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BREAKING NEW GROUND: SECOND CIRCUIT RULES THAT BANKRUPTCY CODE'S SECURITIES TRANSACTIONS SAFE HARBOR BARS FOREIGN COMMON- LAW CLAIMS IN CHAPTER 15 CASE

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U.S. Bankruptcy and appellate courts have long wrangled over whether the provisions of the Bankruptcy Code apply extraterritorially to permit, for example, enforcement of the automatic stay to creditor collection efforts against a debtor or property of its bankruptcy estate outside of the United States, or avoidance and recovery of voidable pre-bankruptcy transfers from non-U.S. creditors by a bankruptcy trustee or chapter 11 debtor-in-possession ("DIP").

Whether various provisions of the Bankruptcy Code may be applied extraterritorially to non-U.S. parties or asset transfers has also been debated in cross-border bankruptcy cases under chapter 15 of the Bankruptcy Code. The U.S. Court of Appeals for the Second Circuit recently addressed this question in a groundbreaking ruling. In *In re Fairfield Sentry Ltd.*, 2025 WL 2218836 (2d Cir. Aug. 5, 2025), the court of appeals reversed a lower court judgment in a chapter 15 case denying dismissal of common-law constructive trust claims asserted by the liquidators of a British Virgin Islands ("BVI") company against various non-U.S. recipients of more than $6 billion in redemption payments made as part of the Madoff Ponzi scheme.

According to the Second Circuit: (i) the constructive trust claims arising under BVI law were barred by the Bankruptcy Code's safe harbor (section 546(e)) insulating certain securities contract payments from avoidance in the absence of actual fraud; and (ii) by expressly providing in the Bankruptcy Code that section 546(e) applies in chapter 15 cases, U.S. lawmakers intended that section 546(e) apply extraterritorially, thereby overcoming the presumption against extraterritoriality of U.S. laws.

PROCEDURES, RECOGNITION, AND RELIEF UNDER CHAPTER 15

Chapter 15 was enacted in 2005 to govern cross-border bankruptcy and insolvency proceedings. It is patterned on the 1997 UNCITRAL Model Law on Cross-Border Insolvency, which has been enacted in some form by nearly 60 nations or territories.

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Under section 1515 of the Bankruptcy Code, the "foreign representative" of a foreign "debtor" may file a petition in a U.S. bankruptcy court seeking "recognition" of a "foreign proceeding."

Section 101(24) defines "foreign representative" as "a person or body, including a person or body appointed on an interim basis, authorized in a foreign proceeding to administer the reorganization or the liquidation of the debtor's assets or affairs or to act as a representative of such foreign proceeding."

"Foreign proceeding" is defined in section 101(23) of the Bankruptcy Code as:

> [A] collective judicial or administrative proceeding in a foreign country, including an interim proceeding, under a law relating to insolvency or adjustment of debt in which proceeding the assets and affairs of the debtor are subject to control or supervision by a foreign court, for the purpose of reorganization or liquidation.

11 U.S.C. § 101(23). More than one bankruptcy or insolvency proceeding may be pending with respect to the same foreign debtor in different countries. Chapter 15 therefore contemplates recognition in the United States of both a foreign "main" proceeding—a case pending in the country where the debtor's center of main interests ("COMI") is located (*see* 11 U.S.C. §§ 1502(4) and 1517(b)(1))—and foreign "nonmain" proceedings, which may be pending in countries where the debtor merely has an "establishment" (*see* 11 U.S.C. §§ 1502(5) and 1517(b)(2)). A debtor's COMI is presumed to be the location of the debtor's registered office, or habitual residence in the case of an individual. *See* 11 U.S.C. § 1516(c). An "establishment" is defined by section 1502(2) as "any place of operations where the debtor carries out a nontransitory economic activity."

Upon recognition of a foreign "main" proceeding, section 1520(a) of the Bankruptcy Code provides that certain provisions of the Bankruptcy Code automatically come into force, including: (i) the automatic stay preventing creditor collection efforts with respect to the debtor or its U.S. assets (section 362, subject to certain enumerated exceptions); (ii) the right of any entity asserting an interest in the debtor's U.S. assets to "adequate protection" of that interest (section 361); and (iii) restrictions on use, sale, lease, transfer, or encumbrance of the debtor's U.S. assets (sections 363, 549, and 552).

Following recognition of a foreign main or nonmain proceeding, section 1521(a) provides that, to the extent not already in effect, and "where necessary to effectuate the purpose of [chapter 15] and to protect the assets of the debtor or the interests of the creditors," the bankruptcy court may grant "any appropriate relief." Such relief can include, among other things, an order "granting any additional relief that may be available to a trustee, except for relief available under sections 522, 544, 545, 547, 548, 550, and 724(a)." These provisions authorize a bankruptcy trustee, among other things, to avoid and recover transfers that are fraudulent under the Bankruptcy Code and/or, under certain circumstances, "applicable" law (generally state law).

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However, these avoidance powers are expressly conferred upon a foreign representative if the debtor files for protection under another chapter of the Bankruptcy Code. Section 1523 authorizes the bankruptcy court to order relief necessary to avoid acts that are "detrimental to creditors," providing that upon recognition of a foreign proceeding, a foreign representative has "standing in a case concerning the debtor under another chapter of this title to initiate actions under sections 522, 544, 545, 547, 548, 550, 553, and 724(a)."

Certain provisions in other chapters of the Bankruptcy Code apply in chapter 15 cases pursuant to section 103(a) of the Bankruptcy Code, which provides that "[chapter 1], sections 307, 362(o), 555 through 557, and 559 through 562 apply in a case under chapter 15."

THE SECTION 546(e) SAFE HARBOR

Section 546 of the Bankruptcy Code imposes a number of limitations on a bankruptcy trustee's avoidance powers, which include the power to avoid certain preferential and fraudulent transfers. Section 546(e) provides that the trustee may not avoid, among other things, a pre-bankruptcy transfer that is a settlement payment "made by or to (or for the benefit of) a . . . financial institution [or a] financial participant . . ., or that is a transfer made by or to (or for the benefit of)" any such entity "in connection with a securities contract," except under section 548(a)(1)(A) of the Bankruptcy Code. Thus, the section 546(e) "safe harbor" bars avoidance claims challenging a qualifying transfer unless the transfer was made with actual intent to hinder, delay, or defraud creditors under section 548(a)(1)(A), as distinguished from constructively fraudulent transfers under section 548(A)(1)(B) where the debtor is insolvent at the time of the transfer (or becomes insolvent as a consequence) and receives less than reasonably equivalent value in exchange.

According to the legislative history of section 546(e), the purpose of the safe harbor is to prevent "the insolvency of one commodity or security firm from spreading to other firms and possibly threatening the collapse of the affected market." H.R. Rep. No. 97-420, at 1 (1982). The provision was "intended to minimize the displacement caused in the commodities and securities markets in the event of a major bankruptcy affecting those industries." *Id.*

Section 546(e) does not on its face apply in cases under chapter 15, nor is it one of the provisions made applicable in chapter 15 cases by section 103(a) of the Bankruptcy Code.

However, section 561(d) of the Bankruptcy Code, which was added to the Bankruptcy Code when chapter 15 was enacted in 2005, makes section 546(e) (and the other Bankruptcy Code provisions relating to securities contracts and other similar financial agreements) applicable in chapter 15 cases. Section 561(d) provides as follows:

> Any provisions of [the Bankruptcy Code] relating to securities contracts, commodity contracts, forward contracts, repurchase agreements, swap agreements, or master netting agreements *shall apply in a case under chapter 15*, so that enforcement of contractual provisions of such contracts and agreements in accordance with their terms will not be stayed or otherwise limited by operation of any provision of this title or by order of a court in any case under [the Bankruptcy Code], and to limit avoidance powers to the same extent as in a proceeding under chapter 7 or 11 of [the Bankruptcy Code] (such enforcement not to be limited based on the presence or absence of assets of the debtor in the United States).

11 U.S.C. § 561(d) (emphasis added).

Many notable court rulings have addressed: (i) whether section 546(e) preempts fraudulent transfer claims that can be asserted by or on behalf of creditors by a bankruptcy trustee under state law; (ii) whether the section 546(e) safe harbor insulates from avoidance only transactions involving publicly traded securities; and (iii) whether a "financial institution" must be the transferor or ultimate transferee, as distinguished from an intermediary or conduit, for a transaction to be insulated from avoidance under the safe harbor.

See, e.g., *Merit Mgmt. Grp., LP v. FTI Consulting, Inc.*, 583 U.S. 366 (2018) (holding that section 546(e) did not protect a transfer made as part of a non-public stock sale transaction through a "financial institution," regardless of whether the financial institution had a beneficial interest in the transferred property and noting that the relevant inquiry is whether the transferor or the transferee in the transaction sought to be avoided overall is itself a financial institution; acknowledging, however, that the Bankruptcy Code defines "financial institution" broadly to include not only entities traditionally viewed as financial institutions, but also the "customers" of those entities, which could include a debtor-transferor); *Petr v. BMO Harris Bank N.A.*, 95 F.4th 1090 (7th Cir. 2024) (affirming a district court ruling broadly construing the section 546(e) safe harbor to bar a chapter 7 trustee from suing under state law and section 544 of the Bankruptcy Code to avoid an alleged constructively fraudulent transfer made by the debtor shortly after it had been acquired in an LBO, and agreeing with the district court that: (i) the safe harbor is not limited to transfers involving publicly traded securities; and (ii) section 546(e) preempted the trustee's claim to recover the value of the transfer under section 544 and state law); *In re Nine W. LBO Sec. Litig.*, 87 F.4th 130 (2d Cir. 2023), *reh'g denied*, Nos. 20-3257-cv (L) *et al.* (2d Cir. Jan. 3, 2024) (adopting a "transfer-by-transfer" rather than a "contract-by-contract" approach to the safe harbor in affirming in part and reversing in part a district court ruling that section 546(e) preempted a litigation trustee's fraudulent transfer and unjust enrichment claims seeking avoidance of payments made to public and non-public shareholders as part of an LBO because

only the public shareholder payments involved a "financial institution."); *In re Tribune Co. Fraudulent Conveyance Litig.*, 946 F.3d 66 (2d Cir. 2019), *dismissing cert. in part*, 141 S. Ct. 728 (2020), *cert. denied*, 141 S. Ct. 2552 (2021) (explaining that, under *Merit*, shareholder payments as part of an LBO were shielded from avoidance under section 546(e) only if either the debtor transferor or the shareholders who received them were "covered entities," and concluding that the debtor was a "financial institution" and "therefore a covered entity"); *Deutsche Bank Trust Co. Ams. v. Large Private Beneficial Owners (In re Tribune Co. Fraudulent Conveyance Litig.)*, 818 F.3d 98 (2d Cir. 2016) (affirming court decisions dismissing creditors' state law constructive fraudulent transfer claims arising from an LBO and holding that, even though section 546(e) expressly provides that "the trustee" may not avoid certain payments under securities contracts unless such payments were made with the *actual* intent to defraud, section 546(e)'s language, its history, its purposes, and the policies embedded in the securities laws and elsewhere lead to the conclusion that the safe harbor was intended to preempt *constructive* fraudulent transfer claims asserted by creditors under state law).

THE PRESUMPTION AGAINST EXTRATERRITORIALITY

"It 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.'" *EEOC v. Arabian American Oil Co.*, 499 U.S. 244, 248 (1991) (quoting *Foley Bros. v. Filardo*, 336 U.S. 281, 285 (1949)). This "presumption against extraterritoriality" is a judicially developed rule of statutory construction whereby federal law is presumed not to apply to conduct or property outside the United States "unless a contrary intent appears." *Morrison v. National Australia Bank Ltd*., 561 U.S. 247, 255 (2010). Contrary intent is shown through "clear evidence," in either the statutory text or the "legislative purpose underlying it." *Smith v. United States*, 507 U.S. 197, 204 (1993). However, a law need not explicitly state that "this law applies abroad" to have extraterritorial effect, and context is relevant to infer the statute's meaning. *Morrison*, 561 U.S. at 255.

In *Morrison* and *RJR Nabisco, Inc. v. European Cmty.*, 136 S. Ct. 2090 (2016), the Supreme Court outlined a two-step approach to determine whether the presumption against extraterritoriality forecloses a claim. First, a court examines "whether the presumption against extraterritoriality has been rebutted—that is, whether the statute gives a clear, affirmative indication that it applies extraterritorially." *Nabisco*, 136 S. Ct. at 2101; *accord Morrison*, 561 U.S. at 255. If the conclusion is that the presumption has been rebutted, the inquiry ends.

If the presumption has not been rebutted, the court must determine whether the case involves a domestic application of the statute by examining its "focus." If the conduct relevant to the statute's focus occurred in the United States, "the case involves a permissible domestic application even if other conduct occurred abroad." *Nabisco*, 136 S. Ct. at 2101; *accord Morrison*, 561 U.S. at 266–67. However, if the conduct relevant to the focus of the statute did not occur in the United States, "the case involves an impermissible extraterritorial application regardless of any other conduct that occurred in U.S. territory." *Id.*; *accord Société Générale plc v. Maxwell Commc'n Corp. plc (In re Maxwell Commc'n Corp. plc)*, 186 B.R. 807, 816 (S.D.N.Y. 1995), *aff'd on other grounds*, 93 F.3d 1036 (2d Cir. 1996).

Most courts have adopted a flexible approach in determining whether a transaction occurred in the United States or was extraterritorial for this purpose. Many apply a "center of gravity" test, whereby the court examines the facts of the case to ascertain whether they have a center of gravity outside the United States. *See, e.g.*, *French v. Liebmann (In re French)*, 440 F.3d 145, 149 (4th Cir. 2006), *cert. denied*, 549 U.S. 815 (2006); *In re Florsheim Group Inc.*, 336 B.R. 126, 130 (Bankr. N.D. Ill. 2005). This analysis may involve consideration of "all component events of the transfer[]," *Maxwell*, 186 B.R. at 816, such as "whether the participants, acts, targets, and effects involved in the transaction at issue are primarily foreign or primarily domestic." *French*, 440 F.3d at 150.

EXTRATERRITORIAL OPERATION OF U.S. BANKRUPTCY LAW

In certain respects, U.S. bankruptcy law has explicitly applied extraterritorially for more than 70 years. In 1952, due to confusion about the scope of a debtor's property to be administered by a bankruptcy trustee under the Bankruptcy Act of 1898, Congress inserted the phrase "wherever located" into section 70a of the act "to make clear that a trustee in bankruptcy is vested with the title of the bankrupt in property which is located without, as well as within, the United States." H.R. Rep. No. 82-2320, at 15 (1952), *reprinted in* 1952 U.S.C.C.A.N. 1960, 1976; *see also* Pub. L. No. 82-456, 66 Stat. 420 (July 7, 1952). This language was preserved in section 541(a) of the Bankruptcy Code (enacted in 1978), which states that the bankruptcy estate includes the debtor's property "wherever located and by whomever held." Section 541(a) provides further that such property includes various "interests" of the debtor in property. Similarly, 28 U.S.C. § 1334(e) gives federal district courts—and, by referral pursuant to 28 U.S.C. § 157(a), bankruptcy courts within each district—exclusive jurisdiction of all property of the debtor and its estate, "wherever located."

Many courts have concluded that, because the automatic stay imposed by section 362(a) of the Bankruptcy Code expressly prohibits, among other things, acts to obtain possession of "property of the estate," the stay bars creditor collection efforts with respect to estate property located both within and outside the United States. *See, e.g.*, *Milbank v. Philips Lighting Elecs. N. Am. (In re Elcoteq, Inc.)*, 521 B.R. 189 (Bankr. N.D. Tex. 2014); *In re Nakash*, 190 B.R. 763 (Bankr. S.D.N.Y. 1996).

However, the provisions of the Bankruptcy Code permitting avoidance and recovery of preferential or fraudulent transfers—i.e., sections 544, 547, 548, and 550—do not expressly refer to "property of the estate" as that term is defined in section 541 or even to section 541 itself. Instead, section 544(a) permits the trustee to avoid certain transfers of "property of the debtor"; sections 544(b)(1), 547(b), and 548(a)(1) provide for the avoidance of "an interest of the debtor in property"; and section 550 permits the trustee to recover "the property transferred" or its value from the transferee.

Some courts have concluded that the Bankruptcy Code's avoidance provisions do not apply extraterritorially. *See, e.g., Maxwell*, 186 B.R. at 816 (Congress did not clearly express its intention, in statutory language or elsewhere, for section 547 to empower a trustee to avoid foreign preferential transfers); *In re CIL Limited*, 582 B.R. 46 (Bankr. S.D.N.Y. 2018) (the Bankruptcy Code's avoidance provisions do not apply extraterritorially because "[n]othing in the language of sections 544, 548, and 550 of the Bankruptcy Code suggests that Congress intended those provisions to apply to foreign transfers"), *amended on reconsideration*, 2018 WL 3031094 (Bankr. S.D.N.Y. June 15, 2018); *Spizz v. Goldfarb Seligman & Co. (In re Ampal-Am. Israel Corp.)*, 562 B.R. 601 (Bankr. S.D.N.Y. 2017) (the avoidance provisions of the Bankruptcy Code, including section 547(b), do not apply extraterritorially: "Property transferred to a third party prior to bankruptcy . . . is neither property of the estate nor property of the debtor at the time the bankruptcy case is commenced, the only two categories of property mentioned in Bankruptcy Code § 541(a)(1)."); *Barclay v. Swiss Fin. Corp. Ltd. (In re Bankr. Estate of Midland Euro Exch. Inc.)*, 347 B.R. 708, 719 (Bankr. C.D. Cal. 2006) (noting that the court could "find no basis for holding that Congress intended the trustee's avoiding powers to apply extraterritorially").

Other courts have reached the opposite conclusion. *See, e.g., French*, 440 F.3d at 149 ("Congress made manifest its intent that § 548 apply to all property that, absent a prepetition transfer, would have been property of the estate, wherever that property is located"); *In re FAH Liquidating Corp.*, 572 B.R. 117 (Bankr. D. Del. 2017) (ruling that the presumption against extraterritoriality with respect to section 548 was overcome because Congress intended the provision to reach foreign transfers), *leave to appeal denied*, 2018 WL 2793944 (D. Del. June 11, 2018); *Weisfelner v. Blavatnik (In re Lyondell)*, 543 B.R. 127 (Bankr. S.D.N.Y. 2016) (Congress could not have intended to exclude extraterritorial transfers from avoidance under section 548 while explicitly defining "property of the bankruptcy estate" under section 541 to include all of the debtor's property "wherever located and by whomever held"); *see also In Official Comm. of Unsecured Creditors of Arcapita Bank B.S.C.(C) v. Bahrain Islamic Bank (In re Arcapita Bank B.S.C.(C))*, 575 B.R. 229, 250–51 (Bankr. S.D.N.Y. 2017) (the automatic stay in section 362 of the Bankruptcy Code and section 542(b), which requires parties in possession of estate property to turn that property over to trustee, were intended by Congress to apply to estate property, wherever located, and could be applied extraterritorially to require foreign entities to turn over property to a chapter 11 debtor).

Finally, some courts, finding that a challenged transfer was domestic rather than foreign, have declined to address (other than in *dicta*) whether the Bankruptcy Code's avoidance and recovery provisions apply extraterritorially. For example, in *In re Picard, Trustee for the Liquidation of Bernard L. Madoff Investment Securities LLC*, 917 F.3d 85 (2d Cir. 2019), *cert. denied*, 140 S. Ct. 2824 (2020), the Second Circuit vacated a bankruptcy court order dismissing a trustee's litigation against various non-U.S. defendants to recover payments by a U.S. debtor that were allegedly avoidable as intentionally fraudulent transfers. The bankruptcy court had ruled that the claims against these subsequent foreign transferees must be dismissed because section 550(a)(2) of the Bankruptcy Code, which provides for the recovery of avoided fraudulent transfers from subsequent transferees, does not apply extraterritorially, and because principles of international comity limited the provision's scope.

In vacating the dismissal, the Second Circuit held that neither the "presumption against extraterritoriality" nor the doctrine of comity barred recovery because: (i) section 550(a)(2) works in tandem with section 548, which "focuses on the debtor's initial transfer of property"; (ii) the initial transfer occurred within the United States, meaning that the case involved domestic, rather than foreign, application of section 550(a); and (iii) comity did not warrant dismissal of the recovery actions because the interest of the United States in applying the Bankruptcy Code's avoidance and recovery provisions "outweighs the interest of any foreign state."

Notably, however, because the Second Circuit found that the case involved a domestic application of section 550(a), it "express[ed] no opinion on whether § 550(a) clearly indicates its extraterritorial application." *Id.* at 98 n.7; *see also Picard v. Bureau of Labor Ins. (In re Bernard L. Madoff Inv. Sec. LLC)*, 480 B.R. 501, 527 (Bankr. S.D.N.Y. 2012) (holding that, because the initial transfers of the debtor's assets occurred in the United States, the trustee was not seeking extraterritorial application of section 550, but noting in *dicta* that "Congress demonstrated its clear intent for the extraterritorial application of Section 550 through interweaving terminology and cross-references to relevant Code provisions").

FAIRFIELD SENTRY

Fairfield Sentry Limited and two affiliates (collectively, "Fairfield") were organized under the laws of the British Virgin Islands ("BVI") in 1990 as "feeder funds" for Bernard L. Madoff Investment Securities LLC ("BLMIS").

On July 21, 2009, after the Madoff Ponzi scheme collapsed, the High Court of Justice of the Eastern Caribbean Supreme Court (the "BVI Court") entered an order commencing liquidation proceedings for Fairfield under the BVI Insolvency Act of 2003. Shortly thereafter, the BVI Court-appointed joint liquidators (the "liquidators") for Fairfield commenced litigation in the BVI (the "BVI litigation") against a number of Fairfield's member (or subsequent transferees) that redeemed some or all of their shares before the collapse of the Ponzi scheme (collectively, the "redeemers") seeking to recover the redemption payments so that the funds could be distributed equitably among members. In the lawsuits, the liquidators argued that the redemption payments were mistakenly calculated based on inflated net asset values ("NAVs"), such that the redeemers received much more than what the redeemed shares were actually worth. The liquidators did not allege that any of the redeemers had acted in bad faith because they received the redemption payments with knowledge of the Ponzi scheme. Rather, they alleged that he redemption payments were "mistaken" based on inaccurate NAVs.

In addition to the BVI litigation, Fairfield's liquidators commenced approximately 300 lawsuits in the United States (the "U.S. litigation") to recover more than $6 billion in allegedly inflated redemption payments. The defendants in the BVI and U.S. litigation overlapped, but the claims asserted in the U.S. litigation involved different redemptions made at different times. In the U.S. litigation, the liquidators asserted causes of action for, among other things, unjust enrichment, mistaken payment, constructive trust under BVI common law, and preferential transfers and undervalue transactions under BVI law (the "BVI avoidance claims").

On June 14, 2010, the liquidators, as Fairfield's foreign representative, filed a petition in the U.S. Bankruptcy Court for the Southern District of New York (the "U.S. bankruptcy court") seeking recognition of the BVI liquidation as a foreign "main proceeding" under chapter 15. The U.S. bankruptcy court granted the liquidators' chapter 15 petition, and on July 22, 2010, recognized the BVI liquidation as a foreign main proceeding.

Upon recognition of Fairfield's BVI liquidation, the U.S. bankruptcy court stayed the U.S. litigation pending resolution of the BVI litigation.

In 2011, the BVI Court ruled that the redeemers had "paid good consideration for the Redemption Payments by surrendering their shares with the Funds, and, consequently, the Liquidators were barred from recovering those payments." After the Eastern Caribbean Court of Appeal affirmed the BVI Court's ruling, a further appeal was taken up by the Judicial Committee of the Privy Council in London—the highest court for the BVI and other British Overseas Territories—which also affirmed the BVI Court's ruling. *See Fairfield Sentry Ltd. (In Liquidation) v. Migani* [2014] UKPC 9, 2014 WL 1219748 (PC Apr. 16, 2014)). The Privy Council did not consider whether the redeemers acted in bad faith.

After the Privy Council issued its ruling in 2014, the U.S. bankruptcy court lifted the stay of the U.S. litigation, whereupon the liquidators sought to amend their complaints to add allegations of bad faith on the part of one of the redeemers. The defendants then moved to dismiss, arguing that the courts presiding over the U.S. litigation lacked personal jurisdiction, the complaints failed to state a claim, and the section 546(e) safe harbor barred any recovery.

In a series of rulings entered from 2018 and 2020, the U.S. bankruptcy court decided that: (i) the foreign selection clauses in the subscription agreements between Fairfield and more than 200 redeemers were insufficient to establish personal jurisdiction over those defendants in the United States (*see In re Fairfield Sentry Ltd.*, 2018 WL 3756343 (Bankr. S.D.N.Y. Aug. 6, 2018); (ii) the claims in the complaints should be dismissed, except for the BVI avoidance claims and the common-law constructive trust claims asserted against defendants alleged to have known that the redemption payments were inflated, because, among other things, the redemption payments were within the scope of the section 546(e) safe harbor, which applies extraterritorially in chapter 15 by means of section 561(d) of the Bankruptcy Code (*see In re Fairfield Sentry Ltd.*, 596 B.R. 275 (Bankr. S.D.N.Y. 2018)); and (iii) the safe harbor barred the liquidators' claims based on BVI statutory law, but the BVI common-law claims were not barred because section 546(e) did not impliedly preempt foreign law claims absent express statutory language to that effect (*see In re Fairfield Sentry Ltd.*, 2020 WL 7345988 (Bankr. S.D.N.Y. Dec. 14, 2020).

The U.S. bankruptcy court denied the defendants' motion for reconsideration of its decision that the common-law claims survived the safe harbor. A district court affirmed the ruling on appeal. *See In re Fairfield Sentry Ltd.*, 2021 WL 771677 (Bankr. S.D.N.Y. 2021), *aff'd*, 630 F. Supp. 3d 463 (S.D.N.Y. 2022).

Both the liquidators and the redeemers appealed from the district court's 2022 decision. In the first, the liquidators argued that the district court should have reversed the U.S. bankruptcy court's dismissal of all of the non-common-law claims. In the second, the redeemers argued that the district court should have reversed the U.S. bankruptcy court's ruling that the constrictive trust claims survived the section 546(e) safe harbor.

The appeals were consolidated before the Second Circuit.

THE SECOND CIRCUIT'S RULING

A three-judge panel of the Second Circuit reversed the district court's judgment permitting the common-law claims to proceed, but otherwise affirmed.

Writing for the panel, U.S. Circuit Court Judge Steven Menashi first determined that the forum selection clauses in the defendants' subscription agreements with Fairfield established personal jurisdiction over them.

Next, turning to the merits of the liquidators' claims, the Second Circuit concluded that the section 546(e) safe harbor barred the common-law constructive trust claims.

Extraterritoriality of the Section 546(e) Safe Harbor. Judge Menashi agreed with the district court's conclusion that the presumption against extraterritoriality did not bar application of the safe harbor to the liquidators' claims under BVI law because U.S. lawmakers expressed a clear intent to apply the safe harbor extraterritorially under section 561(d) of the Bankruptcy Code. Based upon that determination, the Second Circuit found it unnecessary to address whether the district court's alternative basis for affirming the U.S. bankruptcy court's decision—namely, that even in the absence such clear congressional intent, the application of the safe harbor in this case was domestic, rather than extraterritorial. *Fairfield*, 2025 WL 22118836, at *10.

Judge Menashi explained that, although section 546(e) does not by its own terms apply in a foreign proceeding under chapter 15, "the only plausible reading of section 561(d) . . . manifests an unmistakable congressional intent to apply [the provision] extraterritorially." *Id.* (citation and internal quotation marks omitted). According to Judge Menashi, "[s]ection 561(d) must apply extraterritorially if it is to have any effect at all" because, by means of section 561(d), the safe harbor restricts a foreign representative's avoidance powers, "[a]nd the only avoidance powers a foreign representative has in a case under Chapter 15 [by virtue of section 1521(a)(7)] are those that it possess under foreign law." *Id.*

The Second Circuit noted that, in addition to the text of section 561(d), chapter 15's purpose—to permit filing by foreign rather than domestic debtors—indicates that the provision applies extraterritorially. Judge Menashi explained that, when lawmakers provided in section 561(d) that the provision applies "in a case under chapter 15," they "did so with respect to the prototypical Chapter 15 case and the prototypical type of transfer that would be challenged in a Chapter 15 proceeding"—namely, a transfer made by a foreign debtor in a foreign jurisdiction, even if the transferee is a U.S. entity—rather than in "an exceptional or rare circumstance." *Id.* at *12. Moreover, he emphasized, the context from which section 561(d) was enacted—the collapse of Cayman Islands hedge fund that, without injunctive relief in its Cayman liquidation proceeding, would have triggered the liquidation of U.S. collateral pledged by the hedge fund to counterparties—"required an extraterritorial application." *Id.* at *13.

According to the Second Circuit, the liquidators' attempt to "have it both ways" by "benefitting from the domestic forum Chapter 15 has created for foreign law claims as a matter of comity while trying to avoid the limitations that Chapter 15 imposes on their power to bring those claims" is unsupportable. Judge Menashi explained that it would "seem only to increase the possibility of international friction" and could give plaintiffs suing to redress extraterritorial wrongdoing an advantage that they would not have if the defendant's conduct occurred in the United States. In addition, he noted, it is implausible that lawmakers intended to permit a foreign debtor "to take advantage of U.S. bankruptcy law to bring avoidance actions unconstrained by the safe harbor that applies in avoidance actions of a domestic trustee or debtor-in-possession." *Id.*

Application of the Safe Harbor to Preclude Foreign Common Law Claims. Next, the Second Circuit panel held that the section 546(e) safe harbor barred the liquidators' common-law constructive trust claims.

The parties agreed that the redemption payments were "settlement payment[s]" made to "financial institution[s] . . . in connection with a securities contract," as specified in section 546(e). However, the liquidators argued that: (i) the BVI avoidance claims were outside the scope of the safe harbor because they are intentional fraud transfer claims; (ii) because section 546(e) uses the term "avoid," the safe harbor apples only to statutory avoidance claims under the Bankruptcy Code or foreign bankruptcy law, and not to domestic or foreign common-law claims; and (iii) the common-law constructive trust claims did not resemble traditional avoidance claims because they were predicated on the defendants' knowledge rather than the insolvency of the debtor.

The Second Circuit panel rejected each of these arguments.

First, the court agreed with the liquidators that claims under foreign law need not include fraud as an element to fall within the safe harbor's carve-out for intentional fraudulent transfer claims, provided the allegations in support of the claims include actual intent to hinder, delay, or defraud creditors. However, the Second Circuit panel concluded that the liquidators did not allege such intent in this case, but merely what may have amounted to negligence or recklessness, and they never plausibly alleged that whatever intent the redeemers had could be attributed to Fairfield, a necessary element of avoidance under section 548(a)(1)(A) of the Bankruptcy Code and BVI law. *Id.* at **15–17.

Second, the Second Circuit panel rejected the liquidators' argument that section 561(d), which makes the safe harbor applicable in chapter 15 cases, applies only to foreign statutory avoidance claims that are analogous to a bankruptcy trustee's statutory avoidance claims, and not to foreign common-law claims. According to Judge Menashi, that argument contradicts the text of section 546(e), and a trustee's "avoiding powers" are not limited to the statutory avoiding powers under the Bankruptcy Code (e.g., sections 547 and 548). He further noted that courts have applied the safe harbor to bar state common-law claims as well as statutory avoidance claims.

The Second Circuit accordingly concluded that the safe harbor applies to *domestic* common-law claims regardless of principles of implied preemption, because they seek the same remedy as statutory avoidance claims. In addition, because, by operation of section 561(d), the safe harbor applies in chapter 15 to the same extent as in a chapter 7 or 11 case, *foreign* common-law claims are also within the scope of the safe harbor. *Id.* at **18–20. Judge Menashi wrote that "the focus of § 546(e) is the transaction, not the specific legal authority that a domestic trustee would use to avoid that transaction." *Id.* at *21.

Third, the Second Circuit panel concluded that "a common-law claim that seeks to avoid a covered transaction does not escape the safe harbor based on its legal theory or required proof." The court acknowledged that a constructive trust claim does not require a showing of insolvency, but does require a showing of the defendants' bad faith. However, it concluded that the liquidators' constructive trust claims were not premised on a different legal theory than a traditional avoidance claim. *Id.* at **21–22.

Accordingly, the Second Circuit ruled that the district court erred by allowing the liquidators' common-law constructive trust claims to escape the scope of the section 546(e) safe harbor.

OUTLOOK

The Second Circuit's ruling in *Fairfield Sentry* is a notable development in the two decades of chapter 15 jurisprudence. First, the Second Circuit held as an apparent matter of first impression among the federal circuits that the section 546(e) safe harbor applies extraterritorially by means of section 561(d) to bar foreign common-law claims asserted by the foreign representative of a debtor in a recognized chapter 15 case seeking avoidance of a qualifying transfer (or equivalent relief). As the Second Circuit emphasized in its opinion, "[i]t cannot be that Congress," in adding the safe harbor to the Bankruptcy Code, "intended to hobble investors by leaving them exposed to the risk of avoidance litigation brought by the bankruptcy estates of failed foreign companies, especially when the Bankruptcy Code bars domestic trustees from bringing the exact [same] claims." *Id.* at *13.

The bankruptcy and appellate courts in *Fairfield* are not the only courts that have considered the impact of the section 546(e) safe harbor in chapter 15 cases. For example, in *In re Bankr. Est. of Norske Skogindustrier ASA*, 629 B.R. 717, 763 (Bankr. S.D.N.Y. 2021) (Glenn, J.), another Second Circuit bankruptcy court held that sections 546(e) and 561(d) did not bar foreign law avoidance claims, even if the claims do not, like section 548(A)(1)(A), require demonstration of intentional fraud:

> Barring foreign law avoidance claims or imposing an impossibly high standard for the exception to the safe harbor to apply in chapter 15 cases would mean that there is effectively no exception to the safe harbor in such cases, contrary to the language of section 561(d), which makes section 546(e) applicable "to limit avoidance powers to the same extent as" (not to a broader extent than) "in a proceeding under chapter 7 or 11." 11 U.S.C. § 561(d). Accordingly, the Court declines to adopt a rigid rule barring foreign law avoidance claims or requiring the foreign statute to use language virtually identical to section 548(a)(1)(A) to except the challenged transaction from the section 546(e) safe harbor.

Id. at 763 (footnote omitted). The bankruptcy court explained that a contrary view would "risk the U.S. not just providing a safe harbor for qualifying transactions involving qualifying participants, but providing a safe haven for looters and fraudsters of foreign company assets that are transferred to the U.S. and who use banks or brokers to help carry out their schemes." *Id.* at 763 n.38.

In addition, in *In re IIG Glob. Trade Fin. Fund Ltd.*, 666 B.R. 38, 60–61 (Bankr. S.D.N.Y. 2024) (Wiles, J.), a different Second Circuit bankruptcy court held that the safe harbor did not preclude claims asserted in a chapter 15 case by the liquidators of

Cayman Islands investment funds alleging that transfers made by the debtors to acquire "participation interests" in loans were fraudulent transfers under New York law because, among other things, the transferees and the transaction did not satisfy the strictures of section 546(e).

In *In re Hellas Telecommunications (Luxembourg) II SCA*, 526 B.R. 499, 509–10 (Bankr. S.D.N.Y. 2015) (Glenn, J.), a Second Circuit bankruptcy court in a chapter 15 case refused to dismiss an unjust enrichment claim asserted by the liquidators of a UK company, ruling that the safe harbor did not bar the claim, which was premised on allegations that raised factual issues not appropriately resolved on a motion to dismiss, and where it was unclear whether the safe harbor applied extraterritorially to the underlying transfers, and the unjust enrichment claim raised choice-of-law issues that could not be resolved upon a motion to dismiss.

The Second Circuit's ruling in *Fairfield* would appear to have dispelled any lingering doubts among lower courts in the Second Circuit as to the extraterritorial application of the section 546(e) safe harbor by means of section 561(d). It should also quash debate concerning the application of the safe harbor in a chapter 15 case to bar claims under foreign common law seeking avoidance or equivalent relief, even if the claims do not involve actual fraudulent intent.

Finally, taken together with the Seventh Circuit's 2024 ruling in *BMO Harris* that the safe harbor is not limited to transfers involving publicly traded securities, the last two years have seen significant developments concerning the section 546(e) safe harbor, which has been broadly construed to bar a wide range of challenges under both foreign and domestic law to securities contract transfers.

GAP PERIOD INJUNCTIVE RELIEF WARRANTED IN CHAPTER 15 CASE WHERE RECOGNITION OF CANADIAN RECEIVERSHIP LIKELY BASED ON U.S. DEBTORS' RECEIVERSHIP ACTIVITIES

Corinne Ball • Heather Lennox • Dan T. Moss • Nicholas J. Morin

Unlike in cases filed under other chapters of the Bankruptcy Code, the filing of a petition for recognition of a foreign bankruptcy case under chapter 15 does not automatically trigger a stay of creditor actions against a debtor or its U.S. assets. Instead, the automatic stay generally applies only at such time that the U.S. bankruptcy court later enters an order recognizing the foreign bankruptcy as a "main" proceeding under chapter 15 or, in the event of recognition as a foreign "nonmain" proceeding, the court exercises its discretion to grant equivalent provisional relief.

This can be problematic if creditor collection efforts continue during the "gap period" between the filing of the chapter 15 petition and the entry of a recognition order. However, section 1519 of the Bankruptcy Code authorizes bankruptcy courts to grant provisional relief—including extension of the automatic stay or the issuance of a temporary injunction to protect the foreign debtor's U.S. assets—during the gap period "where relief is urgently needed to protect the assets of the debtor or the interests of the creditors."

The U.S. Bankruptcy Court for the Southern District of New York addressed a request for gap period injunctive relief in *In re Giftcraft Ltd*., 2025 WL 1583480 (Bankr. S.D.N.Y. June 4, 2025). Pending its decision on a petition for chapter 15 recognition of a Canadian receivership, the court in an unpublished ruling granted a foreign representative's request for a temporary injunction preventing creditors from proceeding against the assets of three U.S.-incorporated companies that were part of a group of companies subject to the receivership. Among other things, the bankruptcy court concluded that the foreign representative was likely to succeed in obtaining chapter 15 recognition because, although incorporated in the United States, the U.S. companies' "center of main interest" was in Canada. The court also ruled that parties affected by the injunction were adequately protected because they could participate and seek appropriate redress in both the Canadian receivership and the chapter 15 case.

PROCEDURES AND RECOGNITION UNDER CHAPTER 15

Chapter 15 was enacted in 2005 to govern cross-border bankruptcy and insolvency proceedings. It is patterned on the 1997 UNCITRAL Model Law on Cross-Border Insolvency (the "Model Law"), which has been enacted in some form by more than 50 countries.

Under section 1515 of the Bankruptcy Code, the "foreign representative" of a non-U.S. debtor may file a petition in a U.S. bankruptcy court seeking "recognition" of a "foreign proceeding."

Section 101(24) of the Bankruptcy Code defines "foreign representative" as "a person or body, including a person or body appointed on an interim basis, authorized in a foreign proceeding to administer the reorganization or the liquidation of the debtor's assets or affairs or to act as a representative of such foreign proceeding."

"Foreign proceeding" is defined in section 101(23) of the Bankruptcy Code as:

> [A] collective judicial or administrative proceeding in a foreign country, including an interim proceeding, under a law relating to insolvency or adjustment of debt in which proceeding the assets and affairs of the debtor are subject to control or supervision by a foreign court, for the purpose of reorganization or liquidation.

More than one bankruptcy or insolvency proceeding may be pending with respect to the same foreign debtor in different countries. Chapter 15 therefore contemplates recognition in the United States of both a foreign "main" proceeding—a case pending in the country where the debtor's COMI is located (*see* 11 U.S.C. § 1502(4))—and foreign "nonmain" proceedings, which may be pending in countries where the debtor merely has an "establishment" (*see* 11 U.S.C. § 1502(5)). A debtor's COMI is presumed to be the location of the debtor's registered office, or "habitual residence" in the case of an individual. *See* 11 U.S.C. § 1516(c). However, this presumption can be overcome.

Various factors have been deemed relevant by courts in determining a debtor's COMI, including the physical location of each debtor entity's headquarters, managers, employees, investors, primary assets, and creditors, as well as the jurisdiction whose law would apply to most of the debtor's disputes. *See In re SPhinX, Ltd.*, 351 B.R. 103 (Bankr. S.D.N.Y. 2006), *aff'd*, 371 B.R. 10 (S.D.N.Y. 2007).

In addition, courts have considered any relevant activities leading up to the chapter 15 filing, including liquidation or reorganization activities and administrative functions. *See Morning Mist Holdings Ltd. v. Krys (In re Fairfield Sentry Ltd.)*, 714 F.3d 127 (2d Cir. 2013). Such activities can entail the negotiation or execution of a restructuring support agreement with creditors, creditor meetings, liquidation activities (including court hearings), or administrative functions. *See, e.g.*, *In re Oi Brasil Holdings Coöperatief U.A.*, 578 B.R. 169, 222 (Bankr. S.D.N.Y. 2017) (citing *In re Creative Finance Ltd. (In Liquidation)*, 543 B.R. 498, 517 (Bankr. S.D.N.Y. 2016); *In re Modern Land (China) Co*., 641 B.R. 768, 778–81, 789–90 (Bankr. S.D.N.Y. 2022)). In addition, where the debtor is an entity with limited operations, it may be the case that restructuring activities performed outside the United States constitute the debtor's primary business activity prior to the filing of the chapter 15 petition.

Courts may also consider the situs of each debtor entity's "nerve center," including the location from which such entity's "activities are directed and controlled, in determining a debtor's COMI." *Fairfield Sentry*, 714 F.3d at 138. "[R]egularity and ascertainability" by creditors are also important factors in the COMI analysis. *Id.*; *In re British Am. Ins. Co.*, 425 B.R. 884, 912 (Bankr. S.D. Fla. 2010) ("The location of a debtor's COMI should be readily ascertainable by third parties."); *In re Betcorp Ltd.*, 400 B.R. 266, 289 (Bankr. D. Nev. 2009) (looking to whether COMI is ascertainable by creditors). Creditors' expectations regarding the location of a debtor's COMI are also relevant. *See In re Serviços de Petróleo Constellation S.A.*, 613 B.R. 497 (Bankr. S.D.N.Y. 2019); *Oi Brasil*, 578 B.R. at 228.

COMI can sometimes be found to have shifted, or "migrated," from a foreign debtor's original principal place of business or habitual residence to a new location. *See Pirogova,* 593 B.R. at 410; *see also Creative Finance*, 543 B.R. at 519 (ruling that the liquidator's efforts were too minimal to find a shift in COMI and noting that "[i]n the two months between the time [the debtors' principal] retained him and the time he filed his chapter 15 case in this Court, the Liquidator failed to do the basic things that can under normal circumstances cause a change in COMI—even in a liquidation"). In *Fairfield Sentry*, the Second Circuit ruled that, due principally to the present verb tense of the language of section 1517, the relevant time for assessing COMI is the chapter 15 petition date, rather than the date a foreign insolvency proceeding is commenced with respect to the debtor. *See Fairfield Sentry*, 714 F.3d at 137. The Fifth Circuit previously reached the same conclusion in *In re Ran*, 607 F.3d 1017 (5th Cir. 2010), as did the bankruptcy court in *British American*.

In *Fairfield Sentry*, the Second Circuit also expressed concern about possible COMI "manipulation," ruling that a court "may look at the period between the commencement of the foreign proceeding and the filing of the Chapter 15 petition to ensure that a debtor has not manipulated its COMI in bad faith." *Fairfield Sentry*, 714 F.3d at 138.

In cases involving multiple foreign debtors, COMI must be determined on an entity-by-entity basis. *See In re Black Press Ltd.*, No. 24-100044 (MFW) (Bankr. D. Del. Feb. 14, 2024) (unpublished order) (Doc. No. 73) (in a case involving multiple enterprise group debtors, the court must examine each debtor's COMI separately, rather than the enterprise group as a whole, for purposes of chapter 15 recognition; U.S. debtors' guarantee of their Canadian parent company's debts was an insufficient basis to conclude that the U.S. debtors' COMI was located in Canada, or that the U.S. debtor's even maintained an "establishment" in Canada); *In re Servicos de Petroleo Constellation S.A.*, 600 B.R. 237, 244 (Bankr. S.D.N.Y. 2019) ("While the Constellation Group is discussed as a group entity at times throughout this opinion's opening sections for context, it is important to bear in mind that the Court's recognition is granted on an individual debtor by debtor basis."); *In re OAS S.A.*, 533 B.R. 83, 92 n.8 (Bankr. S.D.N.Y. 2015).

If a U.S. court recognizes a foreign main proceeding under chapter 15, section 1520(a)(1) of the Bankruptcy Code provides that actions against the foreign debtor or its property located in the United States are stayed under section 362~~—~~the Bankruptcy

Code's "automatic stay." Following recognition of a foreign main or nonmain proceeding, a bankruptcy court is authorized under section 1521 to grant, among other things, injunctive relief staying actions or execution against the debtor's U.S. assets, the authority to distribute the proceeds of the debtor's U.S. assets, and, with certain exceptions, any additional relief available to a bankruptcy trustee "where necessary to effectuate the purpose of [chapter 15] and to protect the assets of the debtor or the interests of the creditors."

Section 1521(e) provides that "[t]he standards, procedures, and limitations applicable to an injunction shall apply to" requests for injunctive relief authorized by sections 1521(a)(1) and (2), to suspend the right to transfer the debtor's assets (section 1520(a)(3)), and for any extension of provisional relief previously granted during the gap period (section 1521(a)(6)).

During the gap period, section 1519(a) of the Bankruptcy Code authorizes a bankruptcy court to grant provisional injunctive relief and certain other forms of relief where "relief is urgently needed to protect the assets of the debtor or the interests of the creditors." Similar to section 1521(e), section 1519(e) provides that "[t]he standards, procedures, and limitations applicable to an injunction shall apply to relief under this section."

Before granting a preliminary injunction under Fed. R. Civ. Rule 65, Fed. R. Bankr. P. 7065, or section 105 of the Bankruptcy Code, most courts require the party seeking the provisional relief to demonstrate: (i) a reasonable likelihood of success on the merits; (ii) a likelihood of irreparable harm in the absence of relief; (iii) that the balance of hardships tips in the applicant's favor; and (iv) that the public interest would not be disserved if injunctive relief were granted. *See*, *e.g.*, *Broadstripe, LLC v. Natl. Cable Television Coop., Inc. (In re Broadstripe, LLC)*, 402 B.R. 646 (Bankr. D. Del. 2009); *Lyondell Chem. Co. v. CenterPoint Energy Gas Servs. Inc. (In re Lyondell Chem. Co.)*, 402 B.R. 571 (Bankr. S.D.N.Y. 2009).

However, courts sometimes disagree regarding the standard that should apply to a request by a foreign representative for provisional relief under section 1519 during the chapter 15 gap period. *See, e.g., In re Andrade Gutierrez Engenharia S.A.*, 645 B.R. 175, 181 (Bankr. S.D.N.Y. 2022) (in determining whether provisional relief is appropriate under section 1519, the court should apply the "standards, procedure, and limitations" that apply to the entry of a preliminary injunction); *In re Beechwood Re*, 2019 WL 3025283, at *2 (Bankr. S.D.N.Y. July 10, 2019) (same); *In re Pro-Fit Holdings Ltd.*, 391 B.R. 850, 860–61 (Bankr. C.D. Cal. 2008) (ruling that, because the relief sought under section 1519 was an extension of the automatic stay, rather than a temporary injunction, "the rules and jurisprudence for an injunction" did not apply); *In re Worldwide Educ. Servs., Inc.*, 494 B.R. 494, 498 (Bankr. C.D. Cal. 2013) (rejecting the *Pro-Fit* approach as being "flatly inconsistent with the plain and unambiguous language of section 1519(e)"); *In re Vitro, S.A.B. de C.V.*, 455 B.R. 571, 579 (Bankr. N.D. Tex. 2011) (applying the traditional preliminary injunction standard to a request for injunctive relief under sections 105 and 1519 during the gap period); *In re Innua Canada Ltd.*, 2009 WL 1025088 (Bankr. D.N.J. Mar. 25, 2009) (same).

Section 1522(a) provides that the bankruptcy court may exercise its discretion to order the relief authorized by section 1519 or 1521 "only if the interests of the creditors and other interested entities, including the debtor, are sufficiently protected."

Pursuant to sections 1520(c) and 1528, the foreign representative can also commence a full-fledged bankruptcy case under any other chapter of the Bankruptcy Code as long as the foreign debtor is eligible to file for bankruptcy in the United States under that chapter.

Section 1506 of the Bankruptcy Code sets forth a public policy exception to the relief otherwise authorized in chapter 15, providing that "[n]othing in this chapter prevents the court from refusing to take an action governed by this chapter if the action would be manifestly contrary to the public policy of the United States."

GIFTCRAFT

Giftcraft Ltd. ("Giftcraft Canada") supplies gift items, including home décor, jewelry, and other novelties, through specialty retailers and national chains in Canada. Its affiliates include: (i) Giftcraft Inc. ("Giftcraft U.S."), a New York corporation that manages the enterprise's distribution of its products in the United States; (ii) Ripskirt Hawaii, LLC ("Ripskirt"), an Oregon limited liability company that produces and distributes women's vacation and leisure apparel; and (iii) Yosox USA Inc. ("Yosox," and together with Giftcraft U.S. and Ripskirt, the "U.S. debtors"), a Delaware e-commerce retailer.

The ultimate parent of the group of companies (the "Giftcraft companies") is the Canadian corporation Giftcraft Holdings, Inc. ("GHI"). The holding company of the U.S. debtors is Giftcraft Midco, Inc. ("Midco), an Indiana corporation.

The Giftcraft companies have an identical team of officers. The six-member boards of directors of Giftcraft Canada and Midco consist of a president residing in Canada and five members located in the United States. The Giftcraft companies collectively employ 56 people based in Canada and 10 people based in the United States working remotely.

Giftcraft Canada has operated from leased premises in Ontario, Canada, since 2007 and has all of its inventory and accounts receivable in Canada. Giftcraft U.S. does not currently maintain any inventory, but at one time leased sample showrooms in Atlanta and Dallas. Its products are shipped directly to customers either through Giftcraft Canada or overseas suppliers. Giftcraft U.S. has no U.S. employees but has accounts receivable and three U.S. bank accounts holding in aggregate less than $5,000.

Ripskirt ships products from a third-party logistics facility located in Indiana housing its inventory. It has two U.S. bank accounts containing de minimis amounts. Yosox has one U.S. bank account containing less than $5,000.

In March 2024, a predecessor-in-interest to the Royal Bank of Canada (the "lender") extended various loans to Midco and Giftcraft Canada in the aggregate principal amount of approximately $28 million. The loans are secured by first-priority security interests in substantially all the Giftcraft companies' assets and are guaranteed by Midco, GHI, Giftcraft U.S., Yosox, Ripskirt, and another affiliate.

In February 2025, the Lender notified Midco and Giftcraft Canada that they were in default. The Giftcraft companies' other debts included unpaid rent under premises leased by Giftcraft Canada and Giftcraft U.S., and amounts owed by Ripskirt to payment processors and other entities.

In March 2025, the Lender issued a formal demand for payment. The Lender and the Giftcraft companies entered into a short-term forbearance agreement, but the Lender declined to extend the agreement after Giftcraft Canada informed it that the borrowers could not continue to make payments because Ripskirt, which was the principal source of the Giftcraft companies' revenue, had experienced an unprecedented decline in sales in April 2025 following the announcement of global tariffs on Chinese-sourced goods.

As provided in the forbearance agreement, the Lender on May 9, 2025, filed an application in a Canadian court to appoint a receiver under the Canadian Bankruptcy and Insolvency Act (the "BIA") to secure the Giftcraft companies' assets and review strategic alternatives. The Canadian court approved the application for a receivership (the "BIA Receivership") and appointed a provisional receiver for all of the Giftcraft companies' assets.

On May 20, 2025, the receiver, as the Giftcraft companies' foreign representative (the "FR") filed a petition in the U.S. Bankruptcy Court for the Southern District of New York (the "U.S. bankruptcy court") seeking chapter 15 recognition of the BIA Receivership as a foreign main proceeding or, alternatively, as a foreign nonmain proceeding. The FR also sought provisional relief in the form of a preliminary injunction under section 1519 of the Bankruptcy Code preventing creditor collection efforts against the Giftcraft companies' U.S. assets pending resolution of the recognition petition.

The Office of the U.S. Trustee (the "UST") opposed the recognition petition and the related relief, arguing, among other things, that COMI for all of the U.S. debtors is in the United States rather than Canada, and that the FC was not entitled to provisional relief under section 1519 because the FR could not demonstrate a likelihood of success on the merits of the chapter 15 petition as to the U.S. debtors. According to the UST, the U.S. debtors should be required to pursue the relief sought by the FR in chapter 15 by filing for protection under chapter 7 or chapter 11 of the Bankruptcy Code (as authorized by section 1520(c) and 1528).

THE U.S. BANKRUPTCY COURT'S RULING

The U.S. bankruptcy court granted the FR's motion for injunctive relief under section 1519.

Initially, U.S. Bankruptcy Judge Martin Glenn noted that a court should apply the "standards, procedure, and limitations" applicable to the issuance of a preliminary injunction when deciding whether to grant relief under section 1519(e) of the Bankruptcy Code—namely: (i) a likelihood of success on the merits (i.e., the recognition petition); (ii) "imminent irreparable harm" to the debtor absent provisional relief; (iii) a balance of harms tipping toward the party seeking injunctive relief; and (iv) public interest weighing in favor of the party seeking relief. *Giftcraft*, 2025 WL 1583480 at *5 (citing *Andrade*; 645 at 181 (citing *Lyondell,* 402 B.R. at 588–89)).

He emphasized that a showing of irreparable harm is the "'single most important prerequisite for the issuance of a preliminary injunction.'" *Id.* at *6 (quoting *Faively Transp. Malmo AB v. Wabtec Corp.*, 559 F.3d 110, 118 (2d Cir. 2009)). To satisfy this requirement, Judge Glenn explained, the party seeking injunctive relief must show that, without the injunction, it "'will suffer an injury that is neither remote nor speculative, but actual and imminent, and one that cannot be remedied if a court waits until the end of the trial to resolve the harm.'" *Id.* He further noted that the party seeking injunctive relief demonstrates a likelihood of success on the merits in this context by showing that it is likely to obtain chapter 15 recognition of a foreign proceeding. *Id.* (citing *Andrade*, 645 B.R. at 181).

The U.S. bankruptcy court concluded that the FR demonstrated all of the requirements for injunctive relief under section 1519(e).

The court emphasized that it did "not reach this conclusion lightly, as Chapter 15 is not a substitute for Chapters 7 and 11 for U.S.-based debtors, and the Court is vigilant of the potential for U.S. debtors to abuse the Chapter 15 process by bypassing Chapters 7 and 11." *Id.* at *8. Even so, Judge Glenn concluded that, at least for the purpose of injunctive relief under section 1519(e), the FR was likely to demonstrate that the COMI of the U.S. debtors as of the chapter 15 petition date was in Canada. *Id.*

First, the U.S. Bankruptcy court noted that Canadian insolvency proceedings, including court-ordered receivership, have routinely been recognized under chapter 15. *Id.* at *9.

Next, Judge Glenn found that the COMI of Giftcraft Canada and the U.S. debtors was Canada as of the chapter 15 petition date because:

- Giftcraft Canada was organized under the laws of Canada, where its registered office, employees, and executives were located. *Id.*
- Giftcraft U.S. exclusively maintained office space in Canada, where its books, records, and corporate documents were stored, and had no inventory in the United States. All of its material management decisions were made by Giftcraft Canada's senior management.
- Commencement of the BIA Receivership, whereby all of Giftcraft U.S.'s property was vested in the receiver, "constitutes pre-filing restructuring activities of the sort that suggest, as of the Petition Date, Giftcraft U.S.'s COMI was likely Canada." *Id.*
- The COMI of Ripskirt and Yosox was also likely Canada due to the same pre-filing restructuring activities associated with commencement of the BIA Receivership. *Id.* at *10.

The U.S. bankruptcy court explained that, "[i]n the cross-border insolvency context, courts have recognized that irreparable harm exists where local actions could hinder the orderly process of a foreign proceeding and the goal of the fair distribution of assets." *Id.* (citing *In re Petition of Garcia Avila*, 296 B.R. 95, 114 (Bankr. S.D.N.Y. 2003); *In re Berau Capital Res. PTE Ltd.*, No. 15-11804 (MG) (Bankr. S.D.N.Y. Aug. 6, 2015) (ECF Doc. # 20) at 3; *In re Banco Nacional de Obras y Servicios Publicos, S.N.C.*, 91 B.R. 661, 664 (Bankr. S.D.N.Y. 1988); *In re Lines*, 81 B.R. 267, 270 (Bankr. S.D.N.Y. 1988)).

According to Judge Glenn, Giftcraft Canada and the U.S. debtors would be irreparably harmed without an injunction because creditors were actively pursuing collection of their debts from the companies' U.S. assets. *Id.* at *11. He also found that the balance of harms favored the issuance of provisional relief because it would preserve the value of the assets of Giftcraft Canada and the U.S. debtors for the benefit of all creditors, and any creditor alleging harm from the injunction could petition the court for redress.

The U.S. bankruptcy court concluded that the public interest would be served by the issuance of injunctive relief because such relief promoted the bankruptcy policy of affording debtors a breathing spell from creditor collection efforts, ensured the equitable treatment of creditors, facilitated the receiver's efforts to maximize the value of the debtors' assets for the benefit of all stakeholders, and would "minimize jurisdictional inconsistencies pending this Court's recognition order and therefore will 'promote[] cooperation between jurisdictions in cross-border insolvencies,' advancing an express purpose of Chapter 15." *Id.* (citation omitted)

In overruling the UST's objections, the U.S. bankruptcy court noted that the case relied on by the UST—*Black Press*—was distinguishable because, unlike the U.S. debtors in these chapter 15 cases, the U.S.-based debtors in *Black Press* functioned independently from the Canadian debtors, and it did not appear that the U.S. debtors' COMI on the chapter 15 petition date was the in United States rather than in Canada, especially after commencement of the BIA Receivership. *Id.* at **11–12.

According to Judge Glenn, parties affected by the issuance of injunctive relief were sufficiently protected, as required by section 1522(a) of the Bankruptcy Code, because all creditors had access to the Canadian court in connection with the BIA Receivership and could participate in the chapter 15 case. *Id.* at *12. Finally, the U.S. bankruptcy court exercised its discretion to waive the security requirement for temporary injunctive relief in Fed. R. Bankr. P. 7065 as well as the requirement in Fed. R. Bankr. P. 1007(a)(4)(b) that the party seeking the injunction must identify all parties potentially impacted by it.

Because the U.S. bankruptcy court found that the FR was likely to obtain chapter 15 recognition of the BIA Receivership as a foreign main proceeding, it declined to address the FC's alternative argument that the receivership should be recognized as a foreign nonmain proceeding. *Id.* at *10 n.3.

POSTSCRIPT

On June 16, 2025, the U.S. bankruptcy court entered an order recognizing the BIA Receivership as a foreign main proceeding under chapter 15. *See In re Giftcraft Ltd.*, No. 25-11030 (MG) (Bankr. S.D.N.Y. June 16, 2025). Among other things, the court concluded that: (i) the U.S. debtors had a principal place of business and/or property in the United States, and were therefore eligible chapter 15 debtors; (ii) the U.S. debtors' COMI is in Canada; (iii) the requested relief was necessary to effectuate the purposes of chapter 15 and to protect the U.S. debtors' assets and the interests of creditors; (iv) the relief was necessary to effectuate the purposes and objectives of chapter 15 and to protect stakeholder interests; (v) the relief was in the interests of the public and international comity, consistent with U.S. public policy, and would not cause any hardship to any party that was not outweighed by the benefits of the relief; and (vi) absent the relief, creditor collection efforts could frustrate the BIA Receivership, contrary to the purposes of chapter 15.

On August 13, 2025, after the Canadian court approved the sale of substantially all of the assets of Giftcraft Canada, Giftcraft U.S., and Yosox, the U.S. bankruptcy court granted an uncontested motion to sell the companies' U.S. assets free and clear of all liens, claims, and encumbrances under sections 363(b) and 363(f) of the Bankruptcy Code. It also approved the assumption and assignment of various related contracts under section 365. Among other things, the U.S. bankruptcy court: (i) recognized the Canadian court's order approving the sale; (ii) found that the sale transaction satisfied the standard for approval of an asset sale under section 363(b); and (iii) concluded that the assignments passed muster under the business judgment standard. *See In re Giftcraft Ltd.*, No. 25-11030 (MG), 2025 WL 2336275 (Bankr. S.D.N.Y. Aug. 13, 2025).

OUTLOOK

Chapter 15 petitions seeking recognition of foreign bankruptcy proceedings are often filed for the purpose of enjoining creditor collection activities that threaten foreign debtors' U.S. assets so that the property can be administered in the foreign proceedings. However, unlike in cases under other chapters of the Bankruptcy Code, the filing of a chapter 15 petition does not automatically trigger a stay of creditor actions against the foreign debtor or its assets. Instead: (i) the automatic stay applies only if the U.S. bankruptcy court grants chapter 15 recognition of the foreign bankruptcy as a foreign main proceeding; (ii) the court may exercise its discretion to issue injunctive relief upon recognition of a foreign nonmain proceeding; or (iii) as illustrated by *Giftcraft*, the court can exercise its discretion to issue injunctive relief in cases where such provisional relief is urgently needed during the chapter 15 gap period to protect the foreign debtor's assets or the interests of creditors. The provisional relief provisions in chapter 15 are part and parcel of chapter 15's purpose to provide assistance to foreign tribunals in cross-border bankruptcy cases.

Key takeaways for *Giftcraft* include:

- The standard applicable to injunctive relief in other contexts also applies to such relief during the chapter 15 gap period.
- One element of that standard—likelihood of success on the merits—is satisfied if the party seeking injunctive relief demonstrates the bankruptcy court is likely to grant chapter 15 recognition of the foreign bankruptcy case.
- Another element of the standard for injunctive relief—irreparable harm—is satisfied where U.S. creditor actions could hinder the orderly process of a foreign proceeding and the goal of the fair distribution of assets.
- The COMI of each affiliated debtor in a group of companies must be assessed separately for purposes of recognition.
- Restructuring or liquidation activities in a foreign country can be a basis for finding that the debtor's COMI is in that foreign country, even if the debtor it is organized or incorporated elsewhere.

FLORIDA BANKRUPTCY COURT: PROPOSED DIP FINANCING AND SALE FRAMEWORK FOR ADMINISTRATIVELY INSOLVENT DEBTORS DID NOT VIOLATE *JEVIC*'S PROHIBITION OF PRIORITY-DEVIATING DISTRIBUTIONS

Jeffrey B. Ellman

The U.S. Supreme Court ruled in *Czyzewski v. Jevic Holding Corp.*, 580 U.S. 451 (2017), that the Bankruptcy Code prohibits final distributions to creditors that deviate from the Bankruptcy Code's priority scheme as part of a "structured dismissal" of a chapter 11 case without the consent of affected creditors. Since then, courts have been called upon to determine whether the rationale of *Jevic* extends to other contexts, such as proposed settlements and bankruptcy asset sales.

In *In re Silver Airways, LLC*, 2025 WL 1436258 (Bankr. S.D. Fla. May 19, 2025), the U.S. Bankruptcy Court for the Southern District of Florida weighed in on this debate in an unusual context. The court approved the debtors' motion to incur debtor-in-possession ("DIP") financing and for establishment of bidding procedures for an auction sale of assets even though the estate was administratively insolvent, and could remain administratively insolvent absent future events such as increased sale proceeds or successful prosecution of potential claims. According to the bankruptcy court, because the key administrative creditors made an informed decision to support the financing and sale framework as the only possibility of obtaining partial recovery on their claims, and no administrative creditors objected, the DIP financing and sale did not run afoul of *Jevic*.

THE BANKRUPTCY CODE'S PRIORITY SCHEME

The Bankruptcy Code contains certain priority rules governing distributions to creditors in both chapter 7 and chapter 11 cases. Secured claims enjoy the highest priority under the Bankruptcy Code. *See generally* 11 U.S.C. § 506. Section 507(a) of the Bankruptcy Code establishes priority for certain unsecured claims, including claims for administrative expenses allowed under section 503(b) of the Bankruptcy Code, employee wages and benefits, and certain tax claims. General unsecured claims come next in the priority scheme, followed by any subordinated claims and the interests of equity holders.

In a chapter 7 case, the order of priority for distributions on account of unsecured claims is determined by section 726 of the Bankruptcy Code. The order of distribution begins with payments on claims in the order of priority specified in section 507(a), which have the highest priority, and eventually to payment of any residual assets after satisfaction of all claims to the debtor, which has the lowest priority. Distributions are to be made *pro rata* to parties of equal priority within each of the six categories specified in section 726. If claimants in a higher category of distribution do not receive full payment of their claims, no distributions can be made to parties in lower categories.

In a chapter 11 case, the plan of reorganization determines the treatment of secured and unsecured claims (as well as equity interests), subject to the requirements of the Bankruptcy Code. Notably, unless the holder of an administrative expense claim agrees otherwise, the debtor cannot confirm a chapter 11 plan without paying administrative claims in full. *See* 11 U.S.C. § 1129(a)(9)(A) ("*Except to the extent that the holder of a particular claim has agreed to a different treatment of such claim*, [a chapter 11 plan cannot be confirmed unless] the plan provides that . . . with respect to a claim of a kind specified in section 507(a)(2) . . . of this title, on the effective date of the plan, the holder of such claim will receive on account of such claim cash equal to the allowed amount of such claim.") (emphasis added).

JEVIC

In *Jevic*, the Supreme Court held that the Bankruptcy Code does not allow bankruptcy courts to approve distributions to creditors in a "structured dismissal" of a chapter 11 case that violate the Bankruptcy Code's ordinary priority rules except with the consent of the creditors impacted (but not offering any "view about the legality of structured dismissals in general"). In cases where confirmation of a chapter 11 plan is not feasible, a structured dismissal of the case can be a less costly and more attractive alternative to outright dismissal or conversion of the case to a chapter 7 liquidation. An order approving a structured dismissal can include certain terms usually contained in a chapter 11 plan and confirmation order (like settlements and releases) but does not incorporate all of the substantive and procedural stakeholder protections that apply to the plan confirmation process.

The Court distinguished the case before it from cases in which courts have approved interim settlements resulting in distributions of estate assets in violation of the priority rules, such as *In re Iridium Operating LLC*, 478 F.3d 452 (2d Cir. 2007). The 6–2 majority found that *Iridium* "does not state or suggest that the [Bankruptcy] Code authorizes nonconsensual departures from ordinary priority rules in the context of a dismissal—which is a final distribution of estate value—and in the absence of any further unresolved bankruptcy issues." *Jevic,* 580 U.S. at 467. In this sense, the majority explained, the situation in *Iridium* was similar to certain "first-day" orders, where courts have allowed for, among other things, payments ahead of secured and priority creditors to employees for prepetition wages or to critical vendors on account of their prepetition invoices. *Id.* at 468. But such relief typically is in support of preserving a going concern and the opportunity to reorganize and achieve an eventual final resolution of the case consistent with the Bankruptcy Code's priority scheme and other requirements.

The Court explained that "in such instances one can generally find significant [Bankruptcy] Code-related objectives that the priority-violating distributions serve." *Id.* By contrast, it noted, the structured dismissal in *Jevic* served no such objectives (e.g., it did not benefit disfavored creditors by preserving the debtor as a going concern and enabling the debtor to confirm a plan of reorganization and emerge from bankruptcy). Rather, the distributions at issue "more closely resemble[d] proposed transactions that lower courts have refused to allow on the ground that they circumvent the [Bankruptcy] Code's procedural safeguards" (citing, among others, certain section 363 asset sales). *Id.*

In the aftermath of *Jevic,* many courts have examined what kinds of distributions can be authorized under the Court's rationale regarding permitted exceptions to its ruling. *See, e.g.*, *In re Nordlicht*, 115 F.4th 90, 118-20 (2d Cir. 2024) (affirming rulings in a chapter 7 case approving a settlement and related sale of estate claims that would distribute value to unsecured creditors without first paying disputed secured claims, where the estate claims could be sold free and clear of the purported secured creditors' interest because their liens were subject to *bona fide* dispute, and any funds distributed to unsecured creditors pursuant to a conditional indemnity provision did not violate the absolute priority rule); *In re Veg Liquidation, Inc.*, 931 F.3d 730, 739 (8th Cir. 2019) (unequal distribution of the proceeds from a section 363 sale to unsecured creditors with equal priority was not prohibited by *Jevic*); *In re Old Cold LLC*, 879 F.3d 376, 388 (1st Cir. 2018) (refusing to apply *Jevic* to disturb an asset sale under section 363(b) and ruling that section 363(m) rendered statutorily moot an appellate challenge to a sale to a good faith purchaser); *In re Romero*, 2025 WL 933942, at *7 (C.D. Cal. Mar. 27, 2025) ("*Jevic* neither considered nor discussed whether a high-priority secured creditor can assign or carve out a portion of its own recovery for the benefit of the bankruptcy estate and low-priority general unsecured creditors, and does not support Debtors' contention that a high-priority secured creditor may not agree to carve out a portion of its recovery for the bankruptcy estate. Debtors' argument, thus, fails."); *In re Micron Devices, LLC*, 2021 WL 2021468, *10 (Bankr. S.D. Fla. May 20, 2021) (approving a proposed settlement agreement that could avoid violation of priority rules while noting that previous structured dismissal proposals "would not pass muster" under *Jevic* because, among other things, administrative claimants would not be paid in full); *In re Goodrich Quality Theaters, Inc.*, 616 B.R. 514, 521 (Bankr. W.D. Mich. 2020) (relying on the "competing bankruptcy principles" identified in *Jevic*, namely preservation of going concern value and prospects for reorganization, to approve critical vendor payments), *as supplemented*, 2020 WL 1180534 (Bankr. W.D. Mich. Mar. 9, 2020); *In re Claar Cellars, LLC*, 2020 WL 1238924, *7 (Bankr. E.D. Wash. Mar. 13, 2020) (holding that the debtor's use of cash collateral to pay in part a prepetition, allegedly secured debt owed to an affiliated debtor did not violate *Jevic*); *In re ACI Concrete Placement of Kansas, LLC*, 604 B.R. 400, 407 (Bankr. D. Kan. 2019) (holding that enforcing a "carve out" from a secured creditor's collateral for payment of professional fees did not violate *Jevic*); *In re Daily Gazette Co.*, 584 B.R. 540, 546 (Bankr. S.D. W. Va. 2018) (a proposed disbursement following a section 363 sale that would result in an orderly payment of administrative claims, such as attorneys' fees and U.S. Trustee fees, followed by payment to an undisputed secured creditor with essentially a blanket lien covering in excess of the net sale proceeds "neither runs afoul of *Jevic* nor the [Bankruptcy] Code generally"); *In re Fryar*, 570 B.R. 602, 610 (Bankr. E.D. Tenn. 2017) ("In light of the Supreme Court's recent ruling in *Jevic,* parties who seek approval of settlements that provide for a distribution in a manner contrary to the [Bankruptcy] Code's priority scheme should be prepared to prove that the settlement is not only 'fair and equitable' . . . but also that any deviation from the priority scheme for a portion of the assets is justified because it serves a significant [Bankruptcy] Code-related objective.")

In *Silver Airways*, the bankruptcy court considered *Jevic*'s impact on a motion for approval of DIP financing and bidding procedures governing an asset sale in an administratively insolvent chapter 11 case.

SILVER AIRWAYS

In December 2024, Florida-based regional airline Silver Airways LLC ("Silver") and its affiliate Seaborne Virgin Islands, Inc. ("Seaborne" and, together with Silver, the "debtors") filed for chapter 11 protection in the Southern District of Florida. At the time of the bankruptcy filing, the debtors' assets consisted of 16 leased aircraft (shortly afterward reduced to eight) and related equipment, ground support infrastructure, maintenance and operations facilities, airport gate leases, receivables, and intellectual property. The debtors' liabilities included approximately $400 million in secured debt owed to two prepetition lenders (the "prepetition lenders"), aircraft lease obligations, vendor payables, and unpaid employee wages and benefits.

Because cash collateral proved inadequate to fund the debtors' operations, they sought court approval to incur up to $5.5 million in DIP financing from a bank (the "DIP lender") to support ongoing operations and fund a process to sell substantially all of the debtors' assets. In April 2025, the bankruptcy court approved part of the financing on an interim basis under section 364(d) of the Bankruptcy Code and scheduled a May 2025 hearing to approve the remainder of the DIP financing on a final basis.

The DIP financing was to be secured by first-priority priming liens on substantially all of the debtors' assets pursuant to section 364(d), and the DIP lender's claim was conferred with "super-priority" administrative expense status under section 364(c)(1). The interim DIP order also included various protections for the DIP lender, including milestones, a waiver of the debtors' right to surcharge the DIP lender's collateral, and provisions limiting the use of the loan proceeds to items authorized under a budget approved by the DIP lender.

The DIP lender also served as a stalking horse bidder in a proposed section 363(b) sale of Silver's assets, which the DIP lender offered to acquire by credit bidding its approximately $5.8 million first-priority secured debt. The debtors intended to separately seek approval of a sale of Seaborne's assets and Silver's equity interests in Seaborne.

The separate prepetition secured lenders consented to the relief requested by the debtors in their motion for approval of bidding procedures in connection with the proposed sale of Silver's assets (with the exception of a proposed payment to one of the lenders from the proceeds of any subsequent sale of Seaborne). The prepetition lenders also agreed to a "carve out" from their collateral for any unpaid administrative claims (including attorneys' fees).

Nevertheless, the debtors projected that they would have a total of approximately $12 million in administrative expenses as of the closing date of the sale of Silver's assets, including operating expenses, cure obligations for leased aircraft, and various other claims. Because the debtors projected no more than $9 million in monthly revenue, this meant that there would be a $3 million shortfall in closing date administrative liabilities—principally trade payables, taxes, and payroll—that would remain unpaid unless assumed by a buyer. In addition, another $4 million to $5 million in administrative claims, including professionals' fees, priority vendor claims, and aircraft lease cure amounts, could be satisfied only if a purchaser outbid the DIP lender for Silver's

assets or if Seaborne's assets were successfully sold or certain estate claims could be collected. There also were approximately $2.2 million in administrative claims for cure amounts payable as a condition to assuming aircraft leases, but these claims were to be paid by the purchaser rather than the estate.

All of the debtors' principal administrative creditors actively participated in the proceedings and supported the sale process. No administrative creditors objected. But not every administrative creditor gave its affirmative consent. Many remained silent.

THE BANKRUPTCY COURT'S RULING

The bankruptcy court approved both the DIP financing motion and the sales procedure motion.

The court reasoned that the shortfall in estate funds to satisfy administrative claims in full was troubling but did not warrant rejection of the proposed DIP financing and sale procedures. Bankruptcy Judge Peter D. Russin was mindful of *Jevic*'s prohibition of priority-deviating distributions without the consent of priority creditors. However, he explained, the consent of the principal administrative creditors, who participated in the process and were aware of the attendant risks of the DIP financing and sale structure, but viewed it as the best hope of recovery on their claims, "forms the legal basis for approval under [*Jevic*] and aligns with the principles set forth in §1129(a)(9)(A) of the Bankruptcy Code." *Silver Airways*, 2025 WL 1436258, at *5. According to Judge Russin, "[n]othing in *Jevic* or the [Bankruptcy] Code prevents administrative creditors from agreeing to a process that may leave them underpaid, so long as they do so voluntarily, with eyes open and in the absence of better alternatives." *Id.* at *6.

Judge Russin further explained that he would have denied the debtors' motions if administrative creditors objected to the proposed financing and sale structure because their claims were not being paid in full. That was not the case here, however, where "administrative creditors chose a negotiated risk over a guaranteed loss" or "the possibility of at least partial recovery through continued operations over the certainty of loss through collapse." *Id.* at **7–8.

Judge Russin acknowledged the possibility that the DIP lender could argue that the motions should be granted regardless of administrative creditor consent because the DIP lender was fully secured and was simply recovering what it was owed. Although this outcome was "facially consistent with priority," he noted, it failed "to address a deeper concern"—namely, that chapter 11 should not be used by a single creditor "to extract all value through a § 363 sale while leaving those who kept the estate aloft—vendors, lessors, professionals, and employees—unpaid." Secured creditors in this position must "pay the freight." *Id.* at *8 (citing *In re NEC Holdings Corp.*, No. 10-11890 (PJW) (Bankr. D. Del. July 11, 2011)).

Judge Russin explained that:

> A secured creditor that chooses to avail itself of the protections and powers of Chapter 11—including the ability to sell its collateral free and clear under § 363(f), to provide DIP financing under § 364, or to benefit from a structured wind-down—must also accept the obligations that come with that choice. Chief among them is the requirement that the estate's administrative expenses be paid. If those expenses cannot be paid, then a plan dependent on the sale is not feasible or confirmable under the [Bankruptcy] Code. The Court is not free to disregard that reality simply because secured creditor parties prefer the sale to other alternatives. Neither convenience nor expediency justify the erosion of the [Bankruptcy] Code's structural protections.

Id. at *8.

However, the bankruptcy court emphasized, where, as here, administrative creditors "have assessed the circumstances, considered the alternatives, and opted to support a process that may maximize going concern value, that decision deserves respect," especially "when the alternatives are neither a confirmable chapter 11 plan nor a competitive reorganization, but certain collapse." *Id.* The administrative creditors therefor have "chosen potential recovery over certain loss." *Id.* at *1.

Notably, the court did not require all administrative creditors to consent. The informed consent of the major administrative creditors and the lack of objection by others who were given notice was sufficient. The court explained: "Other administrative creditors—potentially including vendors and service providers—may have received notice but remained silent. Their silence does not constitute consent. But it also does not alter the reality that no party has filed an objection or proposed an alternative to the process now before the Court." *Id.* at *5.

The bankruptcy court acknowledged that the relief sought by the debtors was not confirmation of a chapter 11 plan, but emphasized that "the logic is parallel." Judge Russin further noted that "[t]he Court does not relieve the estate of its obligations . . . [but] respects the decision of those entitled to payment to accept uncertainty in the hope of a better outcome." *Id.*

OUTLOOK

Silver Airways is yet another example of bankruptcy courts attempting to determine the scope of *Jevic* in a context other than structured dismissal of a chapter 11 case. As the court explained, *Jevic* does not categorically reject priority-deviating distributions to creditors as part of a structured dismissal, asset sale, or settlement. Instead, the Supreme Court's decision prohibits *final distributions* that deviate from the Bankruptcy Code's priority scheme *without the consent of senior creditors*. Where senior creditors consent to such a framework—as is expressly provided with respect to administrative creditors in a chapter 11 case under section 1129(a)(9)(A)—*Jevic* is not an impediment to the framework.

Silver Airways is also notable because, confronted with the administrative insolvency of the debtors and the consent of administrative creditors to a DIP financing/sale framework as the only likely possibility of partial recovery, the bankruptcy court approved DIP financing that it would have rejected in almost any other case.

POSTSCRIPT

On June 11, 2025, the debtors informed the bankruptcy court that they had ceased operating. On June 18, 2025, the court approved the Sale of Silver's assets to the DIP lender, and after the court was informed that the debtors had secured a $200,000 bid for Seaborne's assets, it scheduled bid procedure, auction, and sale approval hearings in July.

On June 23, 2025, the DIP lender in an emergency motion asked that the court compel the debtors to close the credit-bid sale, claiming that the debtors were trying to extract additional consideration in direct contempt of the court's order approving the sale. According to the DIP lender, on June 22, 2025, the debtors demanded an additional payment of $650,000 and threatened to withhold cooperation in the transfer of assets.

On June 24, 2025, the bankruptcy court, concerned that the debtors' principals were not acting diligently to close the Silver sale, appointed a chapter 11 trustee for the debtors. However, on June 26, 2025, Judge Russin delayed the effectiveness of his order appointing a trustee, allowing current management to continue operating the debtors and administering the going-concern sale process for the Seaborne assets until June 30.

After approving bid procedures, the court approved the sale of Seaborne on July 3 and appointed a chapter 11 trustee. On July 31, the cases were converted to chapter 7 liquidations.

THIRD CIRCUIT LARGELY UPHOLDS ORDER CONFIRMING BOY SCOUTS CHAPTER 11 PLAN

Dan B. Prieto

Five years after it filed for bankruptcy protection in 2020 to deal with thousands of sexual abuse claims, the Boy Scouts of America reached a significant milestone when the U.S. Court of Appeals for the Third Circuit recently rejected the most significant challenges to the organization's chapter 11 plan, which established a trust to pay the claims of abuse victims. In *In re Boy Scouts of Am.*, 137 F.4th 126 (3d Cir. 2025), *reh'g denied*, Nos. 23-1664 *et al.* (3d Cir. June 13, 2025), the court of appeals ruled that:

- An appeal filed by abuse claimants of the bankruptcy court order confirming the plan, which effectuated a global settlement involving the establishment of a trust to satisfy abuse claims and a buyback of insurance policies by insurers under section 363(b) of the Bankruptcy Code to fund the trust in exchange for a nonconsensual release of all liabilities, must be dismissed as "statutorily moot" because the abuse claimants were challenging a bankruptcy sale authorized as part of confirmation of a chapter 11 plan and failed to obtain a stay pending appeal;
- An appeal filed by certain nonsettling insurers seeking minor modifications to the plan to preserve their rights was not statutorily moot because the relief sought would not materially impact the settlement and insurance policy buyback;
- The insurance policy buyback transaction approved under section 363(b) was not an impermissible *sub rosa* chapter 11 plan;
- The nonsettling insurers' appeal was not "equitably moot" because the relief they sought did not threaten to unscramble the chapter 11 plan; and
- The plan did not need to be modified to adequately preserve the rights of certain nonsettling insurers, but had to be changed to ensure that other nonsettling insurers' claims were paid in full because, otherwise, the plan violated the prohibition against nonconsensual third-party releases as set forth in the U.S. Supreme Court's 2024 ruling in *Harrington, United States Trustee, Region 2 v. Purdue Pharma L.P.*

MOOTNESS

"Mootness" is a doctrine that precludes a reviewing court from reaching the underlying merits of a controversy. An appeal can be either constitutionally, statutorily, or equitably moot. Constitutional mootness is derived from Article III of the U.S. Constitution, which limits the jurisdiction of federal courts to actual cases or controversies and, in furtherance of the goal of conserving judicial resources, precludes adjudication of cases that are hypothetical or merely advisory.

An appeal can also be rendered moot (or otherwise foreclosed) by statute. For example, section 363(m) of the Bankruptcy Code provides as follows:

> The reversal or modification on appeal of an authorization [of a sale or lease of property in bankruptcy] does not affect the validity of a sale or lease under such authorization to an entity that purchased or leased such property in good faith, whether or not such entity knew of the pendency of the appeal, unless such authorization and such sale or lease were stayed pending appeal.

11 U.S.C. § 363(m).

Section 363(m) provides powerful protections for good-faith purchases in bankruptcy sales by limiting appellate review of the court's authorization of the transaction. *See Made in Detroit, Inc. v. Official Comm. of Unsecured Creditors of Made in Detroit, Inc. (In re Made in Detroit, Inc.)*, 414 F.3d 576, 581 (6th Cir. 2005) ("'Section 363(m) protects the reasonable expectations of good faith third-party purchasers by preventing the overturning of a completed sale, absent a stay, and it safeguards the finality of the bankruptcy sale.'") (quoting *Official Comm. of Unsecured Creditors v. Trism, Inc. (In re Trism, Inc.)*, 328 F.3d 1003, 1006 (8th Cir. 2003)).

The provision serves the interests of finality and certainty in bankruptcy sale transactions and encourages bidding for estate property. *See In re Sneed Shipbuilding, Inc.*, 916 F.3d 405, 409 (5th Cir. 2019) ("If deference were not paid to the policy of speedy and final bankruptcy sales, potential buyers would not even consider purchasing any bankrupt's property.") (internal citations omitted); *In re Palmer Equip., LLC*, 623 B.R. 804, 808 (Bankr. D. Utah 2020) (section 363(m)'s protection is vital to encouraging buyers to purchase the debtor's property and thus ensuring that adequate sources of financing are available).

The federal circuit courts of appeals had disagreed over whether section 363(m) is jurisdictional, such that the failure to obtain a stay pending appeal of a sale order deprives an appellate court of jurisdiction to hear the appeal outside of the limited issue of whether the sale was made to a good-faith purchaser. *Compare Su v. C Whale Corp. (In re C Whale Corp.)*, 2022 WL 135125, *4 (5th Cir. Jan. 13, 2022) (section 363(m) is jurisdictional and precludes an appeal of an unstayed order approving a bankruptcy sale); and *Sears v. U.S. Trustee (In re AFY)*, 734 F.3d 810, 816 (8th Cir. 2013) (mootness under section 363(m) deprives an appellate court from hearing an appeal of an unstayed sale order) *with Reynolds v. ServisFirst Bank (In re Stanford)*, 17 F.4th 116, 122 (11th Cir. 2021) ("Statutory mootness under 363(m) . . . is not jurisdictional. Though it provides a defense against appeals from bankruptcy court orders, 'even an ironclad defense, does not defeat jurisdiction.'"). The U.S. Supreme Court resolved this circuit split in *MOAC Mall Holdings LLC v. Transform Holdco LLC*, 598 U.S. 288 (2023), ruling that section 363(m) is not jurisdictional.

The court-fashioned remedy of "equitable mootness" bars adjudication of an appeal when a comprehensive change of circumstances has occurred, such that it would be inequitable for a reviewing court to address the merits of the appeal. In bankruptcy cases, appellees often invoke equitable mootness as a basis for precluding appellate review of an order confirming a chapter 11 plan.

The doctrine of equitable mootness is sometimes criticized as an abrogation of federal courts' "virtually unflagging obligation" to hear appeals within their jurisdiction. *See In re One2One Commc'ns, LLC*, 805 F.3d 428, 433 (3d Cir. 2015); *In re Charter Commc'ns, Inc.*, 691 F.3d 476, 481 (2d Cir. 2012). According to this view, dismissing an appeal on equitable mootness grounds "should be the rare exception." *In re Tribune Media Co.*, 799 F.3d 272, 288 (3d Cir. 2015); *accord In re Pac. Lumber Co.*, 584 F.3d 229, 240 (5th Cir. 2009) (equitable mootness should be applied "with a scalpel rather than an axe").

Moreover, although the U.S. Supreme Court has declined on several occasions to weigh in on the propriety of the equitable mootness doctrine, it recently expressed skepticism regarding the concept of mootness generally as a bar to a federal court's consideration of the merits of any appeal. *See Transform Holdco*, 143 S. Ct. at 935 (in ruling that an order approving a lease assignment as a part of a bankruptcy sale transaction was not statutorily moot under section 363(m), the Court noted that "[o]ur cases disfavor these kinds of mootness arguments").

Substantially similar tests have been applied by most circuit courts in assessing whether an appeal of a chapter 11 confirmation order should be dismissed under equitable mootness. Those tests generally focus on whether the appellate court can fashion effective and equitable relief. *See, e.g., PPUC Pa. Pub. Util. Comm'n v. Gangi*, 874 F.3d 33, 37 (1st Cir. 2017) (considering whether: (i) the appellant diligently pursued all available remedies to obtain a stay of the confirmation order; (ii) the challenged chapter 11 plan had progressed "to a point well beyond any practicable appellate annulment"; and (iii) providing relief would harm innocent third parties); *JPMCC 2007-C1 Grasslawn Lodging, LLC v. Transwest Resort Props., Inc. (In re Transwest Resort Props., Inc.)*, 801 F.3d 1161, 1167–68 (9th Cir. 2015) (applying a four-factor test, including whether the court "can fashion effective and equitable relief without completely knocking the props out from under the plan and thereby creating an uncontrollable situation for the bankruptcy court"); *Tribune Media*, 799 F.3d at 278 (considering "(1) whether a confirmed plan has been substantially consummated; and (2) if so, whether granting the relief requested in the appeal will (a) fatally scramble the plan and/or (b) significantly harm third parties who have justifiably relied on plan confirmation"); *Search Market Direct, Inc. v. Jubber (In re Paige)*, 584 F.3d 1327, 1339 (10th Cir. 2009) (applying a six-factor test, including the likely impact upon a successful reorganization of the debtor if the appellant's challenge is successful); *In re United Producers, Inc.*, 526 F.3d 942, 947–48 (6th Cir. 2008) (three-factor test); *TNB Fin., Inc. v. James F. Parker Interests (In re Grimland, Inc.)*, 243 F.3d 228, 231 (5th Cir. 2001) (considering "(1) whether the complaining party has failed to obtain a stay, (2) whether the plan (here, the liquidation) has been substantially consummated, and (3) whether the relief requested would affect the rights of parties not before the court or the success of the plan").

A common element of almost all of these tests is whether the chapter 11 plan has been substantially consummated. Section 1101(2) of the Bankruptcy Code provides that "substantial consummation" of a chapter 11 plan occurs when substantially all property transfers proposed by the plan have been completed, the debtor or its successor has assumed control of the business and property dealt with by the plan, and plan distributions have commenced.

THIRD-PARTY RELEASES

In *Harrington, United States Trustee, Region 2 v. Purdue Pharma L.P.*, 603 U.S. 204 (2024), a 5–4 majority of the U.S. Supreme Court reversed and remanded a 2023 ruling by the U.S. Court of Appeals for the Second Circuit affirming the bankruptcy court confirming the chapter 11 plan of pharmaceutical giant Purdue Pharma L.P. According to the majority, no provision in the Bankruptcy Code other than section 524(g) (providing for the creation of a trust for the payment of asbestos personal injury claims) authorizes a chapter 11 plan to release the claims of nonconsenting creditors against nondebtor entities absent full satisfaction of such claims.

In so ruling, the majority reasoned that:

- The "catchall" provision in section 1123(b)(6) of the Bankruptcy Code stating that a chapter 11 plan "may" also "include any other appropriate provision not inconsistent with the applicable provisions of this title" must be construed narrowly in light of its surrounding context and read to "embrace only objects similar in nature" to the specific examples preceding it, all of which deal with the relationship between a debtor and its creditors, rather than the "radically different" power to discharge the debts of a nondebtor without the consent of affected creditors;
- The proponents of a chapter 11 plan cannot evade the Bankruptcy Code's general limitation that a discharge applies only to debtors who place "substantially all of their assets on the table" and its exclusion from discharge of debts based on "fraud" or those alleging "willful and malicious injury" simply "by rebranding the discharge a 'release'"; and
- If lawmakers had intended "to reshape traditional practice so profoundly" in the Bankruptcy Code, compared to its predecessor statutes, by "extending to courts the capacious new power the plan proponents claim, one might have expected them to say so expressly somewhere" in the Bankruptcy Code itself.

The majority emphasized that nothing in its ruling should be construed to call into question consensual releases in a bankruptcy reorganization plan, and further declined to express a view on what qualifies as a consensual release, observing that those sorts of releases pose different questions and may rest on different legal grounds. Similarly, the majority declined to pass upon a plan that provides for full satisfaction of claims against a nondebtor. The majority also expressly cabined its ruling to the situation before it, noting that "we hold only that the [B]ankruptcy [C]ode does not authorize a release and injunction that, as part of a plan of reorganization under Chapter 11, effectively seeks to discharge claims against a nondebtor without the consent of affected claimants." *Id.* at 206.

SUB ROSA CHAPTER 11 PLANS

Unless a chapter 11 case is dismissed or converted to a chapter 7 liquidation, the ordinary culmination of the process is the bankruptcy court's confirmation of a chapter 11 plan (either a plan of reorganization or a liquidating plan). During the plan confirmation process, the Bankruptcy Code gives creditors and interest holders in the case various substantive and procedural protections, including, among other things: (i) the requirement that they be provided with adequate information to decide whether to accept or reject a plan; (ii) the right to vote on a plan that impairs their rights; and (iii) minimum standards governing the treatment of their claims or interests under a nonconsensual plan (e.g., the absolute priority rule).

However, certain events that precede (or supersede) confirmation of plan, such as a global settlement among major stakeholders, a sale of substantially all of the debtor's assets, or a comprehensive agreement in anticipation of a "structured dismissal," may be a *de facto* chapter 11 plan without providing all parties with the same protections as the plan confirmation process. Such "*sub rosa*" plans are prohibited "based on a fear that a debtor-in-possession will enter into transactions that will, in effect, '"short circuit the requirements of Chapter 11 for confirmation of a reorganization plan."' *Motorola, Inc. v. Official Comm. of Unsecured Creditors (In re Iridium Operating LLC)*, 478 F.3d 452, 466 (2d Cir. 2007) (citing *Pension Benefit Guar. Corp. v. Braniff Airways, Inc. (In re Braniff Airways, Inc.)*, 700 F.2d 935, 940 (5th Cir. 1983)); *In re Miami Metals I, Inc.*, 603 B.R. 531, 536 (Bankr. S.D.N.Y. 2019). The terms of proposed DIP financing may also be a prohibited *sub rosa* plan. *See Resolution Tr. Corp. v. Official Unsecured Creditors Comm. (In re Def. Drug Stores, Inc.)*, 145 B.R. 312, 317 (B.A.P. 9th Cir. 1992) ("[A] bankruptcy court cannot, under the guise of section 364, approve financing arrangements that amount to a plan of reorganization but evade confirmation requirements"); *In re Belk Props., LLC*, 421 B.R. 221, 225–26 (Bankr. N.D. Miss. 2009); *In re Chevy Devco*, 78 B.R. 585, 589 (Bankr. C.D. Cal. 1987).

BOY SCOUTS

Facing tens of thousands of sexual abuse claims, the Boy Scouts of America, Inc., a more than century-old congressionally chartered, nonprofit youth development organization operating nationwide through tens of thousands of nondebtor entities, filed for chapter 11 protection in February 2020 in the District of

Delaware, together with its affiliate Delaware BSA, LLC (together, "BSA"), in an effort to reach a global settlement of tort claims with claimants, insurers, and other interested parties. At the time of the filing, BSA had long maintained insurance policies covering various potential liabilities, including abuse claims.

In September 2022, after mediated negotiations among the parties resulted in the framework of a global settlement, the bankruptcy court confirmed a chapter 11 plan for BSA. The plan provided for the creation of an approximately $2.5 billion trust (the "settlement trust") funded by the sale of certain assets and contributions from BSA and certain nondebtors to make payments to abuse claimants. The vast majority of the funding for the settlement trust was derived from the proceeds of BSA's sale of its liability insurance policies back to a group of its pre-petition insurers (the "settling insurers"). This "insurance policy buyback" was effectuated by means of materially identical settlement agreements between BSA and each of the settling insurers.

Those agreements provided that each settling insurer agreed to pay a specified amount to the settlement trust in exchange for which: (i) BSA would assign and/or sell their policies to the settling insurers free and clear of all claims and interests under sections 363(b) and 363(f) of the Bankruptcy Code; and (ii) the settling insurers, "on behalf of themselves, the named insured(s) under their policies and any additional insureds (whether specifically named or categorically identified)," would receive a "complete release from all parties . . . of all causes of action arising out of their respective insurance policies and any liability for Abuse Claims."

If an insurer (settling or otherwise) declined to provide coverage for an abuse claim, the settlement trust could sue the insurer under the insurance policy in a collateral proceeding.

BSA's chapter 11 plan also included a "judgment reduction provision" limiting the recoveries of nonsettling insurance companies ("nonsettling insurers") from the settlement trust under certain circumstances. Specifically, if the settlement trust obtained a judgment against a nonsettling insurer in a coverage dispute, that nonsettling insurer could obtain its own judgment imposing liability on another insurer for some (or all) of the settlement trust's judgment, after which the nonsettling insurer could offset that portion of its liability. However, a nonsettling insurer under certain circumstances would not be fully compensated by the settlement trust for defense costs that it would otherwise be entitled to under its insurance policy due to the releases and injunctions included in the plan.

All creditor classes voted to accept BSA's plan. However, nearly 40 parties—falling into two categories consisting of: (i) two groups of nonsettling insurers (the "certain insurers" and the "Allianz insurers"); and (ii) direct abuse claimants (the "abuse claimants")—filed objections to confirmation of the plan. After a lengthy confirmation trial, the bankruptcy court approved the key elements of BSA's chapter 11 plan in July 2022, and after certain revisions were made to the plan, the court confirmed the plan in its entirety in September 2022.

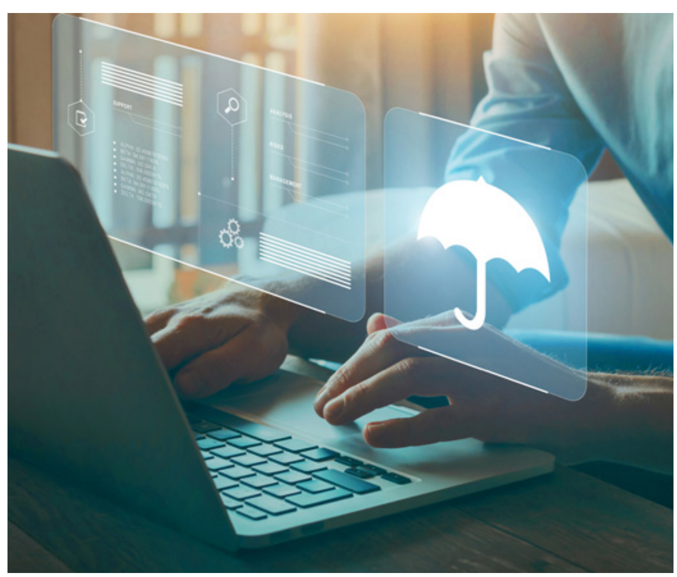
Various nonsettling insurers and abuse claimants (collectively, the "appellants") appealed the confirmation order. The abuse claimants argued that the confirmation order should be reversed because the plan impermissibly included nonconsensual third-party releases. The nonsettling insurers sought narrower relief in the form of the addition of language to the plan and the confirmation order clarifying that their rights and defenses under their insurance policies were preserved—in essence, to protect rights that they would have had outside of bankruptcy to collect on their defense costs and excess liability claims (now from the settlement trust).

The district court affirmed the plan confirmation order on March 28, 2023. The appellants appealed the ruling to the Third Circuit. On April 11, 2023, the district court denied the motions of the appellants to stay the confirmation order pending resolution of the Third Circuit appeal.

BSA's chapter 11 plan became effective on April 19, 2023.

The Third Circuit also denied the appellants' motions for a stay of the confirmation order pending the appeal, but without prejudice to their renewed request for a stay from the district court after the Supreme Court agreed to hear *Purdue* on August 10, 2023. The district court again denied the appellants' request for a stay in October 2023, and the Third Circuit similarly denied their renewed request for a stay on November 2, 2023.

The Supreme Court issued a brief administrative stay of the plan confirmation order on February 16, 2024, but ultimately refused to issue a stay in a February 22, 2024, order. After opening briefs were filed in the Third Circuit appeal, the settling insurers (later joined by BSA) moved to dismiss the appeals as equitably and statutorily moot.



THE THIRD CIRCUIT'S RULING

A three-judge panel of the Third Circuit dismissed the appeal in part, affirmed the district court's order in part, reversed it in part, and remanded the case below.

Statutory Mootness, Sub Rosa Plan. The Third Circuit majority concluded that the appeal of the nonsettling insurers was not statutorily moot under section 363(m) because the relief they sought — addition to the plan of language preserving their rights — was "a limited form of relief sufficiently collateral to the insurance policy buyback and, therefore, their appeals avoid[ed] triggering § 363(m)." *Boy Scouts*, 137 F.4th at 150. Writing for the majority, U.S. Circuit Court Judge Cheryl Ann Krause explained that the proposed changes did not implicate any provision of the insurance policy buyback, and would not materially increase the purchase price paid by the settling insurers.

However, the Third Circuit majority concluded that the appeals filed by the abuse claimants were mooted by section 363(m) because the relief they requested — reversal of the plan confirmation order — "would reverse on appeal an authorization made pursuant to § 363(b)—the very result § 363(m) prohibits." *Id.* at 151. In so ruling, the majority rejected the argument that the insurance policy buyback had not yet occurred because the sale was expressly conditioned in the settlement agreements on the plan confirmation order becoming a "final" (and therefore immediately appealable) order. According to Judge Krause: (i) the insurance policy buyback was completed on the plan's effective date, meaning that "the policies have been sold"; and (ii) "even if that were not the case, § 363(m) speaks in terms of unstayed authorizations under § 363(b)—it does not include an inchoate requirement that a § 363(b) sale be consummated or otherwise effectuated." *Id.* at *20. "By any measure," she wrote, "§ 363(m) applies here." *Id.* at 152.

The Third Circuit majority also rejected the abuse claimants' argument that section 363(m) did not apply because the insurance policy buyback was not a sale under section 363(b) of the Bankruptcy Code, but rather, a sale transaction authorized as part of a chapter 11 plan. Judge Krause explained that the Third Circuit has previously held that "a confirmation order that 'authorized and directed' the consummation of a previously approved asset sale (styled as a 'merger' and conditioned upon the eventual confirmation of a reorganization plan) qualified as an authorization of a sale for purposes of § 363(m)." *Id.* at 153 (citing *In re Energy Future Holdings Corp.*, 949 F.3d 806 819–20 (3d Cir. 2020); *In re Fieldwood Energy LLC*, 93 F.4th 817, 825 (5th Cir. 2024); *In re Made in Detroit, Inc.*, 414 F.3d 576, 582–83 (6th Cir. 2005)). In this case, she wrote, the plan confirmation order, "which authorized the sale of BSA's insurance policies, equally serves as an 'authorization ... of a sale' under § 363(m)." *Id.*

In addition, Judge Krause dismissed as unfounded the abuse claimants' contention that the insurance policy buyback was not a true section 363(b) sale because the settling insurers were not third parties but, rather, insiders that stood to profit from the sale by receiving releases under the chapter 11 plan. According to the Third Circuit majority, "this contention cannot be squared with the text of § 363(m), which 'contains no exception for sales to creditors, or other parties to the bankruptcy proceedings.'" *Id.* at 153 n.10 (citing *Krebs Chrysler-Plymouth, Inc. v. Valley Motors, Inc.*, 141 F.3d 490, 500 (3d Cir. 1998)).

The Third Circuit majority similarly rejected the abuse claimants' argument that section 363(m) did not moot their appeal because the settling insurers were not "good faith purchasers," having bought back their policies even though they knew that the abuse claimants asserted rights in the policies and intended to challenge the plan on appeal. Judge Krause explained that this argument "ignores both the text of § 363(m)," which extends protection to purchasers "whether or not such entity knew of the pendency of [an] appeal" challenging the sale authorization, and the bankruptcy court's amply supported factual finding that each of the settling insurers was a "good faith purchaser for value within the meaning of section 363(m) of the Bankruptcy Code." *Id.* at 152.

The Third Circuit majority was unpersuaded by the argument that the abuse claimants were not attempting to unravel the insurance policy buyback, but merely sought removal of the third-party release provisions included in the settlement agreements and confirmed as part of BSA's chapter 11 plan. Judge Krause characterized this as "a distinction without a difference." She explained that the releases were part of the consideration for the insurance policy buyback, and without them, the settling insurers would receive less than they bargained for in exchange for their contributions to the settlement trust, which "'would materially increase ... the purchase price' and, thus, 'would plainly affect the validity of the sale.'" *Id.* at 154 (quoting *Energy Future Holdings*, 949 F.3d at 821). Moreover, Judge Krause emphasized, granting the relief requested by the abuse claimants "would send BSA and over 82,000 abuse claimants back to square one and would almost certainly unleash years of litigation in the wake of the vacated Plan." *Id.*

Judge Krause also rejected the abuse claimants' contention that a finding of statutory mootness in this case "would effectively 'immuniz[e] the substantive terms of a plan from appellate review' anytime a plan involves a § 363(b) sale." *Id.* at 155 (citation omitted). According to the Third Circuit majority, "our holding does no such thing, and we take this opportunity to emphasize the narrowness of our decision in two respects: the limited scope of § 363(m) and the boundaries of so-called 'sub rosa' plans that fall beyond it."

Judge Krause noted that section 363(m) insulates authorized bankruptcy sales from modification absent a stay pending appeal, but does not immunize "entire reorganization plans" from appellate review whenever they involve approval of section 363(b) sales. According to Judge Krause, a challenge to a bankruptcy sale that is "collateral" to, or would not otherwise "affect the validity of the sale," falls outside the scope of section 363(m), and "given the breadth of issues a reorganization plan may resolve that do not necessarily implicate the terms of a § 363(b) sale, *see* 11 U.S.C. § 1123(a)–(b), the vast majority of challenges, no doubt, will fall into this category." *Id.* (citation omitted).

The Third Circuit majority further determined that its application of section 363(m) to the insurance policy buyback under section 363(b) does not "countenance the use of § 363(b) during the course of bankruptcy proceedings to effectuate a *sub rosa* plan by 'dictat[ing] the terms of a plan.'" *Id.* (citation omitted). The Third Circuit majority noted that "the *sub rosa* doctrine [is] an inherent limitation to authorizations under § 363(b)," and endorsed the approach taken by sister circuits in "applying the *sub rosa* doctrine where warranted," specifically in cases where section 363(b) sale proponents attempt to circumvent the stakeholder procedural protections incorporated in the Bankruptcy Code to govern the chapter 11 plan confirmation process. *Id*. at 156-57 and 157 n.16 (citing *In re Braniff Airways, Inc.*, 700 F.2d 935 (5th Cir. 1983); *In re Lionel Corp.*, 722 F.2d 1063 (2d Cir. 1983)). According to Judge Krause, "[t]his case raises none of those concerns," and "we are confident that bankruptcy and district court judges—and ultimately this Court—are eminently capable of policing the bounds of permissible § 363(b) sales and seeing cleverly disguised transactions for what they are." *Id.* at 156–57 (footnotes omitted).

Equitable Mootness. The Third Circuit majority concluded that, due to the limited relief sought by the nonsettling insurers, "the success of their appeals does not threaten to fatally scramble the Plan . . . [and therefore] equitable mootness does not prevent us from reaching the merits of their claims." *Id.* at 159. In the Third Circuit, Judge Kraus explained, a court considering whether an appeal is equitably moot must inquire: (i) whether the confirmed chapter 11 plan has been substantially consummated; and (ii) if so, "whether granting the relief requested in the appeal will (a) fatally scramble the plan and/or (b) significantly harm third parties who have justifiably relied on plan confirmation." *Id.* at 160 (quoting *In re SemCrude, L.P.*, 728 F.3d 314, 321 (3d Cir. 2013)).

The Third Circuit majority ruled BSA's chapter 11 plan had been substantially consummated because: (i) the settling insurers' placement of funds into escrow as part of the insurance policy buyback qualified as a "transfer" within the meaning of section 1101(2)(A) of the Bankruptcy Code, even though the transfer was conditioned upon satisfaction of the conditions precedent to the settling insurers' funding obligations under the chapter 11 plan, including the finality of the confirmation order; (ii) BSA had been operating as a recognized charitable nonprofit since emerging from bankruptcy in April 2023 and had fully resumed operating, as required by section 1101(2)(B); and (iii) distributions to creditors had begun under the chapter 11 plan's settlement trust, as required by section 1101(2)(C). *Id.* at 161–63.

In addition, the Third Circuit majority determined that, due to the "narrow, cabined relief" sought by the nonsettling insurers, BSA and the settling insurers failed to show that such relief would imperil the success of the chapter 11 plan. Judge Krause wrote that, "[w]e can hardly say that these minor changes—none of which disrupts the funding to the settlement trust or the bargain struck between BSA and the settling insurers, or requires clawing back distributions already made to abuse claimants—meets the high thresholding [sic] of 'knock[ing] the props out from under' the Plan." *Id.* at 163 (citations omitted).

The Third Circuit majority was unpersuaded by the certain insurers' contention that the chapter 11 plan, the confirmation order, and the settlement trust did not adequately preserve their rights and defenses under their insurance policies. Because the express language of each of these adequately protected the certain insurers, the Third Circuit majority "decline[d] to rewrite the Plan and fasten suspenders to this already well-secured belt." For the same reason, the Third Circuit majority also rejected the certain insurers' argument that BSA did not propose its chapter 11 plan in good faith because the plan failed to include language adequately protecting their rights and defenses. *Id.* at 166–67.

Finally, the Third Circuit majority agreed with the Allianz insurers' argument that the judgment reduction provision violated *Purdue* because the nonsettling insurers did not consent to the release of their claims and might not be fully compensated for their extinguished claims. Relying on the principle that a plaintiff is entitled to only one satisfaction for each injury, BSA argued that the nonconsensual third-party release was justified by the fact that the trust distribution procedures would "streamline and reduce defense costs by resolving claims consensually through an out-of-court process," thus significantly reducing the likelihood that the nonsettling insurers would be saddled with material defense costs. The court rejected this argument, noting that the district court did not find that the nonsettling insurers would be fully compensated for payment of defense costs, but instead merely found that they would be "adequately protected" because their defense costs would be reduced. The court accordingly reversed the district court's judgment as to the Allianz insurers' claims and remanded the case below with a direction to modify the judgment reduction provision to ensure full payment of their claims from the settlement trust.

CONCURRING OPINION

U.S. Circuit Judge Marjorie O. Rendell filed an opinion in which she concurred in the result but characterized as "fundamentally flawed" the majority's decision to treat the abuse claimants' appeal as an appeal from a section 363 sale. According to Judge Rendell, section 363(m) clearly indicates "that it does not apply to sales in reorganization plans" and "the nonconsensual third-party releases were not accomplished by way of the purported § 363 authorization, but by way of plan confirmation." Instead, she explained, the abuse claimants' appeal should have been treated as challenge to the plan confirmation order and dismissed as being equitably moot. *Id.* at 170–77 (concurring opinion).

OUTLOOK

The Third Circuit emphasized in *Boy Scouts* that its decision depended on the "unique characteristics" of BSA's chapter 11 plan, the section 363(b) sale transaction involving the insurance policy buyback, and the relief sought by the appellants. It further noted in *dicta* that, "[i]f proposed today, the Plan would be unconfirmable in the wake of *Purdue*," but that the "Bankruptcy Code prevents us from disrupting the nonconsensual third-party releases in BSA's Plan at this late stage."

Judge Rendell's criticism of the majority's conclusion that the abuse claimants' appeal was statutorily moot under section 363(m) because that provision does not apply to sales effectuated under a chapter 11 plan is not without support. As she noted, several courts have suggested that plan sales do not fall within the ambit of section 363(m). *Id.* at 172 and 172 n.6 (citing *Miami Ctr. Ltd. P'ship v. Bank of New York*, 838 F.2d 1547, 1553 (11th Cir. 1988) (holding that section 363(m) does not apply to a sale under a liquidation plan); *In re Texas Extrusion Corp.*, 844 F.2d 1142, 1165 (5th Cir. 1988) (expressing doubt as to whether plan sales may invoke the "shield" of § 363(m) given the "definite implication that [§ 363(b), (c), and (m)] concern the trustee's authority during the administration of the estate and not at the final disposition of the property of the estate pursuant to a plan of reorganization"); *In re Bardos*, 2014 WL 3703923, at *9 (B.A.P. 9th Cir. July 25, 2014) (concluding that section 363(m) did not bar an appeal involving a plan sale, as plan sales are authorized under section 1123(a)(5)(B), not section 363); *In re Smurfit-Stone Container Corp.*, 2010 WL 2403793, at *10 (Bankr. D. Del. June 11, 2010) (suggesting that section 363 does not apply to plan sales)). Judge Rendell acknowledged, however, that some courts have held to the contrary. *Id.* (citing *In re Fieldwood Energy LLC*, 93 F.4th 817, 825 (5th Cir. 2024) (applying section 363(m) to a sale authorized by a confirmation order); *In re Made in Detroit, Inc.*, 414 F.3d 576, 582–83 (6th Cir. 2005) (same)).

Disagreement in the circuits on this issue may be an invitation to U.S. Supreme Court review of the Third Circuit's decision.

Equitable mootness has long been a controversial doctrine, with courts disagreeing over when it should properly be deployed to bar appeals of orders confirming chapter 11 plans. The Supreme Court has declined on several occasions to weigh in on the propriety of the equitable mootness doctrine. However, it recently expressed skepticism regarding the concept of mootness generally as a bar to a federal court's consideration of the merits of any appeal. *See MOAC Mall Holdings LLC v. Transform Holdco LLC*, 143 S. Ct. 927, 935 (2023) (in ruling that an order approving a lease assignment as a part of a bankruptcy sale transaction was not statutorily moot under section 363(m) of the Bankruptcy Code, the Court noted that "[o]ur cases disfavor these kinds of mootness arguments"). This too may be an issue worthy of Supreme Court review to clarify the scope of the doctrine.

On June 13, 2025, the Third Circuit denied a motion filed by certain abuse claimants to reconsider its ruling.

CLARITY IN SINGAPORE: HOW COMI IS DETERMINED UNDER THE UNCITRAL MODEL LAW ON CROSS-BORDER INSOLVENCY

Corinne Ball • Jasper Berkenbosch • David Harding
Sushma Jobanputra • Vinay Kurien • Ben Larkin • Dan T. Moss

In *In Re Fullerton Capital Ltd* [2025] SGCA 11, a British Virgin Islands ("BVI")-incorporated company entered into insolvency proceedings in BVI. The liquidators sought recognition of the BVI liquidation as a "foreign main proceeding" in Singapore under the UNCITRAL Model Law on Cross-Border Insolvency, as adopted in the Insolvency, Restructuring, and Dissolution Act 2018 (the "Model Law"). A former director challenged the application, arguing that the company's "centre of main interests" ("COMI") was not in the BVI.

The Singapore Court of Appeal upheld the lower court's decision, confirming that the presumption under Article 16(3) of the Model Law—that a debtor's COMI is at its registered office—must be the starting point of the analysis. The court clarified that this presumption can be rebutted only if the party challenging it proves, on a balance of probabilities, that another jurisdiction has a comparatively stronger connection to the debtor. The court also clarified that the relevant time for assessing COMI is the date of the recognition application, and that the actions of foreign representatives post-commencement may be relevant, depending on the circumstances.

This decision reinforces Singapore's commitment to the principle of "modified universalism" in cross-border insolvency and provides much-needed clarity on the COMI determination process. It sets a high evidentiary threshold for rebutting the registered office presumption and signals to practitioners that a fact-intensive, comparative analysis is required. The judgment also recognizes the potential for COMI to shift during insolvency and underscores the importance of objective, third-party ascertainable evidence in COMI disputes.

REBUTTABLE PRESUMPTION OF COMI UNDER THE MODEL LAW

Article 16(3) of the Model Law provides that a debtor's COMI is presumed to be the location of its registered office, once proof of the registered office is provided. The court of appeal made clear that this presumption is not a mere tie-breaker or fallback, but the mandatory starting point for the COMI analysis. The burden of proof to rebut this presumption lies squarely on the party asserting that the COMI is elsewhere, and the standard of proof is the balance of probabilities.

The court rejected the U.S. approach, which treats the presumption as imposing only an evidentiary burden and allows the burden to shift back to the applicant upon the production of some contrary evidence. *See In re Tri Continental Exchange Ltd.*, 349 B.R. 627 (Bankr. E.D. Cal. 2006). In Singapore, the legal burden remains on the party seeking to rebut the presumption throughout the analysis.

THE RELATIVITY OF COMI AND THE NEED FOR A POSITIVE CASE

COMI is a relative concept. It is not enough to simply show a lack of connection to the registered office. The party seeking to displace the presumption must identify a specific alternative jurisdiction and demonstrate, with objective and concrete evidence, that this jurisdiction is the true COMI. The analysis is comparative: The court must be satisfied that the alternative jurisdiction has a stronger connection to the debtor than the registered office.

Objective, third-party ascertainable factors are key—such as the location of management, principal assets, or main creditors. General assertions or negative evidence (such as the absence of business activity at the registered office) will not suffice. In Singapore, the legal burden remains on the party seeking to rebut the presumption throughout the analysis.

TIMING OF COMI ASSESSMENT AND THE ROLE OF FOREIGN REPRESENTATIVES' ACTIONS

The relevant time for determining a debtor's COMI is the date of the recognition application. The court moved away from a rigid rule that would exclude the actions of foreign representatives after the commencement of insolvency proceedings. Instead, the court adopted a nuanced approach: The actions of foreign representatives post-commencement may be relevant to the COMI analysis, but the weight accorded to such actions will depend on the circumstances, including whether there is evidence of abusive forum shopping.

This means that a debtor's COMI could shift from one location to another from the time it was "alive and flourishing," to the time it had begun restructuring, to the time recognition of the foreign proceeding is sought. The court emphasized that the analysis is highly fact-specific and that the quality, not just the quantity, of connecting factors is critical.

PREPARING FOR A FACT-INTENSIVE INQUIRY

The court's approach to COMI is highly fact-specific. Practitioners should be ready to present comprehensive, objective evidence regarding the debtor's operations, management, creditors, and business activities. The analysis may be particularly complex where a debtor has operations or management spread across several countries, or where group structures are involved. In such cases, practitioners should anticipate the need to address multiple potential COMIs and be prepared to demonstrate why one jurisdiction has a stronger connection than all others.

Even if the registered office is a mere formality and the debtor has little or no substantive connection to that jurisdiction, the presumption will be displaced only if there is sufficient, objective evidence of a stronger connection elsewhere. The absence of activity at the registered office does not, by itself, rebut the presumption.

KEY TAKEAWAYS

- The presumption that the registered office is the COMI is the starting point and must be affirmatively rebutted on a balance of probabilities.
- COMI is a relative concept: A specific alternative jurisdiction must be identified and substantiated with objective evidence.
- The relevant date for assessing COMI is the date of the recognition application; both pre- and post-commencement activities may be relevant, but their weight depends on the context and the absence of abusive forum shopping.
- Practitioners should prepare for a fact-intensive inquiry and be ready to address the possibility of multiple potential COMIs, especially in complex or multinational structures.
- The decision provides greater legal certainty for creditors and stakeholders in cross-border insolvency, reinforcing Singapore's position as a sophisticated and reliable jurisdiction for cross-border restructuring and insolvency matters.

Kai Yi Ng and Nigel Cheong, associates in Jones Day's Singapore Office, assisted in the preparation of this article.

DELAWARE BANKRUPTCY COURT ALLOWS TRUSTEE TO PURSUE RECOVERY OF FRAUDULENT TRANSFERS FOR THE SOLE BENEFIT OF SUBORDINATED CLAIMHOLDERS

Daniel J. Merrett • Ashton T. Williams

The Bankruptcy Code provides a bankruptcy trustee or chapter 11 debtor-in-possession ("DIP") with the power to avoid and recover certain fraudulent transfers that a creditor could have avoided outside of bankruptcy under applicable non-bankruptcy law. In *In re ONH AFC CS Investors, LLC*, 2025 WL 1353850 (Bankr. D. Del. May 8, 2025), the U.S. Bankruptcy Court for the District of Delaware was presented with the question of whether a bankruptcy trustee may exercise this power for the benefit of defrauded investors whose claims were statutorily subordinated to the level of equity by operation of section 510(b) of the Bankruptcy Code.

Persuaded by the reasoning of another Delaware bankruptcy court, the bankruptcy court in *ONH* concluded that, generally, a bankruptcy trustee cannot seek to avoid fraudulent transfers for the benefit of equity holders. With respect to the specific situation presented, however, the court ruled that the Bankruptcy Code's subordination of certain claims of investors did not preclude the trustee from bringing fraudulent transfer actions for their benefit.

AVOIDANCE OF TRANSFERS IN BANKRUPTCY

The Bankruptcy Code provides a trustee or DIP with the power to avoid certain pre-bankruptcy transfers or obligations. For example, section 547 authorizes a trustee or DIP to avoid a transfer that is preferential because the transfer was made to a creditor by an insolvent debtor on account of an antecedent debt within 90 days prior to a bankruptcy filing (or one year if the recipient is an insider) that permits the creditor to receive more than it would have recovered without the transfer in a hypothetical chapter 7 liquidation. Section 548 of the Bankruptcy Code authorizes the avoidance of pre-bankruptcy transfers or obligations that either are made with the intent to hinder, delay, or defraud creditors or are constructively fraudulent because the debtor was insolvent at the time of the transfer (or rendered insolvent by it) and received inadequate consideration in exchange.

Section 544(b) allows a trustee or DIP to assert avoidance claims that could have been asserted by an actual unsecured "triggering" creditor under applicable non-bankruptcy (generally state) law, such as the Uniform Voidable Transactions Act or its predecessor, the Uniform Fraudulent Transfer Act, which have been enacted in nearly every state. *See generally* COLLIER ON BANKRUPTCY ("COLLIER") ¶ 544.06 (16th ed. 2025). Section 544(b) is an important tool, principally because the reach-back period for avoidance of fraudulent transfers under state fraudulent transfer laws (or even non-bankruptcy federal laws, such as the Internal Revenue Code) is typically longer than the two-year period for avoidance of fraudulent transfers provided under section 548. *Id.*

SUBORDINATION OF INVESTOR CLAIMS IN BANKRUPTCY

The concept of claim, debt, or lien subordination is well recognized under federal bankruptcy law. A bankruptcy court's ability to reorder the relative priority of claims or debts under appropriate circumstances is part and parcel of its broad powers as a court of equity. The statutory vehicle for applying these powers in bankruptcy is section 510 of the Bankruptcy Code.

Section 510(a) provides that an enforceable pre-bankruptcy subordination agreement will be enforced in a bankruptcy case. Section 510(b) generally subordinates claims arising from the purchase or sale of a security of the debtor to all claims that are senior or equal to the claim or interest represented by the security. Under section 510(c), a bankruptcy court can equitably subordinate the claim of a creditor or a shareholder to the claims of other creditors or interest holders in cases of misconduct or unfair advantage.

Section 510(b) provides as follows:

> For the purpose of distribution under this title, a claim arising from rescission of a purchase or sale of a security of the debtor or of an affiliate of the debtor, for damages arising from the purchase or sale of such a security, or for reimbursement or contribution allowed under section 502 on account of such a claim, shall be subordinated to all claims or interests that are senior to or equal the claim or interest represented by such security, except that if such security is common stock, such claim has the same priority as common stock.

11 U.S.C. § 510(b).

The purpose of section 510(b), consistent with the Bankruptcy Code's "absolute priority rule" (generally providing that, absent consent, creditor claims must be paid in full before equity holders can receive any value) is to prevent the bootstrapping of equity interests into claims that are on a par with other creditor claims. *See generally* COLLIER at ¶ 510.04[1].

Interest holders have resorted to a wide array of devices and legal arguments in an effort to overcome the effect of section 510(b), including contractual provisions purporting to entitle them to damages upon the issuer's breach of a stock purchase agreement and alternative theories of recovery, such as unjust enrichment and constructive trust. *See Stucki v. Orwig*, 2013 WL 1499377 (N.D. Tex. Apr. 12, 2013) (discussing case law).

In deciding cases under section 510(b), some courts have highlighted the traditional allocation of risk between a company's shareholders and its creditors. Under this policy-based analysis, shareholders are deemed to undertake more risk in exchange for the potential to participate in the profits of the company, whereas creditors can expect only repayment of their fixed debts. Accordingly, shareholders, and not creditors, assume the risk of a wrongful or unlawful purchase or sale of securities.

This risk allocation model is sometimes referred to as the "Slain/Kripke theory of risk allocation," as described in a 1973 law review article written by Professors John J. Slain and Homer Kripke titled "The Interface Between Securities Regulation and Bankruptcy—Allocating the Risk of Illegal Securities Issuance Between Securityholders and the Issuer's Creditors," 48 N.Y.U.L. Rev. 261 (1973). *See, e.g., In re SeaQuest Diving LP*, 579 F.3d 411, 420 (5th Cir. 2009); *In re Betacom of Phoenix, Inc.*, 240 F.3d 823, 829 (9th Cir. 2001); *In re Granite Partners, L.P.*, 208 B.R. 332, 336 (Bankr. S.D.N.Y. 1997).

As a result of the parties' differing expectations for risk and return, it is perceived as unfair to allow a shareholder to recover from the limited assets of a debtor as a creditor by "converting" its equity stake into a claim through the prosecution of a successful securities lawsuit. The mechanism by which such a conversion is thwarted is subordination of the shareholder's claim under section 510(b).

Notwithstanding general agreement regarding the policy underlying section 510(b), courts have applied differing formulations in interpreting its language. *Compare In re American Housing Found.*, 785 F.3d 143, 156 (5th Cir. 2015) (holding that a claim should be subordinated if: (i) the claim is for "damages"; (ii) the claim involves "securities"; and (iii) the claim "arise[s] from" a "purchase or sale," and explaining that "[f]or a claim to 'arise from' the purchase or sale of a security, there must be some nexus or causal relationship between the claim and the sale"), *with In re Lehman Brothers Holdings Inc.*, 855 F.3d 459, 472–78 (2d Cir. 2017) (examining whether: (i) the claimant owns a security; (ii) the claimant acquired the security by means of a purchase or sale; and (iii) the claimant's damages arose from the purchase or sale of the security or the rescission of such a purchase or sale).

Section 101(49) of the Bankruptcy Code defines the term "security" broadly to "include" notes, stock, treasury stock, bonds, debentures, and an extensive catalogue of other investments. In addition, the definition contains a broad residual clause providing that a security also includes "any other claim or interest commonly known as [a] 'security.'" 11 U.S.C. § 101(49). Although, the scope of the residual clause is broad, the statutory definition also expressly excludes a number of items, including, among other things, currency, checks, drafts, bills of exchange, bank letters of credit, commodity futures contracts, forward contracts, options, and warrants. Section 101(16) of the Bankruptcy Code defines an "equity security" to mean shares in a corporation or any "similar security," limited partnership interests, and certain warrants or rights.

In *Lehman Brothers*, the U.S. Court of Appeals for the Second Circuit noted that "some interests will not perfectly match any of the specific examples in [the Bankruptcy Code's definition of security]," and that, should this be the case, it is of "most significance" that a claimant "ha[s] the same risk and benefit expectations as shareholders." *Lehman Brothers*, 855 F.3d at 473–74; *accord In re Linn Energy*, 936 F.3d 334, 344 (5th Cir. 2019) (even though the beneficiary of a stock trust did "not fit perfectly in the investor box," his claims should be subordinated under section 510(b) because his entitlement to "deemed dividends" originally arising from the trust "was certainly more like an investor's interest than a creditor's interest"); *In re WorldCom, Inc.*, 2006 WL 3782712, at *6 (Bankr. S.D.N.Y. Dec. 21, 2006) ("The form in which the equity interest is held is ultimately irrelevant. So long as the claimant's interest enabled him to participate in the success of the enterprise and the distribution of profits, the claim will be subordinated pursuant to section 510(b).").

The Bankruptcy Code does not define "damages." However, many courts have reasoned that "the concept of damages under Section 510(b) has the connotation of some recovery other than the simple recovery of an unpaid debt due on an instrument." *American Housing*, 785 F.3d at 153–54 (internal quotation marks omitted) (citing cases and ruling that claims seeking compensation for fraud or breach of fiduciary duty are claims for damages under section 510(b) as well as claims "predicated on post-issuance conduct," including breach of contract claims).

ONH

ONH AFC CS Investors, LLC ("AFC") was formed in 2022 to invest in commercial real estate. AFC's owner (the "principal") managed multiple commercial real estate investment companies, which were organized under two limited liability companies.

Beginning in 2022, AFC raised approximately $44 million to purchase the Atlanta Financial Center, an office complex located in Atlanta, Georgia. To do so, AFC and its affiliate ONH 1601 (collectively, the "debtors") used, among other things, the proceeds of equity interests sold to investors through securities offerings listed on an online brokerage platform. Investors were told that the proceeds from the securities offerings would be used to purchase and renovate the office complex. They were also informed that the funds would be held in segregated accounts to be returned if the deal failed to close.

Even though the debtors obtained the necessary funding, the Atlanta Financial Center sale failed to close. On July 14, 2023, the debtors filed for chapter 11 protection in the District of Delaware. The bankruptcy court later confirmed a joint liquidating chapter 11 plan for the debtors. The plan created a liquidating trust with the authority to pursue estate claims. It also subordinated under section 510(b) the investors' claims against the debtors for repayment of their investments, which they alleged were procured on the basis of fraudulent misrepresentations made by the debtors and the principal.

In June 2024, the liquidating trustee filed a complaint seeking to avoid and recover under sections 544(b), 548, and 550 of the Bankruptcy Code $7 million in pre-bankruptcy transfers made by AFC — using funds raised from investors in the abandoned office complex sale transaction — to JOSMIC 2 LLC and JOSMIC HOLDINGS LLC (the "defendants"), in part to repay a $5 million personal loan made by the defendants to the principal in 2022. The complaint, which stated causes of action for both intentional and constructive fraudulent transfers, alleged that ONH AFC and its principal "'made untrue statements of fact and/or omitted statements of material[] facts to investors in connection with the AFC Offering' including with respect to [the principal's] 'intended use of the funds from the Offering.'"

The defendants moved to dismiss the complaint or, in the alternative, to stay the litigation pending the outcome of the liquidating trustee's efforts to recover the transferred funds from the principal. Among other things, the defendants argued that a fraudulent transfer claim cannot be sustained if the beneficiaries of the litigation recovery would be equity holders, rather than creditors.

A report filed by the liquidating trustee with the bankruptcy court indicated that the trustee had already repaid millions of dollars to the class of equity holders that included the investors, and that the claims of all creditors would likely be paid in full (purportedly from funds already recovered by the trustee from the principal).

According to the defendants, because the investors' remaining fraud claims against the debtors would be subordinated under section 510(b), and the bankruptcy estate had more than enough assets to pay creditors in full, holders of equity interests were the sole beneficiaries of the liquidating trustee's fraudulent transfer action.

THE BANKRUPTCY COURT'S RULING

The bankruptcy court granted in part and denied in part the defendants' motion to dismiss, and denied the motion for a stay.

U.S. Bankruptcy Judge Craig T. Goldblatt was persuaded by the "core reasoning" of *In re DSI Renal Holdings, LLC*, 2020 WL 550987 (Bankr. D. Del. Feb. 4, 2020) (Owens, B.J.), where the court held that, although a transfer may be avoidable under section 544 or 548, a trustee's recovery is governed by section 550, which permits recovery "for the benefit of the estate." Based on Third Circuit precedent, the court in *DSI Renal* reasoned that this statutory language should be understood to mean "for the benefit of creditors." *DSI Renal*, 202 WL 550987, at **6–8 (citing *In re Cybergenics Corp.*, 226 F.3d 237, 243–247 (3d Cir. 2000); *In re Messina*, 687 F.3d 74 (3d Cir. 2012); *In re Majestic Star Casino, LLC*, 716 F.3d 736 (3d Cir. 2013)).

Judge Goldblatt interpreted these decisions to mean that fraudulent transfer claims are exclusively "a creditor's remedy." *ONH*, 2025 WL 1353850, at *5. According to Judge Goldblatt, a shareholder could not assert a fraudulent transfer claim outside of bankruptcy under state law based upon the dissipation of a company's assets, and "it would make no sense to permit a bankruptcy trustee to assert a fraudulent conveyance claim for the benefit of that party." *Id.* The bankruptcy court found no reason to believe that Congress intended to expand the rights of equity holders by importing this remedy into the Bankruptcy Code. *Id.*

Even so, the bankruptcy court held that *DSI Renal* was distinguishable from the case before it due to the subordination of the investors' claims under section 510(b). Judge Goldblatt reasoned that equity holders may assert claims against a company as creditors outside of bankruptcy, and subordination under section 510(b) is a limitation imposed solely by operation of the Bankruptcy Code. Thus, he explained, strict application of *DSI Renal* would limit trustee recoveries on fraudulent transfer claims to only "the amount necessary to satisfy in full those claims that are 'allowed' in the bankruptcy case and are not subject to subordination under § 510(b)." *Id.* at *9. According to the bankruptcy court, section 510(b) makes clear that subordination is only "[f]or the purposes of distribution under this title" and not "for the very different purpose of reducing the liability of a fraudulent conveyance defendant. *Id.* at *10.

"Properly understood," Judge Goldblatt wrote, "[the *DSI Renal* rule] does not turn on the allowance, classification, or treatment of the claims in bankruptcy" but instead, "it is focused on whether the beneficiaries of the fraudulent conveyance action would have had the right to assert fraudulent conveyance claims outside of bankruptcy." *Id.* at *6. Following this logic, the court concluded that, "there is no reason why a bankruptcy trustee should not be able to bring a fraudulent conveyance claim for the benefit of [investors]" because the investors could have asserted state law fraudulent conveyance claims outside of bankruptcy. *Id.*

In further elaboration of the general rule articulated in *DSI Renal*, the bankruptcy court also examined the U.S. Supreme Court's ruling in *Moore v. Bay*, 284 U.S. 4 (1931). In that case, which was brought under the former Bankruptcy Act, the Court ruled that a bankruptcy trustee could bring an action to avoid a lien for the benefit of all creditors, even those that would not have been able to bring the action outside of bankruptcy. *Id.* at 5.

Consistent with *Moore*, the bankruptcy court in *ONH* explained that recovery from a successful avoidance action brought pursuant to section 544(b) can extend beyond just the creditors who could bring the action. *ONH* at *8. According to Judge Goldblatt, "[t]he recovery is not for the exclusive benefit of those triggering creditors. Rather, it is 'for the benefit of the estate.'" *Id.* However, he noted, *Moore* does not "require[] the conclusion that the trustee in bankruptcy may affirmatively recover amounts that could not have been recovered by any creditor outside of bankruptcy." *Id.* Thus, settling on a narrow interpretation similar to *DSI Renal*, the bankruptcy court held that "a bankruptcy trustee's recovery on a fraudulent conveyance claim cannot exceed the total value of the valid claims against the bankruptcy estate." *Id.* at *9.

Although the evidence established that creditors would be paid in full under the debtors' liquidating chapter 11 plan after subordination of the investors' claims, there was no evidence that the trustee's recoveries would be sufficient "to pay the amounts the debtor owed to the defrauded investors immediately before the bankruptcy." *Id.* The bankruptcy court concluded that prohibiting the liquidating trustee from avoiding and recovering fraudulent transfers on account of the defrauded investors would effectively undermine the principles of *DSI Renal*. *Id.* It therefore declined to stay the adversary proceeding and found that *DSI Renal* "should not be applied for the very different purpose of reducing the liability of a fraudulent conveyance defendant." *Id.*

The court denied the motion to dismiss the liquidating trustee's actual fraudulent transfer claims against the defendants with respect to the $5 million personal loan, but dismissed the intentional fraudulent transfer claims with respect to the remaining $2 million in payments because the complaint failed to allege intentional fraud in connection with those transfers. The court granted the defendants' motion to dismiss the trustee's constructive fraudulent transfer claims because the complaint did not allege that debtors were insolvent.

OUTLOOK

In allowing a liquidating trustee to continue pursuing fraudulent transfer actions solely for the benefit of creditors whose claims were subordinated by operation of section 510(b), the court in *ONH* adopted and clarified the rationale articulated in *DSI Renal*. While the circumstance presented to the bankruptcy court—a debtor's estate rendered solvent solely by virtue of the subordination of equity-related claims—is perhaps unusual, the bankruptcy court's opinion provides an interesting insight into the balancing of creditors' rights inside and outside of bankruptcy.

NEWSWORTHY

Jones Day was among the "Client Service 30" in BTI Consulting Group's annual survey of law firms providing superior client service. The Firm has been ranked among the BTI client service elite for 10 years running.

Corinne Ball (New York), ***Bruce Bennett (Los Angeles)***, ***Carl E. Black (Cleveland)***, ***Jeffrey B. Ellman (Atlanta)***, ***Gary L. Kaplan (Miami)***, ***Heather Lennox (Cleveland/New York)***, and ***Daniel J. Merrett (Atlanta)*** were recognized in the 2026 edition of Best Lawyers in America® in the practice area Bankruptcy and Creditor Debtor Rights/Insolvency and Reorganization Law; Litigation—Bankruptcy.

Brad B. Erens (Chicago), ***Gregory M. Gordon (Dallas)***, ***Dan T. Moss (Washington/New York)***, ***Kevyn D. Orr (Washington)***, ***T. Daniel Reynolds (Cleveland)***, and ***Thomas W. Wearsch (New York/Cleveland)*** were recognized in the 2026 edition of Best Lawyers in America® in the practice area Bankruptcy and Creditor Debtor Rights/Insolvency and Reorganization Law. ***Caitlin K. Cahow (Atlanta/Chicago)*** was recognized as "One to Watch" in the practice area Bankruptcy and Creditor Debtor Rights/Insolvency and Reorganization Law; Litigation—Bankruptcy. ***Ryan Sims (Washington)*** was recognized as "One to Watch" in the practice area Bankruptcy and Creditor Debtor Rights/Insolvency and Reorganization Law.

Fabienne Beuzit (Paris), ***Rodolphe Carrière (Paris)***, and ***Isabelle Maury (Paris)*** were recognized in the 2026 edition of The Best Lawyers in France™ in the practice area Insolvency and Reorganization Law.

Corinne Ball (New York) (Hall of Fame), ***Bruce Bennett (Los Angeles)***, ***Carl E. Black (Cleveland)***, ***Jeffrey B. Ellman (Atlanta)***, ***Brad B. Erens (Chicago)***, ***Gregory M. Gordon (Dallas)***, ***Heather Lennox (Cleveland/New York)***, ***Joshua M. Mester (Los Angeles)***, and ***Kevyn D. Orr (Washington)*** were included in the 2025 edition of Lawdragon 500 Leading Bankruptcy and Restructuring Lawyers.

An article written by ***Jeffrey B. Ellman (Atlanta)*** and ***Alexandra L. Wainwright (Cleveland)*** titled "New York Bankruptcy Court Adopts Realistic Possibility Standard for Free and Clear Sales Under 11 U.S.C § 363(f)(5)" was published on July 23, 2025, by Lexis Practical Guidance.

An article written by ***Genna Ghaul (New York)*** and ***Benjamin C. Sandberg (New York)*** titled "Avianca: Second Court Adopts Billing Date Approach to Timely Performance of Unexpired Commercial Personal Property Leases in Bankruptcy" was published on July 24, 2025, by Lexis Practical Guidance.

An article written by ***Dan B. Prieto (Dallas)*** titled "Fifth Circuit Reigns in Bankruptcy Court Gatekeeping in Chapter 11 Plans" was published on July 24, 2025, by Lexis Practical Guidance.

An article written by ***Daniel J. Merrett (Atlanta)*** titled "Purdue Prohibition of Nonconsensual Third-Party Chapter 11 Plan Releases Does Not Apply to Bankruptcy Asset Sales" was published on July 25, 2025, by Lexis Practical Guidance.

Heather Lennox (Cleveland/New York), ***Bruce Bennett (Los Angeles)***, ***Kevyn D. Orr (Washington)***, ***Gregory M. Gordon (Dallas)***, ***Carl E. Black (Cleveland)***, ***Daniel J. Merrett (Atlanta)***, ***Dan B. Prieto (Dallas)***, ***Corinne Ball (New York)***, ***Thomas M. Wearsch (New York/Cleveland)***, ***Brad B. Erens (Chicago)***, ***Jeffrey B. Ellman (Atlanta)***, ***Gary L. Kaplan (Miami)***, and ***Dan T. Moss (Washington/New York)*** were recognized as leading lawyers in the practice area Bankruptcy/Restructuring in the 2025 edition of Chambers USA. ***Heather Lennox*** and ***Gregory M. Gordon*** received a "Band 1" designation. ***Heather Lennox*** was also recognized as a "Star Individual," and ***Corinne Ball*** and ***Bruce Bennett*** were designated as "Senior Statespersons."

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