

Prejudgment Asset Freezes: Where the Line Is Drawn

May 28, 2026

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In these turbulent times, more and more creditors are pushing for prejudgment asset freezes and restraints. Recent decisions in New York and Florida illustrate when that is possible.

A district court in New York was reversed when it granted a preliminary injunction against the assets of guarantors who did not give the creditors any security interest. Interestingly, a bankruptcy court in Florida gave a plan trustee an injunction in a fraudulent conveyance action.

The U.S. Supreme Court's decision in *Grupo Mexicano* is the common theme. *Grupo Mexicano de Desarrollo, S.A. v. Alliance Bond Fund, Inc.*, 527 U.S. 308 (1999). *Grupo Mexicano* is considered a departure from practice in the U.K. courts, which issue the so-called *Mareva* injunctions prohibiting defendants from transferring assets before judgment. See *Mareva Compania Naviera S. A. v. International Bulkcarriers S. A.*, 1 All E.R. 213 (1980). *Grupo Mexicano* stands for the proposition that an unsecured creditor has no rights, at law or in equity, in the property of his debtor before judgment.

New York (*Leadenhall v. Advantage Capital* – 2d Cir.)

The Second Circuit Court of Appeals confirmed that where a creditor has no rights in a debtor's assets, neither law nor equity shall operate to grant such rights prejudgment, and reversed, as an abuse of discretion, the District Court's grant of a preliminary injunction against the assets of guarantors.

The lenders extended a secured loan to borrower entities and obtained comprehensive collateral from the borrowers, but only unsecured guarantees from affiliated guarantors who pledged no assets. After discovering alleged fraud and default and accelerating roughly \$600 million in debt, the lenders sued for breach of contract, fraud, and RICO, and sought to freeze both borrower and guarantor assets prejudgment, based on fears of dissipation. The district court granted the injunction, but the Second Circuit reversed because, as to the guarantors, the lenders asserted only legal claims for money damages, identified no specific property, and held no lien or equitable interest in guarantor assets.

Those facts placed the case squarely within *Grupo Mexicano*. An unsecured creditor with a legal damages claim cannot restrain a defendant's general assets before judgment, even where dissipation is likely. The absence of any pledged collateral, traceable res, or equitable remedy (such as restitution of specific property) was dispositive.

Florida (*Vital Pharmaceuticals* – Bankr. S.D. Fla.)

In a recent decision, Judge Russin held that *Grupo Mexicano* was inapplicable in a case arising from the bankruptcy of *Vital Pharmaceuticals*, which was forced into bankruptcy after losing a false advertising lawsuit brought by its competitor, *Monster*

Energy.

The debtor's CEO, while the company faced massive and mounting litigation exposure, caused the company to transfer nearly \$10 million of corporate funds to purchase and maintain a specific luxury property titled in a shell entity he controlled, with no consideration flowing back to the company. The transfers occurred as the company was allegedly insolvent or rendered insolvent, and while facing hundreds of millions of dollars in contingent liabilities.

After confirmation of a liquidating plan, the trustee brought fraudulent transfer claims seeking to recover that specific real property (or its value), and moved to enjoin further encumbrance or transfer. Critically, the trustee traced estate funds directly into an identifiable res (the property) and pursued equitable relief, avoidance, and recovery of the property itself, not merely money damages.

The court granted the preliminary injunction, holding that *Grupo Mexicano* did not apply because the action fit within the traditional equitable exception. It was an equitable fraudulent-conveyance claim targeting specific property, where the injunction served to preserve the res pending adjudication. The strong factual showing of insider transfers, lack of value, insolvency, and pending litigation exposure further supported both the likelihood of success and the need to prevent dissipation.

The recent decisions underscore that *Grupo Mexicano* remains a firm constraint on prejudgment asset freezes in the United States: unsecured creditors pursuing legal claims for money damages cannot restrain a defendant's general assets absent a recognized equitable interest. At the same time, courts will grant such relief where the plaintiff can anchor its claim in equity by tracing funds to a specific, identifiable res and seeking recovery of that property. Ultimately, the outcome determinative factors are not urgency or risk of dissipation, but whether the creditors can tie their claim to an identifiable asset or equitable remedy.