SHORTER ARTICLES, COMMENTS AND NOTES

INTERNATIONAL INSOLVENCY AND THE ENFORCEMENT OF FOREIGN REVENUE LAWS*

In recent years there has been a considerable increase of interest in international bankruptcy and insolvency law, fuelled in no small measure by the failure of a number of well-known international concerns,[1] and augmented by legislative intervention on both sides of the Atlantic. For the domestic bankruptcy practitioner, the presence of an international element may lead him into quite unfamiliar areas; the conflicts lawyer, however, will at once identify issues of jurisdiction and the recognition of foreign judgments.[2] Complications, however, are introduced by the pervasive influence of policy considerations throughout modern insolvency law; the strength of the secured creditors' claims (and the corresponding plight of the unsecured), the extent of preferential debts of employees, and, perhaps more importantly, claims by revenue authorities, are all obvious manifestations of the political/economic attitude a particular country has adopted. These issues must surely be confronted before a satisfactory international agreement can be concluded.[3] In the meantime, such matters fall to be decided by reference to private international law and in particular the rules governing the recognition and enforcement of foreign bankruptcy adjudications.[4]

It must be stressed, however, that a modern insolvency case will, almost without exception, involve a demand by revenue authorities for unpaid taxes:[5] yet most systems of private international law established rules governing the recognition of foreign bankruptcies many years ago, when taxation had little importance in international commercial activity. If it were correct, as Lord Mansfield once said,[6] that "no country ever takes notice of the revenue laws of another," then it would seem that only a minority of foreign adjudications could be recognised; for, although countries adopt different approaches to questions of juris-

* This note was originally prepared as part of the British Institute of International and Comparative Law's programme of research into transnational insolvency law, although the views expressed are those of the author only.

1. See generally Riesenfeld (1976) 24 A.J.C.L. 288 and Nadelman (1984) 33 I.C.L.Q. 431.
2. Thus the EC Draft Bankruptcy Convention, following the approach adopted in respect of other civil judgments, sought to harmonise the laws of the Member States by conferring an exclusive jurisdiction upon the courts of one country which would be recognised throughout the Member States; see Fletcher, *Conflict of Laws and European Community Law* (1982), p.187.
3. Hence the apparent failure of the EC Draft Convention.
4. See generally, Dicey and Morris, *The Conflict of Laws* (10th ed.), pp.711 *et seq.*
5. See *per* Lockhart J in *Re Ayres* (1981) 34 A.L.R. 582 quoted *infra.*
6. *Holman* v. *Johnson* (1775) 1 Cowp. 341, 343. This statement has now been recognised as too broad; see e.g. *per* Denning LJ in *Regazzoni* v. *K.C. Sethia (1944) Ltd.* [1956] 2 Q.B. 490, 515, and *per* Lord Simonds [1958] A.C. 301, 319.

diction and recognition, there is a seemingly universally accepted principle that the courts of one country cannot be used as a tax-collecting agent for another. Thus, according to the conventional doctrine, a Dutch bankruptcy adjudication will not be recognised in England, in order that the Dutch trustee in bankruptcy might recover assets within England, if part of those assets would be used to satisfy a claim by the Dutch authorities in respect of the bankrupt's unpaid liability to tax. But it is inequitable that a foreign trustee's or receiver's claim should be rejected in every case where a foreign revenue debt is involved, particularly as the effect of non-recognition may be an undeserved windfall for those creditors who bring proceedings in England. Any conflicts rule which indiscriminately denies recognition, resulting in not only the unequal treatment of creditors but also a multiplicity of proceedings, is unsuitable for the modern commercial environment. This article examines the current status of the rule against the enforcement of foreign revenue laws in respect of, in particular, insolvency matters, and seeks to show how the restrictions imposed by that rule are gradually being lifted.

A. The General Rule Against Enforcement and its Apparent Exceptions

Despite many confident assertions that foreign revenue laws were never enforced, the point was only firmly established in England in *Government of India* v. *Taylor*,[7] a case where the claim had been brought directly by the foreign state: since then any doubt about the existence of a general rule has been dispelled, indeed the US Court of Appeals has stated:[8]

> The revenue rule has been with us for centuries and as such has become firmly embedded in the law. There were sound reasons which supported its original adoption, and there remain sound reasons supporting its continued validity. When and if the rule is changed, it is a more proper function of our policy-making branches of our government to make such a change.

Nevertheless, courts have on a number of occasions restricted the *scope* and *operation* of this general rule. Thus it is well settled that a foreign tax law can be recognised to the extent that the English courts will not enforce a contract which is illegal under its proper law, including any relevant revenue law (*Regazzoni* v. *K.C. Sethia (1944) Ltd.*).[9] Indeed, it has become apparent that the effect given to a foreign revenue law may depend, to a considerable degree, upon the proper law of the issue raised. In *Re Bliss' Trust*,[10] the US Supreme Court granted an injunction to prevent any assets of a trust, the proper law of which was New York law, being used by the trustees to discharge a liability to UK taxes. However, Slade J in *Re Lord Cable (deceased)*,[11] while accepting that a tax claim by a foreign government would not be enforced, was prepared to allow the English

7. [1955] A.C. 491.

8. *Her Majesty the Queen in Right of the Province of British Columbia* v. *Gilbertson* (1977) 433 F.Supp. 410; on appeal (1979) 597 F.2d 1161, 1166. See also *United States* v. *Harden* (1963) 41 D.L.R. (2d) 721 (Canada), *Re Dwele Estate* (1969) 69 W.W.R. 212 and *Jones* v. *Borland*, 1969 (4) S.A. 29.

9. [1956] 2 Q.B. 490, affirmed [1958] A.C. 301.

10. (1960) 208 N.Y.S.2d 725.

11. [1976] 3 All E.R. 416, 436.

trustees of a settlement, the proper law of which was the law of India, to pay Indian estate duty.[12]

The effect of refusing to prevent trustees discharging a liability to foreign tax goes beyond merely recognising the existence of a foreign revenue law, and actually allows that law to have an effect within the territory of the forum. It would seem therefore that circumstances may well exist where a trustee in bankruptcy, or a receiver, should not be prevented from using assets located within the jurisdiction to satisfy foreign tax liabilities. At first sight such a proposition might seem to offend the Irish case of *Peter Buchanan Ltd.* v. *McVey*[13] and the proposition that neither direct nor indirect attempts to enforce a foreign revenue law will be permitted. However, it will be recalled that in *Peter Buchanan Ltd.* v. *McVey*, although the proceedings were brought by a duly appointed liquidator, the case involved nothing more than an attempt by the Scottish revenue to enforce a tax debt: as Kingsmill Moore J pointed out,[14] that particular liquidator had been appointed because of his proven ability in tracking down revenue debtors; and, having paid the costs and expenses of the liquidators, any money recovered would have gone to the Scottish authorities.[15] After scrutinising the substance of the application, the court was convinced that the sole object and only purpose of the proceedings was to enforce a foreign revenue debt. Further, it should not be forgotten that Maguire CJ in the Supreme Court of Eire said:[16]

> I agree that, if a payment of a revenue claim was only incidental and there had been other claims to meet, it would be difficult for our courts to refuse to lend assistance to bring assets of the company under the control of the liquidator.

In the light of such considerations it is very difficult to maintain the proposition that "*in no circumstances* will the courts directly or indirectly enforce the revenue laws of another,"[17] particularly when one considers the decision of the Court of Session in *Scottish National Orchestra Ltd.* v. *Thomson's Executors*.[18] Here, the deceased had died domiciled in Sweden but with certain assets in Scotland, and the Swedish administrators sought to appropriate that property to pay (*inter alia*) Swedish inheritance duty; Lord Robertson said that the adminis-

12. Similar considerations would, it is submitted, apply where the courts are called upon to give effect to a change in the title to movables occurring e.g. as a result of a claim by foreign revenue authorities in accordance with the proper law of the transfer. In *Brokaw* v. *Seatrain UK Ltd.* [1971] 2 All E.R. 98, the US Government had served a notice of levy in respect of certain goods being shipped from America to England, because of an unpaid liability to tax. The Court of Appeal in England held that on the facts the goods had not been reduced into the possession of the US authorities; the Court stated, however, that if that notice of levy had been effective, the foreign government's claim might have been enforced on the basis of an actual possessory title (p.99).

13. [1954] I.R. 89; [1955] A.C. 516n.

14. [1955] A.C. 516n, 520.

15. See also *Bath* v. *British and Malayan Trustee Ltd.* [1969] 2 N.S.W.L.R. 114, where the application was really brought *only* to enforce a foreign revenue claim (*per* Helsham J, p.117).

16. *Idem*, p.533.

17. *Per* Lord Keith of Avonholm in *Government of India* v. *Taylor* [1955] A.C. 491, 510 (emphasis added).

18. [1969] S.L.T. 325.

trator's claim would fail if the only purpose had been to pay Swedish inheritance duty.[19] However, his Lordship found that, after the tax liability had been satisfied, the remaining property would be held for the beneficiaries in Sweden.[20] Accordingly, as it was not the sole or only purpose of the action to enforce a foreign revenue debt, the Swedish administrator succeeded in his claim.

It can scarcely be denied that Lord Robertson brought about the indirect enforcement of a foreign revenue law: his Lordship allowed a claim which could not have been brought by the revenue authorities of Sweden, but which, nevertheless, had the effect of enriching the Swedish revenue.

Although dicta in *Peter Buchanan Ltd.* v. *McVey* and the decision in *Scottish National Orchestra Ltd.* v. *Thomson's Executors*, show beyond any doubt that the indirect enforcement of a foreign revenue law may be permissible, it is by no means certain where the boundaries of such enforcement lie. Clearly an action will not be entertained if it is in substance a claim for a revenue debt; but Maguire CJ in *Peter Buchanan Ltd.* v. *McVey* thought otherwise if the foreign revenue aspect were only "incidental" and there were other, non-revenue, foreign creditors.[21] Lord Robertson in *Scottish National Orchestra Ltd.* v. *Thomson's Executors* appears to have contemplated a more liberal approach; for his Lordship made no reference to "incidental" and was prepared to allow the claim by a foreign administrator as long as the payment of a revenue debt was not the "only purpose" of the application.[22] Similar reasoning found favour in the Australian case of *Re Ayres, ex parte Evans*;[23] Ayres was adjudicated bankrupt in New Zealand and the High Court issued letters rogatory requesting the assistance of the Federal Court of Australia as the bankrupt had assets in Australia: in the New Zealand bankruptcy proceedings, revenue debts totalled more than 60% of all claims. The Federal Court held that the substance of the application was not the enforcement of a foreign revenue debt and rejected the argument that assistance should not be given where a "greater part"[24] of claims were by a foreign taxing authority. That decision was upheld on appeal, Fox J stating:[25]

> I think the preferable view to be that in a case such as the present where there are non-revenue as well as one or more revenue creditors the rule in question has no application.

B. *The Merits and Demerits of a More Flexible Approach*

In theory, as in practice, there is a great deal of merit in a relaxation of the rule against the enforcement of foreign revenue laws: a strict application of the rule

19. *Idem*, p.330.
20. *Ibid.*
21. *Supra* n.16.
22. *Supra* n.19.
23. (1981) 34 A.L.R. 582; on appeal (1981) 39 A.L.R. 129.
24. Whether this meant 50% or more was not made clear; see *per* Lockhart J (1981) 34 A.L.R. 582, 589.
25. (1981) 39 A.L.R. 129, 133; applied in *Priestly* v. *Clegg*, 1985 (3) S.A. 950 (Transvaal Provincial Division), where revenue debts were estimated as 94% of all claims (*Commissioner of Taxes, Federation of Rhodesia* v. *McFarland*, 1965 (1) S.A. 470 (W), was distinguished).

will deny success to every foreign creditor's claim simply because of the involvement, however marginal, of a foreign revenue authority. It must be stressed that the more flexible approach which has found favour in the courts is far-reaching, for it countenances the indirect enforcement of a foreign revenue law. There has been no attempt to divide up locally situated assets between a bankrupt's creditors, including any foreign creditors, on the fictional basis that a foreign tax liability does not exist; instead, a more realistic solution has been preferred, which takes into account the ever-present importance of taxation in international commercial activity and insolvency law. The absence of any blanket prohibition will often further the principle of equality between *all* the creditors of the bankruptcy; foreign claimants are not ignored, nor is an undeserved benefit conferred upon local creditors. Of course the promotion of equality between creditors discourages not only forum shopping but also a multiplicity of actions, thereby substantially reducing the costs incurred when proceedings are commenced in several jurisdictions.

Although a foreign revenue authority may not itself bring an action in a local court, it is not necessarily objectionable to recognise the same claim when made as one of many claims in a foreign bankruptcy adjudication. For it is a basic principle of private international law that a decision of a foreign tribunal, properly vested with jurisdiction, will be recognised in England even though our courts would have decided the matter quite differently had the original cause of action been brought in England.[26]

Nevertheless, the indirect enforcement of foreign revenue laws may produce certain difficulties. When considering the effect to be attributed to a foreign revenue law, the courts have in the past enquired into the *substance* of the matter raised:[27] an action brought by a liquidator will be struck down if it is, in reality, an attempt by a foreign State to enforce its own revenue laws. Where, however, there are creditors other than the foreign revenue authority, different considerations may apply. But it is easy to imagine a situation where foreign revenue debts amount to perhaps 30% of the total liabilities of the bankrupt: a court might allow locally situated assets to be remitted to the trustee in bankruptcy in the foreign country concerned. Yet, once the assets are abroad, there is nothing to prevent the foreign revenue authority imposing additional taxes, or opening up the bankrupt's accounts and making a new, much higher, assessment, so that all, or at least most, of the bankrupt's assets come into the hands of the foreign taxing authority. (See, for instance, section 460 of the Income and Corporation Taxes Act 1970, under which the Revenue may cancel a tax advantage up to *six years* after the chargeable period to which the tax advantage relates.) However, the recognising court cannot be certain what steps a foreign revenue authority may take, perhaps several years in the future, to recover additional taxes: further, an enquiry into the motives or behaviour of a foreign

26. See generally, *Dicey and Morris, op. cit. supra* n.4, at p.1073.

27. Apart from the cases discussed above, see *Re a Request for International Judicial Assistance* (1979) 102 D.L.R.3d 18, where the Alberta Queen's Bench enforced letters rogatory to assist a foreign tax evasion prosecution because " . . . the pith and substance of the charges are criminal in nature and the assistance of our Court is sought primarily to enable a full hearing to be held on the criminal charges rather than to help the United States collect alleged arrears of income tax" (*per* Miller J, p.38).

revenue authority could prove to be politically sensitive. Quite plainly, permitting even a limited recognition and enforcement of a foreign revenue law may lead to abuse by foreign governmental authorities. Yet the danger of abuse has always been present; liquidators have not always made it clear that they are, in reality, representing a foreign revenue authority;[28] but in practice most revenue authorities behave reasonably, not hiding behind men of straw[29] in an attempt to deceive the courts of friendly neighbouring States.[30] Where "shadowy" claims are made, or there is a hint of concealment, then a judge may be able to exercise his discretion to deny recognition without causing grave political embarrassment. In those few instances where, in substance, there is nothing more than a foreign revenue claim, recognition must be refused, but has this not always been the case? Indeed, the suggested relaxation of the non-enforcement rule will promote frank disclosure by the parties, and will serve rather to diminish an unnecessary area of possible conflict between States.

In the final analysis, however, it must be accepted that the old private international law prejudice against foreign revenue laws can no longer be maintained. It is incongruous for any rational system of jurisprudence which, after all, has as its objective the resolution of disputes between competing laws and jurisdictions, to ignore the influence of the State, in the form of taxation, in modern international business activity. Outdated concepts of sovereignty have, at times, allowed once viable rules of international law, both public and private, to survive beyond their useful lifespan. Ultimately, however, those rules must be modified to take account of the changes in both the role of governments and commercial practice (one might consider in this context the doctrine of absolute sovereign immunity). Many commentators have called for the abolition of the rule against the enforcement of foreign revenue laws[31] and at a later stage the House of Lords, or Parliament, may reconsider the very foundation of the rule. Undoubtedly there are many theoretical difficulties; yet already the judges have appreciated the practical necessity of placing some limitation upon the operation of that rule. Such a development must surely serve to promote a more effective,

28. See e.g. *Re Gibbons, ex p. Walter* [1960] Ir.Jur.Rep. 60, where the High Court of Justice in Ireland made a verbal order to assist the English official receiver's efforts to have the bankrupt's assets, situated in the Republic, transferred to England, but, before that order was perfected, it was revealed that the English bankruptcy proceedings were being used to enforce an English revenue debt.

29. See the comment by Stoel (1967) 16 I.C.L.Q. 663, 679.

30. See *passim, Banco Frances E Brasiliero S.A.* v. *Doe* (1975) 331 N.E.2d 502: the Court of Appeals of New York was asked not to recognise or give effect to certain currency regulations of a foreign state: the Court considered that currency regulations did not fall within the prohibition against the enforcement of foreign revenue laws: however, even if currency regulations had been considered as equivalent to revenue laws, the Court considered that, as both countries involved (the USA and Brazil) were members of the International Monetary Fund, it would be inappropriate to deny effect to the foreign law (*per* Jasen J, p.506).

31. See M. Mann (1954) 3 I.C.L.Q. 465, Albrecht (1950) 30 B.Y.I.L. 454 and, more recently, Carter (1984) 55 B.Y.I.L. 111. Although it is worthy of note that the Court of Appeal and House of Lords have recently referred to the rule without any mention of abolition or of refinement, see *Williams & Humbert Ltd.* v. *W & H Trade Marks (Jersey) Ltd. and others* [1985] 2 All E.R. 619, 626 and 631; [1986] 2 W.L.R. 24.

as well as realistic, legal framework in which international insolvency practitioners may operate.

P. ST. J. SMART

TRANSBORDER DATA FLOWS: THE EUROPEAN CONVENTION AND UNITED KINGDOM LEGISLATION

IN the last ten years there has been considerable legislative activity by European Parliaments in the area of data protection. Such legislation has sought to impose controls on the processing of personal data and to lay down standards of privacy protection. Most countries have placed the controls and standards in the context of a registration or licensing scheme supported by the criminal justice system.[1] The United Kingdom has joined the list of countries that have data protection laws by enacting the Data Protection Act 1984 (the "DPA").[2]

In common with other legislation in this area, the DPA is concerned exclusively with "automatically processed information"[3] or what is called "data". Unless information is recorded in a form in which it can be processed by equipment operating automatically in response to instructions given for that purpose, it is not within the scope of the Act. In effect the privacy standards enshrined in the legislation can be lawfully evaded by transferring sensitive information to manual information systems.[4] The justification for treating automatically processed or computerised information separately is that the use of computers creates unique risks to individual privacy with their capacity to store, handle, retrieve and transfer data at great speed. A government white paper in 1975 observed that computer operations have five features which pose a special threat:

(1) they facilitate the maintenance of extensive record systems and the retention of data in those systems;
(2) they can make data easily and quickly accessible from many different points;
(3) they make it possible for data to be transferred quickly from one information system to another;
(4) they make it possible for data to be combined in ways which might not otherwise be practicable;
(5) because the data are stored, processed and often transmitted in a

1. Austria, Denmark, the Federal Republic of Germany, France, Iceland, Luxembourg, Norway and Sweden.
2. The Act received the royal assent on 12 July 1984 and will be fully in force on 11 Nov. 1987.
3. S.1(2).
4. For a criticism of this aspect of the DPA, see *National Council for Civil Liberties Briefing 1984*, para.2.1.