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Fraudulent Transfers and the Subsequent Transferee Defense Under the Bankruptcy Code and UFTA /UVTA

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Introduction to Avoidance and Recovery Liability and Defenses

The Bankruptcy Code separates the concepts of avoidance and recovery. Bankruptcy Code sections 544, 547, 548 and 549 authorize bankruptcy trustees and DIPs to avoid certain pre- and post-petition transfers to creditors and others.

Introduction to Avoidance and Recovery Liability and Defenses *(cont.)*

- Bankruptcy Code section 550 governs the recovery of avoided transfers or their value.
- Section 550(a) provides that the debtor "may recover, for the benefit of the estate, the property transferred, or, if the court so orders, the value of such property, from—(1) the initial transferee of such transfer or the entity for whose benefit such transfer was made; or (2) any immediate or mediate transferee of such initial transferee."

Introduction to Avoidance and Recovery Liability and Defenses *(cont.)*

Section 550 distinguishes between initial transferees and subsequent transferees.

- Initial transferees receive the transfer directly from the debtor or the transfer is made for the initial transferee's benefit. "For the benefit," can be very technical, with important pleading consequence which we will discuss later in presentation.
- A subsequent transferee can be the recipient of the transfer from the initial transferee or a preceding subsequent transferee.

Introduction to Avoidance and Recovery Liability and Defenses *(cont.)*

Once the a transfer is avoided, it can be traced down the line to any subsequent transferee and recovered so long as properly traced, even if commingled with other funds.

Introduction to Avoidance and Recovery Liability and Defenses *(cont.)*

- Courts have adopted various tests to aid debtors in tracing transfers in commingled bank accounts, which include without limitation:
  - the "first in, first out" test
  - the "last in, first out" test
  - the "lowest intermediate balance" rule
- Other tests may apply in other contexts.
- Certain tracing rules have been restated in the Restatement of Restitution and Unjust Enrichment

Introduction to Avoidance and Recovery Liability and Defenses *(cont.)*

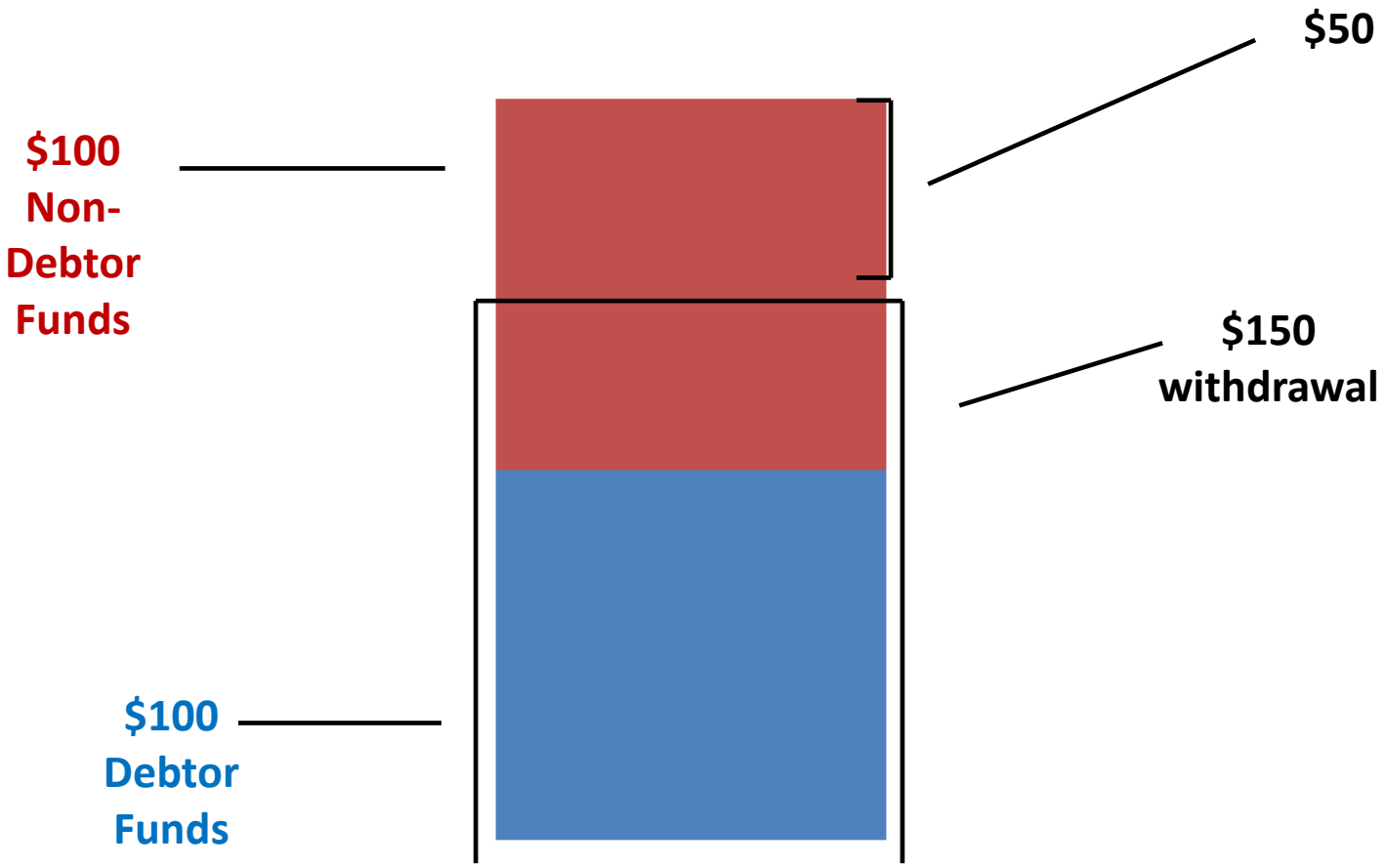
The following hypothetical will be used to illustrate the application of "first in, first out" and "last in, first out" tests:

1. Seller gets a $100 payment from Company for a shipment of widgets.
2. Seller puts the $100 into a concentration account and then puts in $100 of payments from other customers.
3. Seller then withdraws $150 from the concentration account to pay a dividend to Equity Holder.
4. Company files for Chapter 11 bankruptcy shortly afterwards and the debtor-in-possession seeks to avoid and recover the $100 payment from (x) Seller as the initial transferee and (y) from Equity Holder as the subsequent transferee.

Introduction to Avoidance and Recovery Liability and Defenses *(cont.)*

- The "first in, first out" test provides that the first funds withdrawn from a commingled account correspond to the first funds put in, and all subsequent withdrawals correspond to the funds put in thereafter in the order that they were put it.
- In the hypothetical, $100 of the funds paid by Seller to Equity Holder would be traceable to the debtor because (1) the $100 payment from the debtor was the first funds put into the account, and (2) the $150 withdrawal is deemed to be made from the first funds in the account.

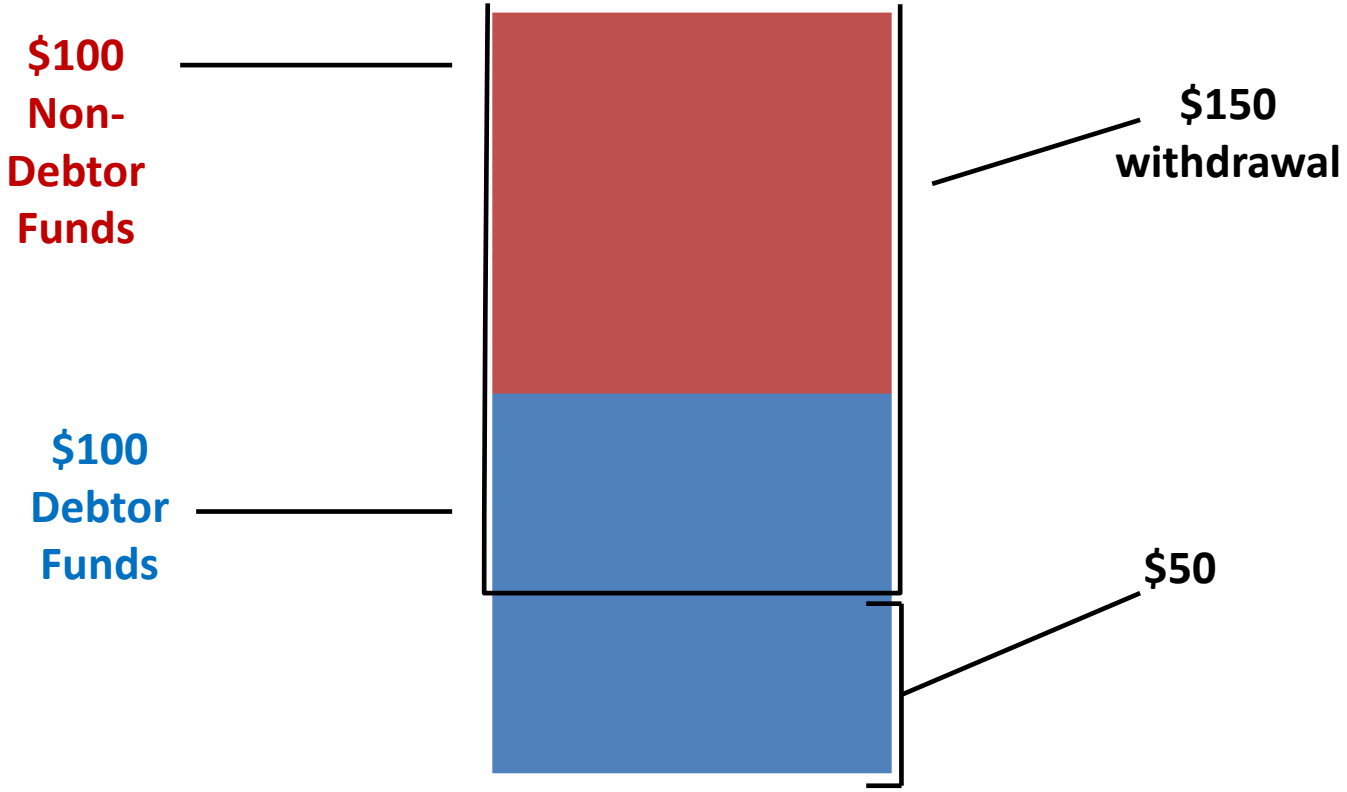
F I F O



Introduction to Avoidance and Recovery Liability and Defenses *(cont.)*

- The "last in, first out" test used in the context of making distributions from a commingled account to depositors who are owed the return of their funds. It would require that the entities that most recently put in money receive distributions of their funds first, followed by other creditors in the inverse order of when they paid into the account.
- In the hypothetical, only $50 of the funds paid by Seller to Equity Holder would be traceable to the debtor because (1) the $100 payment from the debtor was the first funds put into the account, and (2) the $150 withdrawal is deemed to be made from the last funds in the account.

L I F O



Introduction to Avoidance and Recovery Liability and Defenses *(cont.)*

The "lowest intermediate balance" rule (LIBR) applies most often in the context where trust funds have been put into commingled accounts.

- It treats withdrawals from the account as made first against the funds not held in trust.
- For example, if the account balance is greater than or equal to the amount of trust funds, the entire amount of the trust funds are considered traceable to the account.
- Once the trust funds are withdrawn, those funds are no longer considered traceable to the particular account even if the account's balance is later replenished with other unrelated funds.
- Therefore, the party seeking the return of the funds may only recover from the accountholder up to the amount of the lowest balance the account ever held between the time the funds were put in and the action to recover them.

Introduction to Avoidance and Recovery Liability and Defenses *(cont.)*

The following hypothetical illustrates how the LIBR is applied: Law Firm gets $100 in trust from Client to be paid as settlement funds once a dispute in which Law Firm represents Client is resolved. Law Firm puts the $100 payment into an IOLTA and then improperly puts in $100 from another client for payment of services. Law Firm then improperly withdraws $100 from the IOLTA to pay an equity distribution to Partner. Client files for Chapter 11 bankruptcy shortly afterwards and the debtor-in-possession seeks to avoid and recover the trust funds from Law Firm as the initial transferee and from Partner as the subsequent transferee.

- The LIBR will assume Law Firm withdrew the non-trust funds, so that the debtor can trace the $100 of trust funds to the remaining balance in the account.
- Now say Law Firm withdraws $125 to pay Partner. The LIBR will consider only the $75 remaining on deposit in the account to consist of traceable funds. Because $25 of the trust funds have left the account, the LIBR no longer considers these funds traceable.

Introduction to Avoidance and Recovery Liability and Defenses *(cont.)*

Section 550(b) provides defenses to recovery liability for subsequent transferees. Section 550(b)(1) provides a defense to a transferee who "takes for value, including satisfaction or securing of a present or antecedent debt, in good faith, and without knowledge of the voidability of the transfer avoided . . . ." Section 550(b)(2) extends this defense to "any immediate or mediate good faith transferee of such transferee."

- Section 550(b)(1) requires a subsequent transferee to show (1) good faith and (2) value
- Section 550(b)(2) extends this defense to transferees further down the chain.

Introduction to Avoidance and Recovery Liability and Defenses *(cont.)*

These defenses are designed to be consonant with the non-bankruptcy policy of protecting *bona fide* purchasers (BFP) for value or holders in due course from having to disgorge funds or their value based on the knowledge of the initial transferee.

Introduction to Avoidance and Recovery Liability and Defenses *(cont.)*

- As will be discussed in detail, the Uniform Fraudulent Transfer Act section 8(b)(2) is the older model act equivalent of Section 550(b). It protects transferees to the extent the transferees gave "value" in "good faith."
- However, many states have recently enacted the newer Uniform Voidable Transactions Act (2014), which also protects transferees that provide value for the transfer. (*See, e.g.*, N.Y. Debt. & Cred. Law § 274(a) (effective April 4, 2020) ("A transfer made or obligation incurred by a debtor is voidable as to a creditor whose claim arose before the transfer was made or the obligation was incurred if the debtor made the transfer or incurred the obligation *without receiving a reasonably equivalent value* in exchange for the transfer or obligation and the debtor was insolvent at that time or the debtor became insolvent as a result of the transfer or obligation.")))
  - *Note that unlike many other states' versions of the UVTA, the NY UVTA does not explicitly require "good faith"

Introduction to Avoidance and Recovery Liability and Defenses *(cont.)*

Uniform Fraudulent Transactions Act

The Uniform Fraudulent Transfers Act is the older model act adopted by many states to authorize avoidance and recovery of fraudulent transfers. UFTA section 8 sets forth the defenses to avoidance and recovery:

a) *A transfer or obligation is not voidable under Section 4(a)(1) against a person who took in good faith and for a reasonably equivalent value or against any subsequent transferee or obligee.*

b) *Except as otherwise provided in this section, to the extent a transfer is voidable in an action by a creditor under Section 7(a)(1), the creditor may recover judgment for the value of the asset transferred, as adjusted under subsection (c), or the amount necessary to satisfy the creditor's claim, whichever is less. The judgment may be entered against:*

   1) *the first transferee of the asset or the person for whose benefit the transfer was made; or*

   2) *any subsequent transferee other than a good faith transferee who took for value or from any subsequent transferee.*

Introduction to Avoidance and Recovery Liability and Defenses *(cont.)*

Uniform Fraudulent Transactions Act *(cont.)*

- Under the UFTA section 8(a), a transfer made with the intent to hinder, delay, or defraud a creditor is not voidable if a transferee takes the transfer in good faith and for reasonably equivalent value.
- As originally written, the transferee did not need to show that it gave value *to the debtor* for the transfer.

Introduction to Avoidance and Recovery Liability and Defenses *(cont.)*

Uniform Fraudulent Transactions Act *(cont.)*

- There is no equivalent defense to avoidance in the Bankruptcy Code, which requires a showing of good-faith and value *to the debtor*.
  - Section 548(c): Except to the extent that a transfer . . . voidable under this section is voidable under section 544, 545, or 547 of this title, a transferee . . . of such a transfer . . . that takes for value and in good faith has a lien on or may retain any interest transferred . . . to the extent that such transferee . . . gave value *to the debtor* in exchange for such transfer . . . . (Emphasis added.)
- Under the UFTA, any subsequent transferee who took the transfer in good faith and for value also has a defense. (UFTA § 8(b)(2).)

Introduction to Avoidance and Recovery Liability and Defenses *(cont.)*

Uniform Voidable Transactions Act

In 2014, the Uniform Law Commission promulgated revisions to the UFTA and changed the name of the model act to the Uniform Voidable Transactions Act (UVTA). The UVTA made two significant amendments to the defenses to avoidance and recovery:

- Limited the value defense to avoidance to value given to the debtor
- Expanded the value defense to recovery so that it applies to recovery of or from the transferred property or its proceeds

Introduction to Avoidance and Recovery Liability and Defenses *(cont.)*

Uniform Voidable Transactions Act *(cont.)*

Amendment 1: Limited value defense to avoidance to value given to the debtor

UVTA section 8 (as redlined against the UFTA) provides:

(a) A transfer or obligation is not voidable under Section 4(a)(1) against a person ~~who~~ that took in good faith and for a reasonably equivalent value given to the debtor or against any subsequent transferee or obligee.

(b) To the extent a transfer is avoidable in an action by a creditor under Section 7(a)(1), the following rules apply:

(1) Except as otherwise provided in this section, ~~to the extent a transfer is voidable in an action by a creditor under Section 7(a)(1)~~, the creditor may recover judgment for the value of the asset transferred, as adjusted under subsection (c), or the amount necessary to satisfy the creditor's claim, whichever is less. The judgment may be entered against:

(i) the first transferee of the asset or the person for whose benefit the transfer was made; or

~~(2)~~ (ii) ~~any subsequent transferee~~ an immediate or mediate transferee of the first transferee, other than a good faith transferee who took for value or from any subsequent transferee.

(A) a good faith transferee ~~who~~ that took for value, or ~~from~~

(B) ~~any subsequent transferee~~ any immediate or mediate good-faith transferee of a person described in clause (A).

Introduction to Avoidance and Recovery Liability and Defenses *(cont.)*

Uniform Voidable Transactions Act *(cont.)*

Amendment 1: Limited value defense to avoidance to value given to the debtor (cont.)

- This amendment limits the value defense to avoidance to value given *to the debtor.*
- Applies to any defendant against who the debtor is seeking to avoid the transfer, which is typically the initial transferee but may be a subsequent transferee

Introduction to Avoidance and Recovery Liability and Defenses *(cont.)*

Uniform Voidable Transactions Act *(cont.)*

***Amendment 1: Limited value defense to avoidance to value given to the debtor* (cont.)**

- This amendment further aligns the defense to avoidance in state fraudulent transfer law with the defense in the Bankruptcy Code.
- This amendment does not alter the defense to recovery under UFTA, under which defendants need only show good faith and value to the transferor (such as the initial transferee). (See UFTA § 8(b)(1)(ii).)

Introduction to Avoidance and Recovery Liability and Defenses *(cont.)*

Uniform Voidable Transactions Act *(cont.)*

Amendment 2: Expanded value defense to recovery of or from the transferred property or its proceeds

- Under the UFTA, the defense for a subsequent transferee that took in good faith and for value (and for a subsequent transferee of that transferee) literally applied only to an action for money judgment
- The UVTA provides that that defense also applies to recovery of or from the transferred property or its proceeds, by levy or otherwise.
- This amendment is consistent with section 550 of the Bankruptcy Code

Introduction to Avoidance and Recovery Liability and Defenses *(cont.)*

– **“Good Faith” Defense**

- ***In re Bernard L. Madoff Inv. Sec. LLC (Picard v. Citibank N.A.)*, Docket Nos. 20-1333, 20-1334, 2021 WL 3854761 (2d Cir. Aug. 30, 2021)**
  – Recent decision in which the Second Circuit held that under the Bankruptcy Code, **inquiry notice**, rather than willful blindness, is the appropriate standard for determining good faith as a defense to liability for fraudulent transfer.
    » The Second Circuit indicated that because the Bankruptcy Code does not define “good faith,” the term should be afforded its ordinary meaning—that is, the “commonly understood meaning of the statute's words at the time Congress enacted the statute, and with a view to their place in the overall statutory scheme.”
      - Dictionary definitions, the term “good faith” as historically used in fraudulent conveyance case law, The Bankruptcy Act of 1938 (predecessor of the Bankruptcy Code of 1978), as well as the approaches of the Fourth, Fifth, Seventh, Eighth, Ninth, and Tenth Circuit (all of which require inquiry notice) were considered.

Introduction to Avoidance and Recovery Liability and Defenses *(cont.)*

- ***In re Bernard L. Madoff Inv. Sec. LLC*, No. 20-1333, 2021 WL 3854761 (2d Cir. Aug. 30, 2021) (cont.)**

– The Second Circuit further explained that the good faith defense under Sections 548(c) and 550(b)(1) should be approached in a three-step inquiry:
  - **First**, a court must examine what facts the defendant knew; this is a subjective inquiry and not a theory of constructive notice.
  - **Second**, a court determines whether these facts put the transferee on inquiry notice of the fraudulent purpose behind a transaction—that is, whether the facts the transferee knew would have led a reasonable person in the transferee's position to conduct further inquiry into a debtor-transferor's possible fraud.
  - **Third,** once the court has determined that a transferee had been put on inquiry notice, the court must inquire whether diligent inquiry by the transferee would have discovered the fraudulent purpose of the transfer.

– The court clarified that "[a]n objective 'reasonable person' standard applies in the second and third steps, namely, in assessing whether (1) the suspicious facts were such that they would have put a reasonable person in the transferee's position on inquiry notice; and (2) the transferee conducted a reasonably diligent investigation after being put on inquiry notice."

Discussion of key subsequent transferee defenses issues - Value

- "Value" is an affirmative defense; a transferee relying on the defense has the burden of proof.

- "Value" for subsequent transferees is measured against the initial transferee and not the debtor like in the initial transferee context.

- Looks to what the transferee gave up rather than what the transferor or any prior transferor, including the debtor, received. *Bonded Fin. Servs., Inc. v. European Am. Bank*, 838 F.2d 890 (7th Cir. 1988); *see Genova v. Gottlieb (In re Orange County Sanitation, Inc.)*, 221 B.R. 323 (Bankr. S.D.N.Y. 1997).

Discussion of key subsequent transferee defenses issues – Value *(cont.)*

- The transferee next in the chain after the initial transferee (the secondary transferee) must show that it gave value to invoke the section 550(b) defense.

- However, any subsequent transferee of a subsequent transferee that gave value need only receive the transfer in good faith. There is no requirement for a transferee at the third tier or beyond to give value, consistent with treating such a transferee as a BFP.

Discussion of key subsequent transferee defenses issues – Value *(cont.)*

- Value is not defined in the Bankruptcy Code and is a highly fact-based analysis.

- Transactions that satisfy, discharge or secure all or part of an otherwise legitimate obligation are for "value." For example, the repayment of a loan.

Discussion of key subsequent transferee defenses issues – Value *(cont.)*

Transactions that are gifts or other gratuitous transfers do not give value as a matter of law. As a general rule, these include:

- Outright gifts. *See e.g.*, *Youngblut v. Pepmeyer (In re Pepmeyer)*, 275 B.R. 539, 545 (Bankr. N.D. Iowa 2002) (debtor received no value in gifting ownership of an annuity to his daughter)
- Property passing under a will. *See Gray v. Snyder*, 704 F.2d 709 (4th Cir. 1983) (no value could be assigned to release of inheritance rights by the transferee-spouse)

Discussion of key subsequent transferee defenses issues – Value *(cont.)*

Transactions that do not give value *(cont.)*:

- Corporate dividends. *See, e.g., Pereira v. Equitable Life Ins. Society (In re Trace Int'l Holdings, Inc.)*, 289 B.R. 548, 560–61 (Bankr. S.D.N.Y. 2003) (dividends paid from an insolvent corporation to shareholders were made for no value and therefore, were fraudulent conveyances); *Adelphia Communications Corp. v. Rigas* (*In re Adelphia Communications Corp.*), 323 B.R. 345, 377 (Bankr. S.D.N.Y. 2005) (stating that "dividends from insolvent entities are classic fraudulent conveyances")
- Guaranties in which the debtor obliges itself to pay the debts of another. *See In re R.M.L., Inc.*, 195 B.R. 602, 618 (Bankr. M.D. Pa. 1996)

Discussion of key subsequent transferee defenses issues - Value *(cont.)*

Transactions that do not give value *(cont.)*:

- **Charitable contributions**, such as tithes and offerings to a church, to the extent avoidable. *See In re Lewis*, 401 B.R. 431, 436 (Bankr. C.D. Cal. 2009) (collecting cases)
  - However, amendments to the Bankruptcy Code made by the Religious Liberty and Charitable Donation Protection Act of 1998 prevent suits in bankruptcy for constructive fraudulent transfers for charitable contributions that do not exceed "15 percent of the gross annual income for the year in which the transfer of the contribution is made . . . ." 11 U.S.C. § 548(a)(2)(A).
  - For situations involving actual fraud, no law suits for amounts less than the same fifteen percent can be sustained "if the transfer was consistent with the practices of the debtor in making charitable contributions." 11 U.S.C. § 548(a)(2)(B).
  - Furthermore, § 544(b)(2) prevents the trustee from subrogating to the state law rights of a creditor against a charity tied to the same fifteen percent limit. 11 U.S.C. § 544(b)(2).

Discussion of key subsequent transferee defenses issues – Value *(cont.)*

Transactions that do not give value *(cont.)*:

- **College Tuition Paid by Parent for Adult Child (Courts Split).**

  Value

  See, e.g., In re Lewis, 574 B.R. 536 (Bankr. E.D. Pa. Apr. 7, 2017); *Shearer v. Oberdick (In re Oberdick)*, 490 B.R. 687 (Bankr. W.D. Pa. 2013); *In re Cohen*, Adv. No. 07-02517-JAD, 2012 WL 5360956 (Bankr. W.D. Pa. Oct. 31, 2012), rev'd in part on other grounds, 487 B.R. 615 (W.D. Pa. 2013)

  No Value

  *See, e.g., DeGiacomo v. Sacred Heart Univ., Inc. (In re Palladino)**, 942 F.3d 55 (1st Cir. 2019); *In re Leonard,* 454 B.R. 444 (Bankr. E.D. Mich. 2011); *Chorches v. Catholic Univ. of Am.*, No. 3:16-cv-1962 (MPS), 2018 WL 3421318 (D. Conn. July 13, 2018); *In re Sterman*, 594 B.R. 229 (Bankr. S.D.N.Y. 2018); *In re Knight*, No. 15-21646 (JJT), 2017 WL 4410455 (Bankr. D. Conn. Sept. 29, 2017); *Roach v. Skidmore Coll. (In re Dunston*), 566 B.R. 624, 636–37 (Bankr. S.D. Ga. 2017); *In re Sterman*, 594 B.R. 229 (Bankr. S.D.N.Y. 2018); *In re Leonard,* 454 B.R. 444 (Bankr. E.D. Mich. 2011).

  **In re Palladino* was the first appelate court to ever address this issue. Not surprisingly, the decision has prompted other bankruptcy trustees to seek clawback of tuition payments.

Discussion of key subsequent transferee defenses issues - Value *(cont.)*

Courts have crafted three tests to determine whether a subsequent transferee has provided value:

1) contract sufficiency,
2) reasonably equivalent value, and
3) fair market value

Discussion of key subsequent transferee defenses issues - Value *(cont.)*

Contract Sufficiency

- Majority rule Under section 550(b), a subsequent transferee must provide "merely consideration sufficient to support a simple contract . . ." to its transferor. *See, e.g.*, 5 COLLIER ON BANKRUPTCY ¶ 550.03[1] (16th ed. 2015); *Lewis v. Zermano (In re Stevinson)*, 194 B.R. 509, 513 (D. Colo. 1996); *In re Commercial Loan Corp.*, 396 B.R. 730, 744 (Bankr. N.D. Ill. 2008); *Sec. Inv. Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC*, No. 08-01789 (CGM), 2021 WL 3477479, at *9 (Bankr. S.D.N.Y. Aug. 6, 2021); *Sec. Inv. Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC*, No. AP 08-01789 (SMB), 2020 WL 1584491, at *8 (Bankr. S.D.N.Y. Mar. 31, 2020); *Sec. Inv. Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC*, No. AP 08-01789 (SMB), 2020 WL 401822, at *4 (Bankr. S.D.N.Y. Jan. 23, 2020); *Sec. Inv. Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC*, 608 B.R. 181, 195 (Bankr. S.D.N.Y. 2019); *Sec. Inv. Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC*, 594 B.R. 167, 206 (Bankr. S.D.N.Y. 2018); *Enron Corp v. Ave. Special Situations Fund II (In re Enron Corp.)*, 333 B.R. 205, 236 (Bankr. S.D.N.Y. 2005).

Discussion of key subsequent transferee defenses issues – Value *(cont.)*

***Contract Sufficiency* (cont.)**

- Does not require that value given by the transferee be reasonable or a fair equivalent.
- Analogous to the "value" required under state law to achieve the status of a *bona fide* purchaser for value. *See Redmond v. Brooke Holdings, Inc. (In re Brooke Holdings, Inc.)*, 515 B.R. 632 (Bankr. D. Kan. 2014) (only value needed for section 550(b), without regard to its equivalence to the transfer, is value akin to the protections for purchasers of goods under the Uniform Commercial Code).

Discussion of key subsequent transferee defenses issues – Value *(cont.)*

Reasonably Equivalent Value

- In the initial transferee context, the reasonably equivalent value test requires a court to "examine the totality of the circumstances surrounding the transfer in question." *Pereira v. WWRD US, LLC (In re Waterford Wedgwood USA, Inc.)*, 500 B.R. 371, 381 (Bankr. S.D.N.Y. 2013).
- The factors considered are "(i) the fair market value of the economic benefit received by the debtor [from the transferee]; (ii) the arms-length nature of the transaction; and (iii) the good faith of the transferee." *Pereira*, 500 B.R. at 381.

Discussion of key subsequent transferee defenses issues – Value *(cont.)*

***Reasonably Equivalent Value* (cont.)**

- A dollar-for-dollar exchange is not required. Courts instead examine the transaction to see if the transfer was for "roughly" the amount received.
- For subsequent transferees, it may be appropriate to view multiple transfers separately to determine whether value was provided for purposes of section 550(b). *See Rodgers v. Monaghan Co. (In re Laguna Beach Motors, Inc.)*, 159 B.R. 562, 569 (Bankr. C.D. Cal. 1993) (viewing two separate payments independently in determining section 550 defense).

Discussion of key subsequent transferee defenses issues - Value *(cont.)*

Reasonably Equivalent Value *(cont.)*

- ***Klein v. King & King & Jones*, No. 13-4131, 571 F.App'x 702 (10th Cir. July 14, 2014)**
  - A receiver for an investment trust that operated as a Ponzi scheme brought an action against a law firm under the Utah Uniform Fraudulent Transfers Act (UFTA) to recover funds that the trust paid for an individual's defense against a state-court criminal charge.
  - The law firm argued that it received the payments for value because it provided legal services to the individual criminal defendant. The district court rejected this argument and granted summary judgment to the receiver.

Discussion of key subsequent transferee defenses issues - Value *(cont.)*

Reasonably Equivalent Value *(cont.)*

- ***Klein v. King & King & Jones*, No. 13-4131, 571 F.App'x 702 (10th Cir. July 14, 2014) (cont.)**
  - The 10th Circuit Court of Appeal affirmed. It reasoned that the good-faith transferee defense in the Utah UFTA wasn't available to the law firm because:
    (1) the trust did not receive "reasonably equivalent value" for the funds transferred to the law firm; and
    (2) the law firm was an initial and not a subsequent transferee of funds and hence defenses available to subsequent transferees did not apply.

Discussion of key subsequent transferee defenses issues - Value *(cont.)*

Reasonably Equivalent Value *(cont.)*

- ***Klein v. King & King & Jones*, No. 13-4131, 571 F.App'x 702 (10th Cir. July 14, 2014) (cont.)**
  - Transferee defense in Utah UFTA: "A transfer . . . is not voidable . . . against a person who took in good faith and for a reasonably equivalent value or against any subsequent transferee . . . ." Utah Code Ann. § 25-6-9(1).
  - A subsequent transferee who is "a good faith transferee who took for value" also has a defense. Utah Code Ann. § 25-6-91(2)(b).

Discussion of key subsequent transferee defenses issues - Value *(cont.)*

Reasonably Equivalent Value *(cont.)*

- ***Klein v. King & King & Jones*, No. 13-4131, 571 F.App'x 702 (10th Cir. July 14, 2014) (cont.)**
  - Tenth Circuit's Rulings:
    - Reasonably equivalent value
      - Required to give value *to the debtor*
      - Law firm's legal services did not benefit anyone but the individual criminal defendant.
    - Initial transferee v. subsequent transferee
      - Firm received funds directly from trust and thereby was the initial transferee
      - Defenses available to subsequent transferees hence not available.

Discussion of key subsequent transferee defenses issues – Value *(cont.)*

Fair Market Value

- Used by courts either as a subset of the reasonably equivalent value test or as a stand-alone test of value.
- *Brown v. Harris (In re Auxano, Inc.)*, 96 B.R. 957, 965 (Bankr. W.D. Mo. 1989) adopted the fair market value measurement after considering what the subsequent transferee parted with and the purpose of the avoidance and recovery powers to preserve assets of the estate.

Discussion of key subsequent transferee defenses issues - other

FBO defendant versus subsequent transferee

Section 550(a): Except as otherwise provided in this section, to the extent that a transfer is avoided under section 544, 545, 547, 548, 549, 553 (b), or 724 (a) of this title, the [debtor] may recover, for the benefit of the estate, the property transferred, or, if the court so orders, the value of such property, from—(1) the initial transferee of such transfer *or the entity for whose benefit such transfer was made*; or (2) any immediate or mediate transferee of such initial transferee.

Discussion of key subsequent transferee defenses issues – other *(cont.)*

FBO defendant versus subsequent transferee *(cont.)*

- Section 550 provides for recovery from (1) an initial transferee, (2) an entity for whose benefit the transfer was made, who is considered a subset of a direct "initial transferee", or (3) a subsequent transferee.
- *See In re M. Blackburn Mitchell Inc.*, 164 B.R. 117, 130 (Bankr. N.D. Cal. 1994) ("Under § 550(a)(1), *both* entities are liable"- referring to "entity for whose benefit" and "transferee"); *In re The Heritage Org., LLC*, 413 B.R. 438, 499 (Bankr. N.D. Tex. 2009).
- Section 550 does not allow recovery of an avoided transfer *for the benefit of a subsequent transferee*.

Discussion of key subsequent transferee defenses issues - other *(cont.)*

FBO defendant versus subsequent transferee *(cont.)*

- *Hypothetical:* Debtor pays Uncle for purpose of paying Niece's college tuition. Uncle transfers funds to College for tuition for Niece. Debtor can recover from Uncle (entity to whom transfer was made), Niece (entity for whose benefit transfer was made), or College (subsequent transferee).
- *College Tuition Cases*: Pursuit of colleges as initial transferees based on payment of child's tuition may give college a defense that the child was the initial transferee because child obligated to college such that child "FOB" transferee. Raises value and statute of limitations issues.

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Recovery from either initial transferee or subsequent transferee

- The debtor is entitled to recover an avoided transfer either from initial transferee *or* the subsequent transferee. *Both* are liable for the transfer or its value.
- *See e.g.*, *In re Circuit Alliance, Inc.*, 228 B.R. 225, 236 (Bankr. D. Minn. 1998) (the Bankruptcy Code "*contemplates a joint suit against both initial transferee and converting beneficiary, as well as all subsequent transferees* not entitled to the defense of § 550(b)").

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Recovery from either initial transferee or subsequent transferee *(cont.)*

- However, the debtor is limited to a single satisfaction under section 550(d)
- Section 550(d): "[the debtor] is entitled to only a single satisfaction under subsection (a) of this section."
- *See In re Prudential of Florida Leasing, Inc.*, 478 F.3d 1291 (11th Cir. 2007) (under section 550(d), debtor was limited to a single recovery for each transfer).

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Recovery from either initial transferee or subsequent transferee *(cont.)*

- The Bankruptcy Code does not provide an express or implied right to an initial transferee to seek indemnity or contribution from a subsequent transferee or beneficiary of the transfer.
- *See In re Agra-By-Products, Inc.*, No. 82-05701, 1985 WL 660781, at *1 (Bankr. D.N.D. Aug. 1, 1985); *In re Schick*, 223 B.R. 661, 663 (Bankr. S.D.N.Y. 1998); *In re Dunhill Resources, Inc.*, 2006 WL 2090208, at *3 (Bankr. S.D. Tex. June 27, 2006) (dismissing alleged initial transferee's third-party complaints seeking indemnity or contribution for sums the debtor sought to collect as fraudulent transfers).

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Recovery from either initial transferee or subsequent transferee *(cont.)*

- However, courts have recognized that initial transferees may seek contribution or indemnity from subsequent transferees or visa-versa under other applicable law, such as agency law or by agreement. *See e.g., Agra-By-Products*, 1985 WL 660781, at *1.
- Such actions are not within the bankruptcy court's jurisdiction. *See In re Pearson Indus., Inc.*, 142 B.R. 831 (Bankr. C.D. Ill. 1992) (superseded by statute on other grounds) (dismissing for lack of jurisdiction initial transferee's third-party complaint seeking indemnity or contribution for transfer from subsequent transferee).

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Recovery from either initial transferee or subsequent transferee *(cont.)*

- Under section 502(h), a subsequent transferee from whom the debtor recovers a transfer under section 550 may pursue a claim against the bankruptcy estate as if such claim were a prepetition claim. *See Southmark Corp. v. Schulte, Roth & Zabel, LLP*, 242 B.R. 330, 341 (N.D. Tex. 1999).
- Claims traders: should be aware that they may be liable for the transfer with the initial transferee subject to any defenses, such as a value defense

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Subsequent transferee may raise initial transferee defenses

- Section 550 allows recovery of a transfer only "to the extent that a transfer is avoided."
- Some courts have interpreted this to require a successful avoidance action against the initial transferee before the debtor may recover from a subsequent transferee.

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Subsequent transferee may raise initial transferee defenses *(cont.)*

- However, the majority view is that a transfer may be found avoidable and a recovery may be had from a subsequent transferee without first suing the initial transferee.
- In an action against the subsequent transferee, the debtor has the burden of proving that the transfer to the initial transferee is avoidable.

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Subsequent transferee may raise initial transferee defenses *(cont.)*

- The subsequent transferee is not collaterally estopped from litigating the avoidability of the transfer merely because it is a subsequent transferee. *See, e.g., In Re Glob. Prot. USA, Inc.*, 546 B.R. 586, 619 (Bankr. D.N.J. 2016) ("In an action against the subsequent transferee, the estate has the burden of proving that the transfer to the initial transferee is avoidable and the subsequent transferee is not collaterally estopped from litigating that question merely because it is a subsequent transferee." (quoting Collier on Bankruptcy, ¶ 550.02[1].)); *Off. Comm. of Unsecured Creditors of M. Fabrikant & Sons, Inc. v. JP Morgan Chase Bank, N.A. (In re M. Fabrikant & Sons, Inc.)*, 394 B.R. 721, 746 (Bankr. S.D.N.Y. 2008).
- Absent collateral estoppel or *res judicata*, a subsequent transferee may raise any and all defenses to avoidance and recovery available to the initial transferee, including that the transfer was not avoidable or that the transferee did not have knowledge of the voidability of the transfer under section 550(b)(1). *See Tibble v. Farmers Grain Express, Inc. (In re Michigan Biodiesel, LLC)*, 510 B.R. 792, 799 (Bankr. W.D. Mich. 2014)

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Subsequent transferee may raise initial transferee defenses ***(cont.)***

- For example, if initial transferee has settled with the debtor for less than the total amount sought to be recovered, the subsequent transferee defendant may assert defenses available to the initial transferee, even if the initial transferee did not raise those defenses. *See In re Flashcom, Inc.*, 361 B.R. 519, 525 (Bankr. C.D. Cal. 2007) (stipulated or default judgment in avoidance action does not preclude defendants in recovery action from disputing the avoidability of the transfer or raising appropriate defenses).
- However, because of the single satisfaction rule, the subsequent transferee is only liable for the remaining balance of the transfer sought to be recovered.

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Subsequent transferee may raise initial transferee defenses *(cont.)*

- Likewise, if an initial transferee has failed to raise a given defense, the subsequent transferee may raise that defense.
- This is a matter of due process because the subsequent transferee may not have been involved in the litigation to avoid the initial transfer. *See, e.g., Sec. Inv. Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC*, 480 B.R. 501, 522 (Bankr. S.D.N.Y. 2012) (explaining that subsequent transferee "will be afforded its due process rights to contest the avoidability of . . . initial transfers"); *Thompson v. Jonovich (In re Food & Fibre Protection, Ltd.)*, 168 B.R. 408, 416 (Bankr. D. Ariz. 1994) (finding that a default judgment did not preclude defendants from asserting their due process rights to dispute avoidability of the initial transfer and raise whatever defenses were available to the initial transferee).

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Statute of Limitations on Recovery

- Section 550 contains its own statute of limitations.
- Subsection (f) provides that an action to recover under section 550 must be brought no later than the earlier of:
  - one year after the transfer was avoided or
  - the date the case is closed or dismissed.

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Statute of Limitations on Recovery ***(cont.)***

- Debtors will usually, but not always, file a consolidated action to avoid the transfer and recover the property transferred or its value.
- But where the debtor does not know the identity of, or even if there was a subsequent transferee, the debtor can start with the initial transferee and then use the section 550(f) statute of limitations once that initial transfer is avoided.

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Statute of Limitations on Recovery *(cont.)*

- A settlement (subject to the single satisfaction rule) with the initial transferee triggers the section 550(f) statute of limitations. *See, e.g.*, *ASARCO LLC v. Shore Terminals LLC*, No. 11-01384, 2012 WL 2050253, at *5 (N.D. Ca. June 6, 2012);
- Courts have reasoned that, if a settlement did not trigger section 550(f), the statute of limitations would be indefinite because a trigger event, i.e., the initial avoidance, may never occur. *See, e.g.*, *Sec. Inv. Prot. Corp. v. Bernard L. Madoff Inv. Sec. LLC*, 480 B.R. 501, 522 (Bankr. S.D.N.Y. 2012) (explaining that "[a]lthough the Settlement does not constitute a formal avoidance of the initial transfer . . . , it presents the Court with finality with respect to [the initial transferee]. This finality triggers the relevant one-year statute of limitations under section 550(f) of the Code. Without such a trigger, the Trustee would be permitted to bring suit against a subsequent transferee for an indefinite amount of time, a highly inequitable result.").

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Automatic stay of concurrent state-law fraudulent transfer claims: *In re Tribune Co. Fraudulent Conveyance Litigation*, 499 B.R. 310 (S.D.N.Y. 2013)

- The unsecured creditors' committee in the *Tribune* chapter 11 case brought adversary proceedings asserting actual fraudulent transfer claims against the debtor's cashed-out shareholders, directors / officers, and others who benefitted from a prepetition LBO of the debtor.
- Individual creditors then brought actions asserting state-law constructive fraudulent conveyance claims to unwind buyouts of the debtor's shareholders.
- The actions were consolidated into a multi-district litigation and defendants moved to dismiss individual creditor actions.

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Automatic stay of concurrent state-law fraudulent transfer claims *(cont.)*

- The district court granted the motion. It held that the individual creditors lacked standing to bring fraudulent transfer claims targeting the same transactions the committee was targeting.
- The automatic stay deprived the individual creditors from bringing state-law fraudulent conveyance claims, despite the fact that the unsecured creditors' committee was asserting an actual fraud theory and the individual creditors were asserting a constructive fraud theory.

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Automatic stay of concurrent state-law fraudulent transfer claims *(cont.)*

- However, the district court also found that limitations on some of the of the debtor's avoiding powers under section 546 of the Code did not preempt the state-law claims.
- The language of that section did not provide for preemption because it expressly imposed those limitations on a "trustee," which in a Chapter 11 case means a debtor-in-possession, and not other parties with standing and thus there was no preemption under the Supremacy Clause.
- The court recognized the risk that bankruptcy trustees will simply assign section 544(a) claims to creditors if barred by section 546(a), but reasoned that the concerns were overstated in light of the fact that the automatic stay bars state-law fraudulent conveyance claims brought concurrently with the debtor so that the bankruptcy court would still retain some control.

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Tribune Affirmed by Second Circuit:

- ***In re Tribune Co. Fraudulent Conveyance Litigation*, 946 F.3d 66 (2d Cir. 2016)**
  - Court explained that "the regulation of creditors' rights has 'a history of significant federal presence'" and that "once a party enters bankruptcy, the Bankruptcy Code constitutes a wholesale preemption of state laws regarding creditors' rights."
  - Court explained that the Creditors' core theory (i.e., Section 546(e)'s use of the word "trustee" meant that it did not apply to creditors' claims) raised "ambiguities, anomalies, or conflicts with the purposes of the Code."
  - Court explained that Section 546(e) was intended to protect settled securities transactions from disruption and that this protection is "essential to securities markets."
    - Decision stood for the proposition that the 546(e) safe harbor protects transfers that passed through a financial institution or other statutorily enumerated financial market participant (collectively, "Covered Entities") acting as a conduit, even if neither the transferor nor the transferee was itself a Covered Entity.

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Delaware Court Breaks with Second Circuit:

- ***AH Litig. Trust v. Water Street Healthcare Partners, L.P. (In re Physiotherapy Holdings, Inc.)*, No. 15-51238 (KG), 2016 WL 3611831 (Bankr. D. Del. June 20, 2016)**
  - In context of a going private LBO, Court examined whether the purpose of section 546(e) would be thwarted by allowing the Trust to pursue its state fraudulent transfer claims against the defendants.
  - Rejected preemption because the action targeted two controlling shareholders of a non-public corporation so it was difficult for the Court to envision any ripple effect on the market.
  - Second, the Trust brought the actions as a creditor-assignee, not as an estate representative – a scenario not addressed by Congress in section 546(e) despite its ability to do so.
  - Third and finally, the defendants were alleged to have acted in bath faith and thus, dismissal of the action would undermine other overarching policy objectives of the Bankruptcy Code targeted at ensuring a fair distribution of assets and protecting creditors from shareholder wrongdoing.

Discussion of key subsequent transferee defenses issues - other *(cont.)*

US Supreme Court Limits Scope of 546(e) Safe Harbor Protection

- ***Merit Mgmt. Grp., LP v. FTI Consulting, Inc.*, 138 S. Ct. 883, 200 L. Ed. 2d 183 (2018)**
  - Resolving a split between the Second, Third, Sixth, Eighth, and Tenth Circuit, on the one hand, and the Seventh and Eleventh Circuit on the other, the Supreme Court sided with the Seventh and Eleventh Circuit and held, in a unanimous ruling, that the presence of a "financial institution" in a multi-step transfer is insufficient to invoke a safe harbor under 546(e)—which prohibits the trustee from avoiding certain transfers made by, to or for the benefit of Covered Entities—if the financial institution is a mere conduit.

Discussion of key subsequent transferee defenses issues - other *(cont.)*

US Supreme Court Limits Scope of 546(e) Safe Harbor Protection

- ***Merit Mgmt. Grp., LP v. FTI Consulting, Inc.*, 138 S. Ct. 883, 200 L. Ed. 2d 183 (2018) (cont.)**
  - The Supreme Court explained that the relevant substantive focus of a safe harbor analysis is on the specific transfer that the trustee seeks to avoid.
    - The Court noted that a narrow reading the safe harbor provision is in line with the statute's text, context, and focus on the substantive nature of the transfer, as well as language in other sections of the Bankruptcy Code.
  - In reaching its decision, the Court declined to consider the statutory purpose for Section 546(e).
    - This reasoning is directly at odds with that of courts like the Second Circuit (e.g., *In re Tribune Co. Fraudulent Conveyance Litigation*, 946 F.3d 66 (2d Cir. 2016)), which have stressed that Congress intended to shield securities markets from the unwinding of securities transactions in enacting Section 546(e).

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Second Circuit Revisits 546(e) Safe Harbor Protection

- ***In re Tribune Company Fraudulent Conveyance Litigation*, 2019 WL 6971499 (2d Cir. Dec. 19, 2019)**
  - The Supreme Court invited the Second Circuit to reconsider its ruling in *Tribune* in view of *Merit* (as the *Tribune* creditors had filed a petition for certiorari which was pending when *Merit* was decided).
  - As a result of *Merit*, the Second Circuit recalled its mandate and considered whether Tribune (as transferor) and/or its shareholders (as transferees) constituted Covered Entities under the statute.
    - The court determined that Tribune did constitute a Covered Entity—specifically, a financial institution pursuant to the Bankruptcy Code definition of "financial institution," which includes the "customer" of a financial institution when the financial institution acts as the customer's "agent or custodian … in connection with a securities contract."
    - The Second Circuit ultimately held that Section 546(e) barred claims seeking to claw back payments that Tribune made to its shareholders.

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Second Circuit Revisits 546(e) Safe Harbor Protection

- ***In re Tribune Company Fraudulent Conveyance Litigation*, 2019 WL 6971499 (2d Cir. Dec. 19, 2019) (cont.)**
  - In addition, the Second Circuit reaffirmed that Section 546(e) preempts constructive fraudulent conveyance claims under state law because the claims are "in conflict with" "[e]very congressional purpose reflected in Section 546(e)."
  - The decision suggests that, at least in the Second Circuit, the 546(e) safe harbor may still protect transactions where a financial institution acts as "an agent or custodian" for the transferor or transferee.

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Extraterritoriality and Fraudulent Transfers

- Where a trustee seeks to recover property from subsequent transferees located outside of the US who received property from transferors also located outside of the US, the question arises as to whether the Bankruptcy Code's fraudulent transfer recovery provision (§ 550(a)) reaches that transaction.

- Courts are divided regarding whether § 550(a) applies extraterritorially. *See, e.g., In re CIL Ltd.*, 582 B.R. 46, 83-93 (Bankr. S.D.N.Y. 2018) (collecting cases).
  - Most courts apply two principal doctrines to assess extraterritoriality:
    - 1. The presumption against extraterritoriality; and
    - 2. International comity

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Extraterritoriality and Fraudulent Transfers (cont.)

- *Presumption Against Extraterritoriality*
  - provides that absent clearly expressed congressional intent to the contrary, U.S. laws will be construed to have only domestic application. *RJR Nabisco v. European Cmty.*, 136 S. Ct. 2090, 2100 (2016)

  - Acknowledging the foregoing, courts conduct a two-part analysis:
    - First, courts ask whether the statute "gives a clear, affirmative indication that it applies extraterritorially." *RJR Nabisco*, 136 S. Ct. at 2101.
      - If the answer is yes, the inquiry ends.
      - If the answer is no, then courts consider the statute's focus and the particular facts of the case to assess whether the conduct regulated by the statute occurred domestically.

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Extraterritoriality and Fraudulent Transfers (cont.)

- *International Comity*
  - The principle that one sovereign nation voluntarily adopts or enforces the laws of another sovereign nation out of deference, mutuality, and respect.

    - In the Second Circuit, "comity is especially important in the context of the Bankruptcy Code." *In re Maxwell Commc'n Corp. plc by Homan*, 93 F.3d 1036, 1048 (2d Cir. 1996).

Discussion of key subsequent transferee defenses issues - other *(cont.)*

Extraterritoriality and Fraudulent Transfers (cont.)

- Most courts agree that Bankruptcy Code §§ 548(a) and 550(a) do not give a clear, affirmative indication that the statute applies extraterritorially.
  - Therefore, courts generally look to the second part of the inquiry: the "focus" test
- Recent decisions out of the Southern District of New York and Second Circuit pertaining to the Liquidation of Bernard L. Madoff Investment Securities are particularly enlightening.

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Extraterritoriality and Fraudulent Transfers (cont.)

- ***Securities Investor Protection v. Bernard L. Madoff Investment Securities*, 513 B.R. 222 (S.D.N.Y. 2014)**
  - Madoff Securities made initial transfers from the US to feeder fund customers in the British Virgin Islands and the Cayman Islands.
  - Feeder fund customers subsequently transferred the money to investors in other countries outside of the US.
  - Madoff Securities was placed into liquidation in December 2008, and a trustee was appointed to liquidate the company. The trustee filed fraudulent transfer actions against the feeder funds under § 548(a) seeking to avoid the initial transfers, as well as actions against foreign investors under § 550(a) seeking to recover money transferred to the foreign investors by the feeder funds.
  - Applying the "focus" test, the US District court for the Southern District of New York found that the statute seeks to regulate "the transfer of property to a subsequent transferee, not the relationship of that property to a perhaps-distant debtor . . . . Here, the relevant transfers and transferees are predominately foreign: foreign feeder funds transferring assets abroad to their foreign customers and other foreign transferees." 513 B.R. at 227.
  - The court thus concluded that the presumption against extraterritoriality was not rebutted and "the Trustee may not use §550(a) to pursue recovery of purely foreign subsequent transfers." *Id.* at 232.
  - The court also held that international comity precluded recovery from foreign subsequent transferees.

Discussion of key subsequent transferee defenses issues - other *(cont.)*

Extraterritoriality and Fraudulent Transfers (cont.)

- The actions were remanded to the bankruptcy court with instructions.
  - The bankruptcy court dismissed the trustee's claims on remand based on the presumption against extraterritoriality and comity.

- However, ***In re Irving H. Picard, Trustee for the Liquidation of Bernard L. Madoff Investment Securities*, Case No. 17-2992, 917 F.3d 85 (2d Cir. Feb. 25, 2019) (BLMIS)**, the Second Circuit, reversed the two lower court rulings.
  - The Second Circuit held that trustees *can* pursue recovery from foreign subsequent transferees who received property via transactions that occurred entirely outside of the US.
  - Specifically, the Second Circuit held that § 550(a) functions "in tandem" with § 548(a) such that the focus of the statute is the initial transfer which occurred *inside* of the US. *BLMIS*, 917 F.3d at 97-99.
    - The Second Circuit clarified that when § 550(a) operates in tandem with § 548(a), "recovery of property is 'merely the means by which the statute achieves its end of' regulating and remedying the fraudulent transfer of property." *Id.* at 98.

Discussion of key subsequent transferee defenses issues - other *(cont.)*

Extraterritoriality and Fraudulent Transfers (cont.)

- ***In re Irving H. Picard, Trustee for the Liquidation of Bernard L. Madoff Investment Securities*, Case No. 17-2992, 917 F.3d 85 (2d Cir. Feb. 25, 2019) (BLMIS) (cont.)**

  – Given the foregoing, the Second Circuit concluded that recovering property from foreign subsequent transferees is a domestic application of § 550(a) and therefore permissible.

  – The Second Circuit also disagreed with the lower courts regarding the issue of comity under the circumstances. It determined that "[t]he United States has a compelling interest in allowing domestic estates to recover fraudulently transferred property" and that the US' interest "outweighs the interest of any foreign state." *Id.* at 103.

Discussion of key subsequent transferee defenses issues – other *(cont.)*

Recovery of Proceeds of Fraudulently Transferred Property

- ***Generation Res. Holding Co.*, LLC, 964 F.3d 958, 963 (10th Cir. 2020)**
  - in its widely panned July 2020 decision, the United States Court of Appeals for the Tenth Circuit held that the remedy for recovery of some transfers is limited to the property actually transferred and not simply the proceeds therefrom
  - The question on appeal was whether, under Section 550, the trustee could recover proceeds of property that was the subject of an avoided fraudulent transfer from firms who received such proceeds.
  - The Tenth Circuit instructed that to state a claim under Section 550, three separate requirements must be satisfied:
    - 1. the trustee must invoke a transfer that was avoided under one of the enumerated sections of the Code;
    - 2. the trustee must plausibly allege that he seeks to recover *the property transferred* or the value of such property; and
    - 3. the trustee must plausibly allege that the defendants are either the initial transferee, the entity for whose benefit such transfer was made, or any immediate or mediate transferee of such initial transferee.

Discussion of key subsequent transferee defenses issues - other *(cont.)*

Recovery of Proceeds of Fraudulently Transferred Property(cont.)

- ***Generation Res. Holding Co.*, LLC, 964 F.3d 958, 963 (10th Cir. 2020) (cont.)**
  - The Tenth Circuit evaluated "the property transferred" with respect to the fraudulent transfer at issue, and it determined that the property transferred was the debtor's contractual "right and interest to be paid [certain] sales proceeds."
  - It then assessed whether the firms were "immediate or mediate transferees"—that is, subsequent transferees—of the actual property transferred.
    - The court ultimately determined that because the firms never received the actual property transferred, they were not subsequent transferees who could be recovered from under Section 550.
      - The court explicitly held that "property transferred" as related to an avoided transfer under Section 550 does not include proceeds of the property transferred.
  - In short, *Generation* stands for the proposition that the universe of transferees is limited to those who exercised dominion and control over the actual property transferred

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