.
20 11 USC § 548(a)(1)(A).
21 *Nabisco*, 136 S Ct at 2101.
22 *ET*, 513 BR at 231.
23 The second form of comity is 'adjudicative' comity, which asks whether a court should abstain from exercising jurisdiction in deference to a foreign nation's courts that might be a more appropriate forum for adjudicating the matter. The appellees in *Picard* raised adjudicative comity as a separate basis for arguing that the court should decline to exercise jurisdiction, but only did so in a footnote. The *Picard* court thus did not consider the issue to have been 'adequately raised' for appellate review. *Picard*, 917 F3d at 102 No. 14.
24 *Maxwell*, 93 F3d at 1048.
25 'The Bankruptcy Code gives us no reason to think Congress would have decided that trustees looking to recover property in domestic proceedings are out of luck when trustees in foreign proceedings may be interested in recovering the same property'. *Picard*, 917 F3d at 104-05.
26 The *Picard* court recognised this aspect of its holding, and explicitly provided no guidance: 'We express no opinion on whether either factor standing alone would support a finding that a transfer was domestic'. *Picard*, 917 F3d at 99.

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