In re Fairfield Sentry Ltd.: Extraterritorial Application the US Bankruptcy Code's Securities Safe Harbor from Constructive Fraudulent Transfer Claims

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Introduction

United States courts have long grappled with application of various US Bankruptcy Code provisions to non-US parties through the lens of a chapter 15 proceeding. In August 2025, the US Court of Appeals for the Second Circuit (the "**Second Circuit**") resolved a split of lower court decisions, ruling that the Bankruptcy Code's securities safe harbor under section 546(e) shields transfers between non-US entities from constructive fraudulent transfer and related claims pursued through chapter 15 proceedings.[1]

Background

The debtors in *In re Fairfield Sentry Ltd.* (collectively, the "**Debtors**" and each, a "**Debtor**") were investment funds based in the British Virgin Islands ("**BVI**") that invested heavily in Bernard L. Madoff Investment Securities ("**BLMIS**"). As Madoff's Ponzi scheme unraveled, the Debtors were forced into liquidation and initiated insolvency proceedings in the BVI in 2009. In July 2010, the Bankruptcy Court for the Southern District of New York (the "**Bankruptcy Court**") granted US chapter 15 recognition of the BVI proceedings as a foreign main proceeding.

Before the collapse of Madoff's Ponzi scheme, some investors redeemed their shares in the Debtor funds at overstated redemption prices reflecting inflated fund valuations based on BLMIS's fictitious account statements. The liquidators appointed for the Debtors brought suits in the BVI seeking to claw back these redemption payments from certain of the non-US investors that redeemed shares before the collapse (the "**Defendants**") so those Defendants would not benefit from a windfall at the expense of investors whose shares suffered substantial losses following disclosure of BLMIS's fraud.[2] Those proceedings ultimately came before the Privy Council in London, which upheld the finality of the Defendants' redemption.

The liquidators then moved for leave to amend the complaint in the US chapter 15 proceeding. The Defendants moved to dismiss the liquidators' claims for lack of personal jurisdiction, failure to state a claim, and the safe harbor for securities transactions of section 546(e) of the Bankruptcy Code. The three central issues first considered by the Bankruptcy Court were: (i) whether the forum selection clause in the Debtor fund subscription agreements established personal jurisdiction over the investors who were non-US Defendants, (ii) whether the securities safe harbor of section 546(e) of the Bankruptcy Code applies extraterritorially to bar the liquidators' fraudulent transfer claims and (iii) whether section 546(e)'s safe harbor applies to common-law claims based on non-US legal theories. The Second Circuit addressed each of these questions on appeal.

[1] *In re Fairfield Sentry Ltd.*, No. 22-2101-BK, 2025 WL 2218836 (2d Cir. Aug. 5, 2025).

[2] The liquidators also filed about 300 separate actions in the United States to claw back over $6 billion in allegedly inflated redemption payments, asserting a number of claims directly under US law, including unjust enrichment, constructive trust, among others. The US chapter 15 proceeding consolidated and stayed all these US actions pending the outcome of the BVI proceedings.

Personal Jurisdiction Through Fund Document Forum Selection Clause

The forum selection clause in the Defendant investors' fund subscription agreements provided that a "[s]ubscriber agrees that any suit, action or proceeding ... with respect to this Agreement and the [Debtor fund] may be brought in New York." The Second Circuit adopted a broad interpretation of this clause, holding that an action was "with respect to" the subscription agreement as long as there was even an "established or discoverable relation," under which the liquidators' actions qualified. Thus, the Defendants' contractual consents through the fund documents' forum selection clause established personal jurisdiction for the liquidators' claims against the Defendants.

Extraterritorial Application of the Bankruptcy Code's Securities Safe Harbor

The Second Circuit also addressed a split among earlier decisions about whether the US Bankruptcy Code's securities safe harbor shields transfers between non-US parties. Section 546(e) of the Bankruptcy Code provides a safe harbor from the trustee's avoidance power for settlement payments "made by or to (or for the benefit of) a ... financial institution ... in connection with a securities contract" with respect to certain types of avoidance actions, including constructive fraudulent transfer claims.[3] This safe harbor is extended to chapter 15 proceedings via section 561(d) of the Bankruptcy Code, which provides that:

Any provisions of this title relating to securities contracts ... 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 this title, 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).[4]

The parties did not dispute that the relevant transactions were settlement payments made to financial institutions in connection with a securities contract. The sole dispute was whether section 546(e) applies extraterritorially to shield transfers from and to non-US parties.

The Second Circuit started the analysis with the established presumption against extraterritorial application of US statutes and applied the standard set forth in *RJR Nabisco v. Eur. Cmty.*, 579 U.S. 325 (2016), considering (i) whether Congress intended the statute to apply extraterritorially and (ii) if the presumption against extraterritoriality has not been rebutted, whether the conduct occurred domestically.

Under the Court's analysis of the first element, Congress expressed a clear intent to apply section 546(e) extraterritorially through enactment of section 561(d) because section 561(d) would be superfluous if the safe harbors only applied domestically. Under chapter 15, the only avoidance powers possessed by a foreign representative are those under foreign law because, through section 1521(a)(7) of the Bankruptcy Code, "[c]hapter 15 expressly prohibits a foreign representative from using the statutory avoidance powers of the Bankruptcy Code" or from using state law pursuant to section 544(b). Therefore, the Court found that section 561(d) "must apply extraterritorially if it is to have any effect at all." Additionally, the Court inferred congressional intent to apply section 546(e) extraterritorially through the overall purpose of chapter 15 ("to provide filing by foreign, not domestic, debtors") and the legislative history of section 561(d). Congress added section 561(d) in response to the collapse of Long Term Capital Management L.P. ("**LTCM**")—which operated a Cayman Islands fund—to impose the US Bankruptcy Code's

[3] 11 U.S.C. § 546(e).

[4] 11 U.S.C. § 561(d).

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securities safe harbors upon transfers initiated by a foreign debtor to domestic recipients with the goal of preventing financial contagion stemming from foreign debtors' bankruptcies.[5] The Court reasoned that Congress, when legislating section 561(d) in the wake of LTCM's collapse, could not have "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."[6]

Because it found that Congress clearly intended extraterritorial application, the Second Circuit did not need to consider the second *Nabisco* element.

The Scope of Section 546(e)'s Powers

After determining that the securities safe harbor applies extraterritorially, the Second Circuit proceeded to hold that section 546(e) bars all of the liquidators' claims, including the constructive trust claims based on BVI common law. First, the Court held that the liquidators' claims did not meet section 546(e)'s carve-out for intentional fraudulent transfer claims under section 548(a)(1)(A) (transfers made "with actual intent to hinder, delay, or defraud" a creditor) because (i) the liquidators failed to establish the requisite intent on the part of Citco Fund Services (Europe) B.V. ("**Citco**"), the fund administration service provider that calculated and certified the funds' net asset values to the fund administrators based on fictitious account statements provided by BLMIS and (ii) even if Citco had fraudulent intent, the liquidators failed to plausibly allege that such intent was attributable to the Debtors who authorized the transfers.[7]

The Court next held that, based on a natural reading of the text of section 546(e), section 546(e)'s safe harbor covers state common-law and foreign common-law claims that seek to avoid covered transactions through alternative means. As the Court noted, "the focus of § 546(e) is the transaction, not the specific legal authority that a domestic trustee would use to avoid that transaction." The Court also rejected the argument that the liquidators' constructive trust claims bypassed section 546(e) altogether because they were based on a different legal theory than a traditional avoidance claim. Ultimately, all of the liquidators' claims against the Defendants fell under section 546(e)'s safe harbor and were dismissed.

Conclusion

In recent years, multiple US court decisions have addressed the extraterritorial application of trustees' recovery powers, including the extent to which they reach property that was subject of an overseas transaction.[8] In *Fairfield*, the Second Circuit extended extraterritorial application of the US securities safe harbor, shielding these transactions between non-US parties from some of the most potent types of US fraudulent transfer liability.

The *Fairfield* decision also broadens section 546(e) to cover common-law claims based on non-US legal theories. This reflects the continued expansion of the reach of section 546(e) within the Second Circuit, whose rulings are binding authority on the Bankruptcy Court for the Southern District of New York where many non-US debtors file chapter 15 petitions for recognition of non-US proceedings. ■

[5] *See* President's Working Group, *Hedge Funds, Leverage, and the Lessons of Long-Term Capital Management* (Apr. 1999).

[6] Brief of the Securities Industry and Financial Markets Association as Amicus Curiae Supporting Appellees, *Fairfield Sentry Ltd. (In Liquidation) by & through Krys v. Citibank, N.A. London*, 630 F. Supp. 3d 463 (S.D.N.Y. 2022), 14.

[7] 11 U.S.C. § 548(a)(1)(A).

[8] *See e.g. Inv'r Prot Corp v. Bernard L Madoff Inv Sec LLC*, 480 BR 501 (Bankr. S.D.N.Y. 2012); *Sec Inv'r Prot Corp v. Bernard L Madoff Inv Sec LLC*, 513 BR 222 (S.D.N.Y. 2014); *In re Picard*, 917 F3d 85 (2d Cir. 2019).