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NEW OUTER LIMITS FOR THE EXTRATERRITORIAL REACH OF THE U.S. BANKRUPTCY CODE

In this article, the authors discuss a recent Second Circuit decision which, they suggest, could be used to substantially expand the extraterritorial reach of U.S. courts in bankruptcy cases and limit the deference U.S. courts will show to foreign jurisdictions in such cases.

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On February 25, 2019, the U.S. Court of Appeals for the Second Circuit issued a landmark decision, ruling that the trustee liquidating Madoff Securities can recover funds transferred to overseas entities under the Bankruptcy Code's recovery statute.¹

The case involved transfers of funds among Bernard L. Madoff Investment Securities LLC, feeder funds, and foreign investors. During the course of Madoff's Ponzi scheme, the feeder funds served as intermediaries between investors and Madoff Securities. In the case of distributions from Madoff Securities, money would first be transferred from Madoff Securities in New York to feeder funds located in a variety of locations ("Initial Transfers") outside of the United States. The feeder funds would then distribute the money to foreign investors ("Subsequent Transfers"). The primary issue was whether the presumption against extraterritoriality barred the trustee, appointed in the U.S. proceeding of Madoff Securities pending in the Bankruptcy Court for the Southern District

of New York, from recovering Subsequent Transfers made from the foreign feeder funds to foreign investors.

BACKGROUND

The question of extraterritorial application of the recovery statute was first considered in the District Court for the Southern District of New York before Judge Rakoff, who had withdrawn the reference to the Bankruptcy Court of numerous clawback actions seeking to recover fraudulent conveyances. Judge Rakoff applied a two-step test, originating from two Supreme Court cases, *Morrison* and *Nabisco*.² In those cases, the Supreme Court recognized a presumption against extraterritorial application of U.S. federal statutes. The Court stated in those decisions that in order to determine whether foreign application of U.S. laws is blocked by the presumption, a court should determine: (i) whether Congress intended the statute to apply extraterritorially and, if not, (ii) whether the litigation involves

¹ *In re Picard*, 2019 U.S. App. LEXIS 5411 Case No. 17-2992(L) (2d Cir. Feb. 25, 2019).

² *Morrison v. National Australia Bank Ltd.*, 561 U.S. 247 (2010); *RJR Nabisco Inc. v. European Cmty.*, 136 S. Ct. 2090 (2016).

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