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The Myth of Cross-Border Cooperation: Mutual Assistance for the Collection of Tax Claims in Cross-Border Insolvencies

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THE MYTH OF CROSS-BORDER COOPERATION: MUTUAL ASSISTANCE FOR THE COLLECTION OF TAX CLAIMS IN CROSS-BORDER INSOLVENCIES

MATHEWS VATTAMALA

“No country is an island to itself.” Cross-border tax cooperation and compliance are crucial to the health of the United States economy and the protection of its tax base. Yet, foreign courts administering cross-border insolvencies may deny a U.S. tax claim, even when such claims are treated as secured claims under local law. In a similar vein, a U.S. bankruptcy court recently refused to recognize the tax claim of a foreign government in reliance of the anachronistic common law doctrine, known as the “revenue rule.” To ensure other governments extend the U.S. the necessary cooperation it will need to collect its tax claims in the cross-border context, this Article recommends that the U.S. government:

(1) revoke the revenue rule; or at minimum grant an exclusion to employee pension and insolvency related claims;
(2) amend its current network of bilateral tax treaties to incorporate specific provisions to provide mutual assistance in the collection of tax claims in cross-border insolvencies;
(3) initiate a dialogue with the member nations of the Organization for Economic Cooperation and Development to create measures that protect the tax base of every nation without discouraging competition or the cross-border flow of business, capital, and ideas.

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I. INTRODUCTION

“Tax co-operation and compliance are of crucial importance for all countries and citizens - and not only in times of a tight fiscal and budgetary environment.” ¹ If we accept these assertions as true, what should it mean for a country to provide legitimate tax co-operation and compliance? And what would such co-operation and compliance look like in practice? Because a U.S. or foreign multinational can incur significant tax liabilities in one State,² and within the time it takes to press enter on a computer keyboard, transfer its assets and capital to another State,³ any adequate response must address the treatment of governmental tax claims in the context of cross-border insolvencies.⁴

Today, capital and assets move throughout the world at an unprecedented rate. For example, the United States Department of Commerce, Bureau of Economic Analysis (BEA) estimates that the exports of goods and services, and income receipts from the United States totaled $2.5 trillion ($1.83 trillion in goods and services and $0.66 trillion in income receipts of U.S. owned assets in foreign jurisdictions) for calendar year 2010.⁵ For the same period, the BEA estimates total imports of goods and services, and income payments of $2.83 trillion into the United States ($2.33 trillion in goods and services and $0.5 trillion in income payments on foreign-owned assets in the U.S.).⁶ And the total U.S. gross domestic product (GDP)⁷ for 2010 is estimated at $14.66 trillion.⁸ Therefore, total exports and imports of goods, services, and income receipts for the U.S. in 2010, is equivalent to 37%⁹ of the entire U.S. GDP for 2010. Given this

¹ OECD Secretary-General Angel Gurría, Cannes G20 Summit, 2011, Available at: http://www.oecd.org/document/48/0,3746,en_2649_37427_48981680_1_1_1_37427,00.html (last visited November 9, 2011).
² This Article refers to sovereign nations as State/s and countries.
³ See Lawrence Collins, Professor Lowenfeld And The Enforcement Of Foreign Public Law, 42 N.Y.U. J. INT’L L. & POL. 125, 148 (citing) (Professor Lowenfeld was responsible for the following section of the Restatement of the Law of Foreign Relations: “in an age when ... instantaneous transfer of assets can be easily arranged, the rationale for not recognizing or enforcing tax judgments is largely obsolete.” RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW OF THE UNITED STATES § 483, Reporter’s Note 2 (1987)).
⁴ For the purposes of this Article, a cross-border insolvency is any insolvency proceeding where a debtor has substantial assets in more than one country.
⁶ See id.
⁹ The percentage of U.S. GDP for 2010 that is equivalent to the total cross-border trade for the U.S. in 2010 is derived from the following calculation: $5.33 trillion (the total estimated U.S. exports and imports for calendar year
data, and the fact that 25% of U.S. exports are connected to income receipts from U.S. owned foreign assets, it is clearly in the best interest of the U.S. to continue to develop cooperative relationships with its trading partners, and thus secure its ability to collect the taxes due on such income.

Tax cooperation and compliance are crucial to the health of the U.S. economy and the protection of its tax base. Yet, as this Article will show, a foreign court can deny a U.S. tax claim even when the tax claim would be treated as a secured claim under U.S. law. In a similar vein, a U.S. bankruptcy court recently refused to recognize the tax claims of a foreign government, not on the merits of the claim, but in reliance of the anachronistic common law doctrine known as the “revenue rule.” That decision also serves as a clear illustration that the best tool available to U.S. bankruptcy courts for the administration of a case with cross-border implications, Chapter 15 of the U.S. Bankruptcy Code, fails to address the issue of secured or priority tax claims of foreign jurisdictions.

Given the extensive network of bilateral tax-treaties in-force between the U.S. and foreign governments, why do U.S. bankruptcy courts refuse to recognize foreign tax claims, and vice versa? This Article shows how a string of poorly reasoned U.S. court decisions that adopt an unnecessary allegiance to the “revenue rule” led to this result in the United States.

To ensure the United States can secure the assistance of other countries for assistance to collect its tax claims, as well as legitimize its requests for such assistance, this Article recommends that the U.S. government:
(1) revoke the common law doctrine of the revenue rule, or at minimum provide an exclusion in the context of cross-border bankruptcies and pension related claims both in and out of bankruptcy;
(2) amend its network of bilateral treaties to incorporate provisions for mutual assistance in the collection of tax claims that arise in the context of bankruptcy, and:
(3) initiate a dialogue with the other member nations of the Organization for Economic Co-Operation and Development (OECD) and the G-20 to identify measures that will protect the tax base of each country without discouraging competition and the cross-border flow of business, capital, and ideas.

2010, see notes 4 and 5 supra); divided by $14.33 trillion (the estimated total U.S. GDP for 2010, see note 6 supra); multiplied by 100%.

10 See infra notes 233-245 and accompanying text.
11 See discussion of In re BearingPoint, infra notes 253-304 and accompanying text.
13 Pre-cursor to the G-20, G-7 established in 1976 by its founding members: Canada, France, Germany, Italy, Japan, the United Kingdom and the U.S. The G-7 conducts dialogue and seeks agreement on current economic issues on the basis of the comparable interests of those countries. How does the G-20 differ from the G-7? Available at: http://www.g20.org/about_faq.aspx, (last visited December 20, 2011); G-20 was established in 1999 and reflects the diverse interests of the systemically significant industrial and emerging-market economies. The G-20 nations include: Argentina, Australia, Brazil, Canada, China, European Union, France, Germany, India, Indonesia, Italy, Japan, Mexico, Russia, Saudi Arabia, South Africa, Republic of Korea, Turkey, United Kingdom, and the United States of America. See G-20, About the G-20, available at: http://www.g20.org/about_what_is_g20.aspx (last visited December 22, 2011).
The revenue rule must be revoked to ensure U.S. courts will perform the requisite level of analysis to adjudicate foreign claims within the context of the global economy and contemporary U.S. policy. Further, while the revenue rule ‘lives,’ foreign governments have no reason to believe that the U.S. would consistently fulfill a commitment to provide assistance in the collection of tax claims.

The ‘death’ of the revenue rule is likely to improve the success of the second recommendation. Currently, there are over sixty-five bilateral income tax treaties in-force between the U.S. and other nations.\footnote{See I.R.S. Publication 901 (April 2011) Table 3. List of Tax treaties (Updated through March 11, 2011), available at: \url{http://www.irs.gov/pub/irs-pdf/p901.pdf} (last visited December 24, 2011).} Five of those treaties provide for mutual assistance in the collection of certain taxes.\footnote{See infra notes 181-185 and accompanying text.} Therefore, this Article contends that were the U.S. to request an amendment to provide for mutual assistance in the collection of bankruptcy related tax claims; its treaty partners, particularly those countries already committed to mutual assistance in other tax claims, are likely to agree for at least two reasons. One, any concern as to whether the U.S. would reciprocate would be moot. Because the request to amend the treaty would establish that the U.S. intends to reciprocate.\footnote{See infra notes 173-185 and accompanying text.} Second, because U.S. courts must respect and enforce the provisions of an in-force tax treaty.\footnote{See Pasquantino v. United States 544 U.S. 349, 374 (2005).}

The U.S. has played a significant role in efforts to advance cooperation in cross-border commerce since the early twentieth-century.\footnote{See infra notes 206-232 and accompanying text.} Moreover, the U.S. economy is the largest in the world.\footnote{See supra note 6.} And as a nation, the U.S. is the top investing country in the world, as well as the largest beneficiary of foreign direct investment.\footnote{Foreign Direct Investment (FDI) Statistics - OECD Data, Analysis and Forecasts, FDI IN FIGURES, October 2011- Revised, available at \url{http://www.oecd.org/document/8/0,3746,en_2649_33763_40930184_1_1_1_1,00.html} (last visited December 26, 2011). For 2010, foreign direct investment into the U.S. totaled $236.2 billion. And U.S. interest invested $351.4 billion in other countries for the same period.} Therefore, in a world where physical borders mean less and less every day, the U.S. is the ideal candidate to open a dialogue with the rest of the world to address the treatment of tax claims in cross-border bankruptcies on a global scale.

The Article starts by illustrating why unresolved issues in the cross-border context can significantly impact the economic interests of the United States. Part I provides an overview of the administration of a cross-border insolvency under Chapter 15 of the United States Bankruptcy Code and the historical development of cross-border insolvency administration under U.S. law.\footnote{See 11 U.S.C. §§ 1501-1524.}

Part II sets forth the treatment of United States tax claims under domestic law and the specific public policy concerns implicated by the uncertain treatment of secured-tax claims in cross-border insolvencies, particularly in the context of pension benefit claims.

Part III shows the current role of bilateral tax treaties under U.S. law and examines how well the U.S. and other model conventions address the treatment of priority and secured tax claims in cross-border insolvencies.
Part IV illustrates how U.S. courts would treat foreign tax claims in a cross-border insolvency based on the current law and in-force treaties. As well as how a foreign court would treat a U.S. tax claim in the same context and under the same principles.

Part V describes the common law doctrine of the revenue rule, and shows how its continued relevance both in and out of the bankruptcy context “short-circuits” measures put in place by the United States Congress to address contemporary concerns.

Part VI proposes the resolution of the treatment of secured tax claims in a cross-border insolvency by amending the in-force bilateral tax treaties between the United States and the revocation of the revenue rule) would provide an effective solution to the issues identified, and combat tax evasion worldwide.

The Article concludes with a discussion of how the changes proposed reflect and legitimize the long-standing commitment on the part of the United States to advance the worldwide interest of providing mutual assistance in the administration of tax matters.

II. PRESENT TREATMENT OF CROSS-BORDER INSOLVENCIES UNDER U.S. LAW


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27 Id.
the concern that a lack of coordination and cooperation in cross-border insolvencies made it unlikely that a debtor would emerge as a viable business post-bankruptcy as well as hindered efforts to ensure a fair and efficient distribution of the debtors’ assets.\(^{28}\) Although Chapter 15 is discussed in greater detail below, a brief discussion of the underlying theory and intended purpose of the Model Law should prove useful.\(^{29}\) Before the Model Law, a global mechanism for courts to address cross-border insolvencies did not exist.\(^{30}\) And to ‘capitalize’ on this fact, multinational debtors “focused first on where--in what country--they would file for bankruptcy,”\(^{31}\) i.e., the forum.\(^{32}\) Because many countries refuse to acknowledge the laws of another, by filing for bankruptcy in a given forum, a multinational debtor could potentially “avoid a priority that would otherwise be enjoyed by a particular creditor constituency in another country where some assets or operations were located.”\(^{33}\) Moreover, the selection of forum is important for debtors because it is the laws of the forum that control the administration of a bankruptcy\(^{34}\), and any choice of law questions that arise.\(^{35}\)

Thus, before the Model Law, a multinational contemplating bankruptcy could base its decision on where to file on how the laws of the forum would affect its assets subject to security and priority interests worldwide.\(^{36}\) But, gaining access to a given forum alone, does not guarantee a strategically filing multinational that it would succeed in extinguishing the secured and priority claims held by creditors on its assets located outside the jurisdiction of the forum. Because, a forum has no legal means to compel a court in another country (the ancillary court) to turnover the debtor’s assets under its jurisdiction for administration and distribution under the laws of the forum. Understandably, ancillary courts would be especially disinclined to accommodate such requests, when the likely result was the impairment, if not complete disregard, of local creditors’ interests in the subject assets.\(^{37}\) The following hypothetical serves to illustrate the point.

In 2004,\(^{38}\) XYZ a U.S. multinational files for bankruptcy in a New York court. XYZ’s assets include real property and inventory in Canada subject to Canadian secured and priority interests. To administer the bankruptcy, the New York court submits a request to the Canadian

\(^{28}\) Id.
\(^{29}\) See The Hon. Leif M. Clark & Karen Goldstein, Sacred Cows: How to Care for Secured Creditors’ Rights in Cross-Border bankruptcies, 46 TEX. INT’L L. J. 513, 515 note 3 (quoting Vern Countryman, “[t]o understand how we hot where we are it is necessary to understand where we were.” Marshall v. Stern, 600 F. 3d 1037, 1050 (9th Cir. 2010) (quoting Vern Countryman, Scrambling to Define Bankruptcy Jurisdiction, 22 HARV. J. ON LEGIS. 1, 2 (1985))).
\(^{30}\) See id. at 515.
\(^{31}\) See id. n. 5.
\(^{32}\) Unless otherwise provided, in this Article, the term forum refers to the court where a debtor files for bankruptcy.
\(^{33}\) See supra note 29.
\(^{34}\) See id. n. 6.
\(^{35}\) See id. n. 7.
\(^{36}\) See id. n. 8.
\(^{37}\) See In re HAMILTON, 240 F.3d 148 (2d Cir. N.Y. 2001); see infra notes 96-114 and accompanying text.
\(^{38}\) The hypothetical uses 2004 as the time of XYZ’s filing because the United States and Canada enacted the Model Law in 2005 and 2009 respectively. See supra note 25.
court with jurisdiction over XYZ’s assets to turnover the assets for administration and distribution to all of XYZ’s creditors under U.S. law. The Canadian court considers the request, and determines that the New York court will treat the Canadian priority and secured claims as general unsecured claims. And under U.S. law, general unsecured claims are granted the lowest priority in distribution of a debtor’s assets.\(^{39}\) Therefore, even if the value of XYZ’s Canadian assets far exceed the secured and priority claims held by Canadian creditors, such creditors could receive nothing in the administration of XYZ’s bankruptcy. To determine whether to honor the request, the Canadian court must consider its duty to local interests against the ‘global’ interest of XYZ emerging from bankruptcy as a viable business.\(^{40}\) In consideration of this and other issues that can arise in the cross-border context, UNCITRAL created the Model Law.\(^{41}\)

Before turning to the procedural aspects of Chapter 15\(^{42}\) it is important to point out how the environment prior to Chapter 15 relates to the problem this Article seeks to resolve. Before Chapter 15, U.S. courts charged with the administration of a U.S. multinational debtor’s bankruptcy faced several ‘hurdles’ to complete its task. First and foremost, courts had to seek the assistance of their foreign counterparts to marshal a debtor’s assets outside of the United States. Provisions of the United States Bankruptcy Code\(^{43}\) prevent creditors from moving forward on any collection efforts against a debtor’s assets during the pendency of a bankruptcy. But, such provisions do not prevent the collection efforts of creditors against a debtor’s assets located outside of the United States.

### A. The Purpose and Procedure of Chapter 15

Chapter 15 is the only chapter of the United States Bankruptcy Code\(^{44}\) that sets forth an explicit statement of its intended goals, function, and scope.\(^{45}\) Specifically, Chapter 15 endeavors to advance:

- cooperation between United States courts, trustees, examiners, debtors, and debtors in possession and the courts and other competent authorities of foreign countries;
- greater legal certainty for trade and investment;
- fair and efficient administration of cross-border insolvencies that protects the interests of all creditors and other interested entities, including the debtor;
- the protection and maximization of the debtor’s assets; and
- the facilitation of the rescue of financially troubled businesses.\(^{46}\)

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41 See supra note 25.
42 See supra note 22.
43 See infra notes 65–91 and accompanying text.
To facilitate these goals, Chapter 15 permits courts to also grant assistance to representatives from countries that have not enacted the Model Law, *i.e.*, do not offer the U.S. reciprocity.\(^47\) In contrast, several other countries that have also enacted the Model Law, condition assistance on reciprocity.\(^48\) Thus, the framework of Chapter 15 allows a court to take a more holistic approach than some of its contemporaries when administering cross-border insolvencies. The scope of Chapter 15 is set forth in section 1501 (b).\(^49\) Specifically, Chapter 15 applies when:

1. a foreign court or representative seeks assistance with a foreign proceeding;
2. a foreign court or representative seeks assistance in a foreign country with a case under the United States Bankruptcy Code;
3. a debtor is subject to a foreign proceeding and a U.S. bankruptcy proceeding concurrently; or
4. creditors or other parties in a foreign country possess an interest in requesting the commencement of or participating in a pending case or proceeding under the United States Bankruptcy Code.\(^50\)

Apparently, the scope of Chapter 15 is quite broad; however, there are some important exceptions, discussed in greater detail below, that limit its applicability.\(^51\)

**B. Procedure to Commence a Chapter 15 Case**

Technically, a Chapter 15 case commences when a foreign representative files a petition requesting a U.S. bankruptcy court to grant “recognition” of a foreign proceeding.\(^52\) “Recognition” is defined as the “entry of an order granting recognition of a foreign main proceeding or foreign nonmain proceeding [under Chapter 15]; and within the territorial jurisdiction of the United States.”\(^53\) A debtor’s property “within the territorial jurisdiction of the United States”\(^54\) includes all tangible property located in the U.S.\(^55\); intangible property deemed in the U.S. under applicable nonbankruptcy law\(^56\); and “any property subject to attachment or garnishment that may properly be seized or garnished by an action in a Federal or State court in the United States.”\(^57\)

\(^47\) See Ranney-Marinelli, *supra* note 45, at 271 n. 12.

\(^48\) See id. (“A reciprocity requirement has been imposed *de jure* or *de facto* in the British Virgin Islands, Mexico, Romania, and South Africa.”). See Look Chan Ho, *Overview*, in CROSS-BORDER INSOLVENCY: A COMMENTARY ON THE UNCITAL MODEL LAW, 8 (Look Chan Ho ed., 2009).

\(^49\) See 11 U.S.C. §1501 (b).

\(^50\) See id.

\(^51\) See 11 U.S.C. §103 (k)(1), (2).


\(^53\) 11 U.S.C. § 1502 (7), (8).

\(^54\) 11 U.S.C. § 1502 (8).

\(^55\) Id.

\(^56\) Id.

\(^57\) Id.
Once a U.S. court grants recognition, it must determine whether a foreign proceeding is a “main” or “non-main” proceeding. Chapter 15 defines a “foreign main proceeding” as a foreign proceeding pending in the country that is the “center of main interest” or COMI of the debtor. Chapter 15 does not define or provide a clear standard for what level of activity or contact by a debtor would give rise to a COMI. However, U.S. caselaw provides that a COMI “generally equates with the concept of a ‘principle place of business’ in United States law.” But “[i]n the absence of evidence to the contrary the debtor’s registered office is presumed to be the center of the debtor’s main interest.”

Once a U.S. court determines a foreign proceeding is a foreign main proceeding, Chapter 15 requires the court to recognize such proceeding. Upon such recognition, several provisions of the Bankruptcy Code immediately go into effect. Arguably, the most important of those provisions is “the automatic stay.” In broad strokes, the automatic stay prohibits any creditor action against the debtor or the “property of the estate.” Simultaneously, the automatic stay maintains order amongst the numerous and well-informed creditors who would otherwise engage in a “free-for-all” to attach their interests or claim to a debtor’s assets.

11 U.S.C. § 1517 (a), (c).  
See Ranney-Marinelli, supra note 45, at 279.  
See 11 U.S.C. §1520 (a)(1); provisions of the bankruptcy code that immediately apply include the automatic stay pursuant to 11 U.S.C. § 362, and the right to adequate protection under 11 U.S.C. § 361 “with respect to the debtor and the property of the debtor that is within the territorial jurisdiction of the United States.”  
See 11 U.S.C. §§ 362 (a), and 507. 11 U.S.C. §362 (a) specifically provides: (1) the commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case under this title, or to recover a claim against the debtor that arose before the commencement of the case under this title; (2) the enforcement, against the debtor or against property of the estate, of a judgment obtained before the commencement of the case under this title; (3) any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate; (4) any act to create, perfect, or enforce any lien against property of the estate; (5) any act to create, perfect, or enforce against property of the debtor any lien to the extent that such lien secures a claim that arose before the commencement of the case under this title; (6) any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the case under this title; (7) the setoff of any debt owing to the debtor that arose before the commencement of the case under this title against any claim against the debtor; and (8) the commencement or continuation of a proceeding before the United States Tax Court concerning a tax liability of a debtor that is a corporation for a taxable period the bankruptcy court may determine or concerning the tax liability of a debtor who is an individual for a taxable period ending before the date of the order for relief under this title.  
bankruptcy Code defines “estate property” as a debtor’s property, “wherever located and by
whomever held,” the automatic stay has no legal effect outside of the U.S. Therefore, a Chapter
15 proceeding will not hinder the collection efforts of creditors against a debtor’s assets located
outside the U.S.71

Upon recognition, a court may ‘entrust’ all or just a portion of a debtor’s U.S. assets72 to
a foreign representative.73 However, such “entrustment” does not mean that a foreign
representative can distribute all of a debtor’s U.S. assets as they see fit.74 Rather, courts may
limit such entrustment to only a portion of a debtor’s U.S. assets.75 Furthermore, entrustment is
only granted by a court if it is certain that the interests of U.S. creditors76, other interested
parties, and the debtor are all “sufficiently, protected.”77 Because, the legislative history and text
of Chapter 15 are both ‘silent’ as to what it means for an interest to be “sufficiently protected,” guidance must be derived from case law.78

Post-recognition, a court may provide a foreign representative any “additional
assistance” available under the provisions of Chapter 15, and the “other laws of the United
States.”80 To determine whether such assistance is warranted, a court must consider whether the

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Maxwell Communication Corporation Case: One Example of Progress in the 1990s, in International Bankruptcies: Developing Practical Strategies 7, 10 (Practicing Law Institute Series No. 628, 1992)).

72 See supra notes 49-51 and accompanying text.
74 Id.
75 Id.
78 Id. To avoid confusion, the U.S. legislature amended the word “adequately” in Articles 21(2) and 22 (1) of the Model Law to “sufficiently” in section 1521(b) and section 1522(a). Because, “adequately protected” is “a term that has history and baggage that Congress intended not to import into those provisions of Chapter 15.” See H. R. Rep. No. 109-31, § 1521, at 115 (2005) (“The word ‘adequately’ in the Model Law, articles 21(2) and 22(1), has been changed to "sufficiently" in sections 1521(b) and 1522(a) to avoid confusion with a very specialized legal term in United States bankruptcy, 'adequate protection'.").
79 See Jeremy Leong, Is Chapter 15 Universalist or Territorialist? Empirical Evidence from United States Bankruptcy Court Cases, 13 (2010) (unpublished manuscript), available at: http://works.bepress.com/jeremy_leong/1 (last visited December 1, 2011). Leong examined 94 Chapter 15 cases filed between October 17, 2005 and June 8, 2009 and found that although U.S. courts granted recognition in 94% of the total cases, in only 8.5% of the total cases did the court grant entrustment without qualifications when U.S. creditors and assets were implicated.
81 See id.; the full text of § 1507 provides:
(a) Subject to the specific limitations stated elsewhere in this chapter [11 USCS §§ 1501 et seq.] the court, if recognition is granted, may provide additional assistance to a foreign representative under this title or under other laws of the United States.
(b) In determining whether to provide additional assistance under this title or under other laws of the United States, the court shall consider whether such additional assistance, consistent with the principles of comity, will reasonably assure--
   (1) just treatment of all holders of claims against or interests in the debtor's property;
   (2) protection of claim holders in the United States against prejudice and inconvenience in the processing of claims in such foreign proceeding;
   (3) prevention of preferential or fraudulent dispositions of property of the debtor;
assistance reasonably assures: the just treatment of all claim holders, the protection of U.S. claim holders against prejudice and inconvenience, the prevention of fraudulent transfers of estate property, the distribution order of estate property under the U.S. Bankruptcy Code, and the debtor’s ‘fresh start.’ Essentially, once a U.S. bankruptcy court determines a foreign proceeding is a “foreign main proceeding,” there is a sizable reservoir of additional relief available to the foreign representative. On the other hand, if a U.S. court determines a foreign insolvency proceeding is a nonmain proceeding (ancillary), the court may still recognize the proceeding. And in such cases, the court rather than the provisions of Chapter 15 control the scope of assistance. Thus, whether a foreign insolvency is a main or nonmain proceeding is not dispositive for the scope of assistance a U.S. court will provide.

Although recognition of a foreign main proceeding is mandatory, a court may deny recognition if it “would be manifestly contrary to the public policy of the United States” to do so. The legislative history of Chapter 15 provides that Congress intended the term “manifestly” to emphasize that the public policy exception should only apply to “the most fundamental policies of the United States.” Neither the Model Law nor the provisions of Chapter 15 define the term “public policy.” However, case law indicates that U.S. courts view the application of the public policy exception narrowly.

To gain a deeper understanding of the policy and procedural concerns Chapter 15 endeavors to address, an examination of the ‘tools’ U.S. courts relied upon before its enactment to administer cross-border insolvencies should prove helpful. The United States Congress enacted Chapter 15, and repealed its functional predecessor, section 304 of the Bankruptcy

(4) distribution of proceeds of the debtor's property substantially in accordance with the order prescribed by this title; and

(5) if appropriate, the provision of an opportunity for a fresh start for the individual that such foreign proceeding concerns.

86 See 11 U.S.C. § 1507 (b)(5). Any assistance offered under § 1507 must also comport with the principle of “comity.” See infra notes 80-91 and accompanying text.
88 See Clark and Goldstein supra note 29 at 527 (citing) (11 U.S.C. §§1519, 1521, 1507, 1522 (2005); Model Law, supra note 22, art. 21; Legislative Guide, supra note 85, paras. 135-137, 154-157)).
91 See id.
95 See id. at 340-350.
Code under the same legislation. Section 304 provided the framework to administer the ancillary cases of foreign insolvency proceedings filed in the United States. The basic underlying principle of Section 304 was to encourage U.S. courts to facilitate a unitary distribution of a debtor’s estate and to extend deference to foreign insolvency proceedings. To achieve those ends, section 304 provided bankruptcy courts significant flexibility to enable the best possible remedy for a given case. However, section 304(c) required bankruptcy courts to determine whether to assist a foreign representative by considering the “global interest” of a fast and efficient administration of a debtor’s insolvency against six factors. Those six factors included: the just treatment of all claim holders, the protection of U.S. claim holders against prejudice and inconvenience, the prevention of fraudulent transfers of estate property, the just treatment of all claim holders, the protection of U.S. claim holders against prejudice and inconvenience, the prevention of fraudulent transfers of estate property, the just treatment of all claim holders, the protection of U.S. claim holders against prejudice and inconvenience, the prevention of fraudulent transfers of estate property,
effect on the distribution order of the estate property prescribed under the U.S. Bankruptcy Code, granting the debtor a fresh start, and comity. Although Congress repealed section 304, five of the factors under section 304(c) are reproduced almost in their entirety in section 1507(b). Section 1507(b) ‘transplants’ one of section 304(c)’s six factors, comity, to the introductory text “to make it clear that it is the central concept to be addressed.” Because comity is a foundational principle of Chapter 15 and section 304(c) a brief overview of the concept will prove useful.

Before the enactment of section 304 in 1978, U.S. courts analyzed questions of law implicated in cross-border insolvencies under the common law principle of “comity.” In the late nineteenth-century, The United States Supreme Court defined comity as:

the recognition which one nation allows within its territory to the legislative, executive or judicial acts of another nation, having due regard both to international duty and convenience, and to the rights of its own citizens or of other persons who are under the protection of its laws.

Thus, comity is the recognition one country allows the laws of another within its territory. To determine whether to allow such recognition, a country must consider the interest of its own citizens against international custom, and convenience. In general, under comity a U.S. court would defer jurisdiction to a foreign insolvency proceeding provided “the foreign court had jurisdiction and enforcement [did] not prejudice the right of United States citizens or violate domestic policy.” However, U.S. courts would refuse comity to a foreign proceeding if the foreign court did not follow “fundamental standards of procedural fairness.”

III. THE TREATMENT OF TAX CLAIMS IN BANKRUPTCY UNDER U.S. LAW

A wealth of scholarship has focused on the question of which “system of priorities” should control in the administration of unsecured claims in cross-border insolvencies. In
contrast, this Article focuses on the treatment of tax liens granted security status under U.S. law. To illustrate the nuances of such claims, this Article uses the example of a lien arising from the nonpayment of pension contributions that is perfected and ultimately treated as a secured tax claim in a U.S. bankruptcy.

A. THE EMPLOYEE RETIREMENT INCOME SECURITY ACT (ERISA)

Under U.S. law, the administration of certain private employee-retirement benefit plans is governed by federal and state law, as well as the Internal Revenue Code (I.R.C.). To explain why the treatment of tax claims in a cross-border bankruptcy could put certain U.S. retiree benefits at risk, requires a brief overview of the applicable federal statute and its interaction with the U.S. tax code.

In 1974, The U.S. legislature enacted the Employee Retirement Income Security Act (ERISA). "ERISA protects employee pensions and other benefits by providing insurance[,] ... specifying certain plan characteristics in detail[,] ... and by setting forth certain general fiduciary duties applicable to the management of both pension and nonpension benefit plans." The provisions of ERISA are divided into four titles. Title I contains the statute to regulate private employee pension and benefit plans, and sets forth a mechanism for the Department of Labor and employee-beneficiaries to enforce their rights under such plans. Title II amends the I.R.C. to establish the standards a defined benefit plan must satisfy for the employer qualify for certain tax advantages. Title III coordinates the interaction of the Internal Revenue Service, the Department of Labor, the Pension Benefit Guarantee Corporation (PBGC), and other federal agencies. Title IV of ERISA addresses the powers, responsibilities, and operations of the PBGC. In general, the PBGC guarantees the payment of benefits “under terminated defined

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116 See infra notes 133-150 and accompanying text.
119 ERISA § 502 grants federal courts exclusive jurisdiction over actions brought by a participant, beneficiary, fiduciary, or the Secretary of Labor; however, certain civil suits, remain under the jurisdiction of state courts. See ERISA §502(a)(1)(B), 29 U.S.C. § 1132(a)(1)(B). Today, the enforcement of employee rights under private benefit plans is almost exclusively, a matter of federal law. ERISA § 514(a), 29 U.S.C. § 1144(a).
120 See note 89 supra.
121 See supra notes 133-150 and accompanying text.
122 See SP1-Monograph1 Collier Employee Benefits in Corporate Bankruptcy Section 7, [1] Title IV of ERISA and Defined Benefit Pension Plans, (2011). Title IV of ERISA only applies to “defined benefit pension plans.” “PBGC pays for monthly retirement benefits, up to a guaranteed maximum, for 801,000 retirees in 4,200 single-employer and multiemployer pension plans that cannot pay promised benefits. Including those who have not yet retired and participants in multiemployer plans receiving financial assistance, PBGC is responsible for the current and future
benefit pension plans.”123 A defined benefit pension plan provides its beneficiaries a formula-based pension benefit that is determined by the benefits available at retirement.124

Under U.S. law, private employers are not required to offer their employees any retirement benefits.125 However, any employer provided defined benefit pension plan must comply with all the applicable requirements of ERISA and the I.R.C.126 The overlap between ERISA and the I.R.C. is significant.127 And it is most prevalent in the rules governing the vesting and funding of plans.128 The vesting requirement ensures that beneficiaries are covered through their retirement.129 While, the funding requirement ensures that the actual funds will be available to pay the retirees their benefits.130 As mentioned above, most defined pension benefits are guaranteed by PBGC.131 In general the maximum benefit guaranteed by a pension plan is preset; however, if a plan terminates due to an employer’s bankruptcy then the

In the case of a single employer with a defined benefit plan, ERISA funding standard requires current funding for the benefits accrued each year.132 While the I.R.S. may grant a waiver to employers that fail to meet the funding standard for a given year, such employers must contribute the funding shortfall within five years.133 But, if an employer fails to pay its minimum contributions to a defined benefit plan, and the employer’s total missed payments exceeds $1 million to any single plan, a tax lien in favor of the PBGC automatically arises ‘against the property of the employer and all of its controlled group members for the unpaid amounts.”134 The lien will be for the total unpaid balance plus interest.135 And the lien period commences on the day the payment is due and continues until the total amount owed by the employer is less than one million.136 The PBGC may perfect such a lien by filing notice under the same procedure for a tax lien, which is discussed in greater detail below.137 If a PBGC lien arises and is perfected before bankruptcy, the PBGC lien will be treated as a secured claim against the debtor. In the


123 Id.
124 Id.
126 See supra notes 119-124 and accompanying text.
127 Id.
128 See ERISA §§ 203 through 206, and §§ 301 through 305.
129 See ERISA §§ 203 through 206.
130 See ERISA §§ 301 through 305.
131 See note 95 supra.
132 I.R.C. § 430 (a)(1)(A); ERISA § 303 (a)(1)(A). Unless otherwise provided, all sections of the United States Internal Revenue Code referred to in this Article are to the 1986 Code.
133 I.R.C. § 430 (a)(1)(B), (c); ERISA § 303 (c).
case of a multinational, the protection of the automatic stay will not apply to entities, including foreign subsidiaries that are not included in the bankruptcy filing.\textsuperscript{138}

For example, if a defined pension benefit plan is maintained by a plan sponsor,\textsuperscript{139} and the plan sponsor is a member of a controlled group,\textsuperscript{140} all of the members of the group are held joint and severally liable for the unpaid contributions to the pension plan.\textsuperscript{141} Additional rules apply to plans connected to multiple employers,\textsuperscript{142} and plans with substantial funding shortfalls, but are not addressed by this Article.\textsuperscript{143}

Underfunded defined benefit plans can be a significant factor in encouraging a corporate debtor to seek Chapter 11 bankruptcy relief.\textsuperscript{144} Thus, the PBGC has the authority to initiate an inquiry into any corporation with a defined benefit plan that has significant underfunded pension liabilities. Under the Early Warning Program,\textsuperscript{145} the PBGC may initiate an inquiry if: (1) a company’s bond rating is below investment grade and the current liabilities on its sponsored pension plan exceed $25 million; or (2) a company, regardless of its bond rating, sponsors a pension plan with current liabilities exceeding $25 million and the plan’s current unfunded liabilities exceed $5 million.\textsuperscript{146} Once the PBGC initiates an inquiry, it may negotiate with a corporation to protect the pension plan prior to a bankruptcy filing and reorganization, or when necessary, terminate the plan. If the PBGC terminates an underfunded plan and the employer fails to provide the PBGC the underfunding liability upon demand, a lien will arise in favor of the PBGC against the employer.\textsuperscript{147} If the PBGC perfects such a lien,\textsuperscript{148} and the employer subsequently files for bankruptcy, a U.S. bankruptcy court would treat the PBGC claim as a secured tax claim against the property of the employer-debtor.\textsuperscript{149} But, if the PBGC fails to perfect a lien prior to an employer-debtor filing for bankruptcy, such lien will be treated as an unsecured priority tax claim.\textsuperscript{150}

\textsuperscript{138} I.R.C. § 412 (b)(2); ERISA §§ 302 (b)(2), 4062 (a), 4007 (e)(2), 29 U.S.C. §§ 1082 (b)(2), 1362(a), 1307 (e)(2).
\textsuperscript{139} See supra note xxx, PBGC Fact Sheet.
\textsuperscript{140} I.R.C. § 1563 (a).
\textsuperscript{141} ERISA follows the definition of a “controlled group” provided by I.R.C. § 4001 (a)(14). Section 4001 (a)(14) refers to §§ I.R.C. 414 (b)(c), which in turn refers to I.R.C. § 1563 (a).
\textsuperscript{142} I.R.C. § 430 (a)(1)(C), (e); ERISA § 303 (e).
\textsuperscript{143} The single-employer program of the PBGC protects approximately 33.8 million employees and retirees in over 26,000 pension plans. The multi-employer program covers approximately $10.4 million workers and retirees in over 1,400 pension plans. In general, multiemployer plans are established via collective bargaining agreements connected to more than one unrelated employer in a given industry, e.g., United Auto Workers (U.A.W.) See PBGC Corporation Fact Sheet, note 125 supra.
\textsuperscript{144} See supra note 95.
\textsuperscript{145} PBGC Technical Update 00-3: PBGC’s Early Warning Program (July 24, 2000), available at: http://www.pbgc.gov/res/other-guidance/tu/tu00-3.html. Updated on January 4, 2008 to provide current contact information, last visited October 10, 2011.
\textsuperscript{146} Id.
\textsuperscript{147} ERISA § 4068, 29 U.S.C. § 1368.
\textsuperscript{148} See infra notes 155-172 and accompanying text.
\textsuperscript{149} Id.
\textsuperscript{150} See 11 U.S.C. §507 (a)(8).
Because the question of whether a tax lien or a PBGC lien is treated as a secured or priority unsecured claim in a bankruptcy relies upon the attachment and perfection of a lien, a brief discussion of the mechanics is warranted.

**B. THE TREATMENT OF TAX CLAIMS IN A U.S. BANKRUPTCY**

Under the U.S. Bankruptcy Code, an unsecured tax claim of a “governmental unit” is treated as an eighth priority claim.\(^{151}\) For the purposes of the U.S. Bankruptcy Code, the definition of a governmental unit includes foreign states, and foreign governments.\(^{152}\) Therefore, the Bankruptcy Code not only allows the payment of foreign tax claims,\(^{153}\) when applicable, it treats such claims as priority unsecured claims.\(^{154}\)

Once the Internal Revenue Service (I.R.S.) completes an assessment of taxes and issues a demand for payment to a taxpayer, and the taxpayer fails to pay the assessed taxes, a federal tax lien arises and attaches to all of the taxpayer’s property, real and personal.\(^{155}\) In terms of timing, a federal tax lien arises at the time of assessment.\(^{156}\) But, such liens are not valid against "any purchaser, holder of a security interest, mechanics' lienor, or judgment lien creditor until notice thereof ... has been filed."\(^{157}\) Thus, unless a tax lien is properly filed before a debtor files for bankruptcy,\(^{158}\) it may be avoided by a U.S. bankruptcy court or trustee\(^ {159}\); because, an unfiled federal tax lien will not prevail over the claim of a hypothetical bona fide purchaser for value.\(^ {160}\) And for avoidance purposes, a U.S. bankruptcy trustee is deemed a hypothetical bona fide purchaser for value.\(^ {161}\) Under U.S. law, whether a tax lien is properly filed, *i.e.*, perfected is a

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\(^{151}\) See id. Other unsecured priority claims include: administrative expenses, limited employee wage claims, and contributions to employee benefit plans. See 11 U.S.C. § 507 (a) (1-7), (9), and (10).


\(^{153}\) See supra notes 122-125 and accompanying text.

\(^{154}\) Id.

\(^{155}\) See I.R.C. § 6321; see Treas. Reg. § 301.6321-1 Lien for taxes: For purposes of subsection 6321...the term "any tax" shall include a State individual income tax which is a "qualified tax", as defined in paragraph (b) of § 301.6361-4. The lien attaches to all property and rights to property belonging to such person at any time during the period of the lien, including any property or rights to property acquired by such person after the lien arises. For the purpose of U.S. taxes, the definition of a “person” includes “an individual, a trust, estate, partnership, association, company or corporation.” See I.R.C. § 7701(a)(1). See In re Wesley, 455 B.R. 383, 385 (Bankr. D.N.J. 2011).


\(^{157}\) See I.R.C. § 6323 (a). Properly filed federal tax lien prevails. See Spicer v. United States (In re Motions Marketing Solutions, Inc.), 403 B.R. 403 (Bankr. N.D. Tex. 2009) (holding that the term “fixing” includes perfecting a tax lien). I.R.C. § 6323 (h)(5) defines the term “tax lien filing” as “the filing of notice (referred to in subsection (a)) of the lien imposed by section 6321.” I.R.C. § 6323 (h)(6) defines a “purchaser” as: “a person who, for adequate and full consideration in money or money's worth, acquires an interest (other than a lien or security interest) in property which is valid under local law against subsequent purchasers without actual notice.”


\(^{159}\) See I.R.C. §6323 (a). The trustee is not granted the status of a purchaser.

\(^{160}\) See 11 U.S.C. § 545 (2).

\(^{161}\) See 11 U.S.C. § 544, 545, 546, 547.
question of state law.\textsuperscript{162} Thus, to illustrate the mechanics of the attachment and perfection of a tax lien, this Article looks to New York law.

In the state of New York, Article 62 of the New York’s Civil Practice Law & Rules governs the attachments of liens.\textsuperscript{163} The purpose of New York’s nonresident attachment statute is two-fold: (1) obtain jurisdiction over nondomiciliaries residing outside of the state, and (2) secure judgments against nondomiciliaries residing outside of the state.\textsuperscript{164} On its own, an order of attachment does not award a creditor any additional rights or priority status.\textsuperscript{165} To do so, "an attaching creditor must deliver the order of attachment to the sheriff to obtain priority in specific property or a debt."\textsuperscript{166} If, the order of attachment is delivered to the sheriff before "levy,” the attaching creditor’s rights will usually be superior to that of a subsequent transferee.\textsuperscript{167} The

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\textsuperscript{162} See I.R.C. § 6323 (f). § 6323 (f) provides in part:
\begin{enumerate}
\item[(f)] Place for filing notice; form.
\begin{enumerate}
\item[(1)] Place for filing. The notice referred to in subsection (a) shall be filed--
\begin{enumerate}
\item[(A)] Under state laws.
\begin{enumerate}
\item[(i)] Real property. In the case of real property, in one office within the State (or the county, or other governmental subdivision), as designated by the laws of such State, in which the property subject to the lien is situated; and
\item[(ii)] Personal property. In the case of personal property, whether tangible or intangible, in one office within the State (or the county, or other governmental subdivision), as designated by the laws of such State, in which the property subject to the lien is situated, except that State law merely conforming to or reenacting Federal law establishing a national filing system does not constitute a second office for filing as designated by the laws of such State; or
\end{enumerate}
\item[(B)] With clerk of district court. In the office of the clerk of the United States district court for the judicial district in which the property subject to the lien is situated, whenever the State has not by law designated one office which meets the requirements of subparagraph (A); or
\item[(C)] With recorder of deeds of the District of Columbia. In the office of the Recorder of Deeds of the District of Columbia, if the property subject to the lien is situated in the District of Columbia.
\end{enumerate}
\item[(2)] Situs of property subject to lien. For purposes of paragraphs (1) and (4), property shall be deemed to be situated--
\begin{enumerate}
\item[(A)] Real property. In the case of real property, at its physical location; or
\item[(B)] Personal property. In the case of personal property, whether tangible or intangible, at the residence of the taxpayer at the time the notice of lien is filed.
\end{enumerate}
\end{enumerate}
\end{enumerate}
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\textsuperscript{164} See Int’l Banking Corp, note _ supra at 621 (citing) (ITC Entm’t, Ltd. v. Nelson Film Partners, 714 F.2d 217, 220 (2d Cir. 1983)).
\textsuperscript{165} Id.
\textsuperscript{167} See N.Y. C.P.L.R. 6203. Section 6203 provides:
Where a plaintiff has delivered an order of attachment to a sheriff, the plaintiff's rights in a debt owed to the defendant or in an interest of the defendant in personal property against which debt or property a judgment may be enforced, are superior to the extent of the amount of the attachment to the rights of any transferee of the debt or property, except:1. a transferee who acquired the debt or property before it was levied upon for fair consideration or
\end{flushright}

\textsuperscript{18}
sheriff levies by serving the order of attachment to the garnishee or party in possession of the property.\textsuperscript{168} At that point, only a transferee without knowledge of the levy could take priority over the attaching creditor.\textsuperscript{169} Once a sheriff seizes, \textit{i.e.}, takes possession, of attached property, the lien is perfected against all transferees.\textsuperscript{170} If the levy is upheld via the issuance of a judgment of execution in favor of the attaching creditor, the sheriff can treat the attached property as though the levy arose from the execution rather than the attachment.\textsuperscript{171} But, if a court finds in favor of the debtor, the order of attachment will be vacated.\textsuperscript{172}

To review, a U.S. court must consider the applicable provisions of the U.S. Bankruptcy Code, I.R.C., and state law to administer tax claims in cross-border insolvencies. In addition, a U.S. court must comply with the provisions of an active tax treaty. The following discussion sets forth the application of tax treaties in the context of cross-border insolvencies.

\section*{IV. TAX TREATIES}

There is not a ‘World Tax Organization’\textsuperscript{173} to regulate international taxation. Rather, it is a network of bilateral tax treaties that serves as the world’s “international tax regime”\textsuperscript{174} and primary mechanism to avoid the double-taxation of taxpayers.\textsuperscript{175} Today, the majority of active tax treaties follow the model created by the Organization for Economic Co-Operation and Development (OECD Model Treaty).\textsuperscript{176} The United States Treasury Department has also created a model tax treaty.\textsuperscript{177} The U.S. Model Treaty adopts many of the provisions of the OECD Model;
however there are some key distinctions between the two that are discussed in greater detail below. As a result, many U.S. tax treaties share a common framework and contain similar provisions. However, each U.S. tax treaty is the result of direct negotiations and can take decades to implement.\textsuperscript{178} A common reason for the lengthy process is the reconciliation of the treaty partners’ tax laws and policies with the provisions of the treaty.\textsuperscript{179}

Today, the United States is party to five bilateral tax treaties that incorporate provisions for assistance in the collection of taxes.\textsuperscript{180} In addition, bilateral tax treaties between the United States and seventeen other countries provide mutual assistance for the collection of taxes via limitation of benefits (LOB) clauses.\textsuperscript{181} LOB clauses require both Contracting States to ensure

\textsuperscript{178}For example, income tax treaty negotiations started with Brazil the week of November 13, 1990. An unresolved sticking point between the U.S. and Brazil is the latter’s demand for a “tax sparing provision.” The definition of a tax sparing provision can be illustrated by the following example. XYZ Co. a U.S. Corporation establishes XYZ Brazil. Brazil collects a fee from XYZ Brazil that is unrelated to domestic tax debt. XYZ Brazil subsequently includes the fee in its calculation for a foreign tax credit on its U.S. federal income tax liability. Essentially, Brazil benefits at the expense of the U.S. tax base. In regards to tax sparing provisions, the United States Treasury refuses to entertain such provisions in a tax treaty and will cease negotiations with a state that insists on such provisions. On March 17, 2011, Senator Richard Luger (R- Ind.) introduced a resolution to encourage President Obama to negotiate a tax treaty with Brazil (S. Res. 108) (2011), full text of resolution available at: http://thomas.loc.gov/cgi-bin/query/z?c112:sr108 (last visited November 15, 2011).

\textsuperscript{179}In a bilateral tax treaty, either state cannot impose a duty on the other without expecting the same duty in return.

\textsuperscript{180}The five countries and the relevant treaties and provisions are:

- **NETHERLANDS — U.S.A. INCOME TAX TREATY (1992)**, (as amended by 2004 Protocol), Effective: January 1994, Article 30 - Exchange of information and administrative assistance; and

\textsuperscript{181}The sixteen countries and the relevant treaties and provisions are:

- **BELGIUM–U.S.A. INCOME TAX TREATY**, Effective: January 2008, Article 26 – Assistance in Collection;
- **ESTONIA–U.S.A. INCOME TAX TREATY (1998)**, Effective: January 2000, Article 26 - Exchange of information and administrative assistance;
- **GREECE — U.S.A. INCOME TAX TREATY (1950)**, Effective: January 1953, Article XIX;
- **INDONESIA–U.S.A. INCOME TAX TREATY (1980)**, Effective: January 1990, Article 29, Assistance in Collection;
- **LATVIA–U.S.A. INCOME TAX TREATY (1998)**, Effective: January 2000, Article 27 - Exchange of information and administrative assistance;
- **LITHUANIA — U.S.A. INCOME TAX TREATY (1998)**, Effective: January 2000, Article 27 - Exchange of information and administrative assistance;
- **SOUTH AFRICA — U.S.A. INCOME TAX TREATY (1997)**, Effective: January 1998, Article 26 - Exchange of information and administrative assistance; and
that the preferential tax rates pursuant to a bilateral income tax treaty are only enjoyed by its citizens. For example, the treaty between the United States and Belgium provides:

Each of the Contracting States shall endeavor to collect on behalf of the other Contracting State such taxes imposed by that other Contracting State as will ensure that any exemption or reduced rate of tax granted under this Convention by that other Contracting State shall not be enjoyed by persons not entitled to such benefits. 182

The primary purpose of LOB provisions is to avoid “treaty shopping.” The compliance and enforcement issues implicated by “treaty shopping” are beyond the scope of this Article. For the purposes of this Article, these treaties evidence that the U.S. and foreign governments are well aware that mutual co-operation is important and necessary to enforce tax law in a cross-border context.

All five of the U.S. treaties that provide mutual assistance in the collection of taxes, limit such assistance to taxes owed by the “citizens” of the Requesting State. 183 For example, pursuant to the Canada – U.S. tax treaty, Canada will only assist the U.S. in the collection of U.S. taxes owed by a U.S. taxpayer, and vice versa. Furthermore, the Requesting State must certify that the tax debt “has been finally determined.” 184 If Canada accepts such a claim, the claim “shall not have…any priority accorded to the revenue claims of the [U.S.].” 185 Thus, tax claims treated as secured or priority claims under U.S. law would not be awarded such status by Canada.

Because this Article recommends amendments to U.S. tax-treaty provisions, a comparison of the alternative models available should prove beneficial.

In 1998, the OECD published a report titled, Harmful Tax Competition: An Emerging Global Issue. 186 The report recommends that countries “review the current rules applying to the enforcement of tax claims of other countries and that the Committee on Fiscal Affairs pursue its work in this area with a view to drafting provisions that could be included in tax conventions for that purpose.” 187 As a result, in 2003 the OECD added a new Article 27 to its Model Tax Convention that provides a mechanism for countries to bilaterally agree to extend assistance in the collection of taxes. 188

Under Article 27, the Contracting States provide mutual assistance in the collection of “revenue claims.” 189 Article 27 defines a “revenue claim” as “any amount owed in respect of all taxes that are imposed on behalf of the Contracting States, or of their political subdivisions or

183 See supra note 180, Canada, Article 26, ¶ 8; Denmark, Article 27, ¶ 8; France, Article 28, ¶ 5; Netherlands, Article 31, ¶ 4; Sweden Article 27, ¶ 4.
184 Id. Canada, Article 26, ¶ 3.
185 Id. Canada, Article 26, ¶ 7.
187 See id.
189 Id.
local authorities, but only insofar as the imposition of such taxes is not contrary to the Convention or other instrument in force between the Contracting States.” But, Article 27 requires that a revenue claim satisfies two prerequisites before a Requested State will assist in its collection. Such claims must:

1. be enforceable under the laws of the Requesting State, and
2. be owed by a person who, at that time, cannot, under the laws of the Requesting State, prevent its collection.

The OECD commentary provides the following example of when these standards are met: “the Requesting State has the right, under its internal law, to collect the revenue claim and the person owing the amount has no administrative or judicial rights to prevent such collection.” Unlike the United States, the laws of many countries allow the collection of a tax claim, regardless of whether the tax debtor retains a legal right to challenge the amount or validity of the tax claim at the time of execution. But under Article 27, regardless of how a Requesting State handles appealable tax claims, a Requested State can only provide assistance on non-appealable tax claims.

Under the default provisions of Article 27, Contracting States agree to provide comprehensive assistance in tax collection, i.e., any and all taxes owed by residents and non-residents alike. However, States are free to limit the assistance available under an in-force bilateral treaty to only certain taxes, for example, direct taxes owed by residents. The likelihood that a state will enter such an agreement is based on “whether their protection of fundamental taxpayers’ rights is similar,” e.g., timely and sufficient notice of tax claims, rights to appeal a tax assessment and confidentiality, a right to counsel and the right to a fair trial.

The OECD Model Convention also requires that any “claims subject to assistance in collection shall not benefit from any priority” granted to tax claims under the laws of the Requesting State. The reason for this limitation is to avoid “competition between the priorities of the taxes of the two states or the complication of devising special rules for such occasions.”

Another legal mechanism that provides a framework to extend trans-border cooperation in the collection of taxes is the joint 1988 Council of Europe and OECD Convention on Mutual Administrative Assistance in Tax Matters (COE/OECD Convention). As of

191 See id. at 412-414.
192 See id at 413.
193 Id.
194 Id.
195 Id.
196 Id. at (47).
197 See supra note 190 at 413 [15].
198 See supra note 190 at (48).
199 See Convention on Mutual Administrative Assistance in Tax Matters, Press release, available at:
December 16, 2011, twenty-one nations have signed the COE/OECD Convention and its amended protocol. 200 Articles 11 through 16 of the Convention set forth the rules and guidelines for Contracting States to provide mutual assistance in the collection of taxes. 201 In terms of scope, the collection assistance permissible under the COE/OECD Convention and Article 27 of the OECD Convention are almost identical. Another characteristic of Article 27 shared by the COE/OECD convention is that it also does not allow a Requested State to recognize the priority status granted a tax claim in the Requesting State. 202 However, the COE/OECD convention goes one step further, in that a Requested State may not award a tax claim any priority treatment, “even if the recovery procedure used is the one applicable to its own tax claims.” 203 The United States signed the COE/OECD Convention in 1989. 204 However, the U.S. is the only signatory to reserve, i.e., elected not to enforce Articles 11 through 16. 205

To illuminate the intended goals of tax treaties from a U.S. perspective, this section describes their origin. Specifically, the ‘evolution’ of bilateral tax treaties negotiated between the United States and other nations after World War I.

In August of 1920, the attendees of an International Finance Conference held in Brussels recommended that the League of Nations address the issue of double taxation. 206 In February of 1925, The Financial Committee of the League of Nations (Finance Committee) instructed the Committee on Double Taxation and Tax Evasion (Committee) to prepare draft conventions to ensure the avoidance of double taxation and prevent tax evasion. 207 Two years later, the
The Committee presented its final report to the Finance Committee.\footnote{208} For expedience, the Committee split the issues of double taxation and tax evasion and then drafted two separate model conventions to address each issue, for a total of four.\footnote{209} Thus, in spite of the relatively ‘simple’ nature of international tax issues at that time,\footnote{210} the Committee found it a challenge to appropriately address the subject matter with just one or even two instruments.\footnote{211} The fourth convention drafted by the Committee, Assistance in the Collection of Taxes provides a mechanism for two States to enter an agreement to provide mutual assistance in the collection of taxes.\footnote{212}

After prolonged negotiations, the Committee agreed to design all four conventions as bilateral\footnote{213}, rather than multilateral agreements.\footnote{214} On the subject of double taxation, the Committee believed it would be difficult, if not impossible to obtain unanimity on a multilateral agreement.\footnote{215} But, in terms of the convention to address tax evasion, the Committee believed a multilateral, \textit{i.e.}, a single convention, was possible. However, the Committee believed such a convention would require prolonged and delicate negotiation.\footnote{216} And rather than delay Contracting States from enacting bilateral conventions that “would immediately satisfy the legitimate interests of the tax-payers as well as those of the Contracting States,”\footnote{217} the Committee promulgated the models as bilateral conventions.

First and foremost, the fourth draft requires the ‘Contracting States’ to specify the taxes that are to be included under the Convention.\footnote{218} Once the Convention is in force, assistance usually only applies to tax liabilities that are \textit{res judicata}.\footnote{219} Essentially, the Committee defines

\footnote{208} See Reports Presented by the Comm. of Technical Experts on Double Taxation and Tax Evasion, League of Nations Doc. C.216M.85 1927 II, at 23 (1927) [hereinafter 1927 Report], available at http://www.law.wayne.edu/tad/Documents/League/League_Tech_Experts.pdf (last visited December 11, 2011).\footnote{209} The 1927 Committee report includes the following model conventions: (1) Bilateral Convention for the Prevention of Double Taxation, (2) the Bilateral Convention for the Prevention of Double Taxation in the Matter of Succession Duties, (3) the Bilateral Convention on Administrative Assistance in Matters of Taxation, and (4) the Bilateral Convention on Judicial Assistance in the Collection of Taxes. \textit{Id.} at 10-30.\footnote{210} The four model conventions represent the collective work of several of the League of Nations’ committees from 1920 through 1928. \textit{1927 Report supra} note 4, \textsc{Introduction}.\footnote{211} See note 7 supra.\footnote{212} \textit{Id.} at 26.\footnote{213} \textit{Id.} at 8, 10-30.\footnote{214} The U.S. representative passionately advocated for mutual rather than bilateral agreements specifically to avoid the current state of affairs- States have little if any motivation to enter multilateral agreements when they already have bilateral agreements in force with the States they are most concerned about entering into such agreements with.\footnote{215} \textit{Id.} at 8.\footnote{216} \textit{Id.}\footnote{217} \textit{Id.}\footnote{218} \textit{Id.} at 26, Article 1.\footnote{219} \textit{Id.} at Articles 3,¶ 5. A legal dictionary defines \textit{res judicata} as: [t]he principle that an existing final judgment rendered upon the merits, without fraud or collusion, by a court of competent jurisdiction, is conclusive of rights, questions, and facts in issue, as to the parties and their privies, in all other actions in the same or any other judicial tribunal of concurrent jurisdiction. \textit{See} Ballentine’s Law Dictionary, (2010 LexisNexis). Therefore, under the fourth draft convention, a Requesting State had to guarantee its treaty partner that the tax liability was final under local law.
a *res judicata* liability as one that is not subject to appeal.\textsuperscript{220} However, if a tax liability is open to appeal a creditor State may still seek assistance from the Requested State in the form of taking “conservancy measures…mutatis mutandis.”\textsuperscript{221} The Committee conceded that the *res judicata* prerequisite could unintentionally facilitate a debtor’s efforts to evade taxes.\textsuperscript{222}

Article 9 of the fourth convention specifies that the tax liability must be “collected in accordance of the laws of the State to which the application is made.”\textsuperscript{223} However, this requirement does not “oblige” a Requested State to “employ a means of execution” unavailable under the laws of a Requestor State.\textsuperscript{224} For example, State X and State Y agree to provide mutual assistance in the collection of taxes under the fourth model convention. State X requests the assistance of State Y to collect taxes owed by Corporation Z. Under the convention, State Y would enforce the tax liability owed by Z Corporation under its laws rather than the laws of State X. However, if a certain mechanism or procedure for execution is available under Y’s laws, but unavailable under the laws of X, Y has no obligation to pursue the tax claim under such mechanism. This ‘limitation’ makes sense in terms of ease of administration and good public policy. The following hypothetical provided by the Committee in its commentary on Article 9 illustrates this point: “It would certainly offend public opinion if the State to which the application is made were to adopt methods of constraint alien to the laws of the creditor State. The people of Morania would say: ‘Why does Imeria imprison a fellow-country man of ours who, if he had remained in our territory, would merely have had his property seized?’”\textsuperscript{225} Further, why should X be permitted to enforce a tax claim extraterritorially under the aegis of Y through means its own legislature, for whatever reason, has not enacted?

In addition, Article 9 provides that a Requested State “may adopt a special form or procedure, even if not provided for by its laws”\textsuperscript{226} in order to assist a Requestor State, provided doing so would not conflict with the laws of the Requested State.\textsuperscript{227}

In light of these political ‘hazards,’ the Committee recommends, “no means of execution should be employed unless it is clear… the details must in all cases be governed by the laws of the State to which the application is made.”\textsuperscript{228} Thus, a Requested State would follow the same procedure and law it would apply to its own tax claims to execute a claim of the Requestor State. Thus, from a substantive perspective, debtors subject to the convention would arguably be no better or worse off.

In 1928, the Committee published the four draft conventions again with some changes.\textsuperscript{229} The first model convention, designed to address double taxation laid the groundwork for the current network of bilateral income tax treaties and TIEAs that support international taxation.\textsuperscript{230}

\textsuperscript{220} *Id.* The committee explains Article 3 through the following euphemism: It would hardly be desirable to invite a foreign administration to take measures to collect a debt which was still liable to be cancelled on appeal.”

\textsuperscript{221} *Id.* at 27, Article 11.

\textsuperscript{222} *Id.* at 30, Article 11 (explanation).

\textsuperscript{223} *Id.* at 27, Article 9.

\textsuperscript{224} *Id.*

\textsuperscript{225} *Id.* at 29.

\textsuperscript{226} *Id.* at 27.

\textsuperscript{227} *Id.*

\textsuperscript{228} *Id.* at 29-30.


\textsuperscript{230} See Dean *supra* note 173; Reuven Avi-Yonah, The Structure of International Taxation: A Proposal for Simplification, 74 TEX. L. REV. 1301 (1995-1996);
Of the four conventions drafted by the Committee in 1927, only the convention to prevent double taxation can be traced to a significant number of bilateral tax treaties that are currently in force.\textsuperscript{231} In fact, the foundation of the current OECD, United Nations, and the United States model tax treaties is the League of Nations bilateral tax treaty.\textsuperscript{232}

V. THE TREATMENT OF TAX CLAIMS IN CROSS-BORDER INSOLVENCIES UNDER THE LAWS OF THE UNITED STATES AND ITS TREATY PARTNERS

As discussed above, under the United States Bankruptcy Code, unsecured tax claims of “governmental units” receive an eighth priority.\textsuperscript{233} The insolvency laws of several countries, including Canada, the United Kingdom, and Mexico grant certain tax claims a preferential status.\textsuperscript{234} On the other hand, several countries do not award tax claims any preferential treatment.\textsuperscript{235} A comparison of how various insolvency laws treat tax claims is beyond the scope of this Article. Neither does this Article endeavor to address whether insolvency laws should grant priority status to cross-border claims, and if so which laws to apply. Rather, these distinctions are mentioned for the sole purpose of establishing the fact that the insolvency regimes of many countries grant tax claims preferential status.\textsuperscript{236}

Currently, the United States is party to five bilateral tax treaties that provide for the mutual assistance of collection of taxes.\textsuperscript{237} Because Canada is the largest trading partner of the United States\textsuperscript{238}, the tax treaty between Canada and the U.S. provides the best example to illustrate the treatment a U.S. secured tax claim would receive in the context of a cross-border insolvency, and vice versa. The original bilateral income-tax treaty between the United States and Canada entered into force on August 16, 1984.\textsuperscript{239} An amendment to the original treaty signed March 17, 1995 added Article XXVIA – Assistance in Collection.\textsuperscript{240} Article XXVIA provides that Canada and the United States mutually agree to assist one another in the collection of certain taxes.\textsuperscript{241}

\textsuperscript{231} See Dean supra note 173 at 642-643.
\textsuperscript{234} See Barbara K. Morgan, Should the Sovereign be Paid First? A Comparative International Analysis of the Priority for Tax Claims in Bankruptcy, 74 Am. Bankr. L.J. 461, 500 (2000); U.K. Insolvency Act, 1986, Ch. 45, § 175 (Eng.), (Section 386 and Schedule 6 to Section 386 then lists income tax as a preferential debt) Id. at § 386; France and Mexico also have broad tax priorities, with New Zealand and Canada offering limited priorities.
\textsuperscript{235} See id. at 480, 492, and 500.
\textsuperscript{236} See id.
\textsuperscript{237} See supra notes 180-185 and accompanying text.
\textsuperscript{238} See supra note 5.
\textsuperscript{239} See supra note 180.
\textsuperscript{240} Id.
\textsuperscript{241} The taxes included under the bilateral tax-treaty in-force between Canada and the United States include: (a) In the case of Canada, the taxes imposed by the Government of Canada under the Income Tax Act; and (b) In the case of the United States, the Federal income taxes imposed by the Internal Revenue Code of 1986. However, the Convention shall apply to: (i) The United States accumulated earnings tax and personal holding company tax, to the extent, and only to the extent, necessary to implement the provisions of paragraphs 5 and 8 of Article X (Dividends);
along “with interests, costs, additions to such taxes and civil penalties referred to…as a revenue
claim.” However, as discussed above, neither Canada nor the U.S. will consider the priority
status awarded a tax claim under the laws of the other. Moreover, from the U.S. perspective,
the tax treaty provides no relief at all if the tax-debtor is a Canadian citizen, and vice versa.
Thus, if a U.S. secured or priority tax claim is owed by a Canadian entity, the treaty provides no
relief whatsoever, and Canada would be in the same position if the situation were reversed.

The problem created by countries mutually agreeing to ignore the priority status they award
to tax claims becomes more acute in the context of cross-border insolvencies. Under Canadian
insolvency law, state and federal tax claims are treated as unsecured creditors. Thus, the eighth
priority granted unsecured tax claims under U.S. law is unavailable under the treaty as well as
under Canadian law in general. But, similar to U.S. bankruptcy law, under Canadian law
certain tax claims perfected pre-bankruptcy are treated as secured claims. Canadian law grants
priority status to amounts withheld from employees for income taxes, unemployment insurance,
and employee contributions to the Canadian Pension Plan, under a “deemed trust” theory.
Under Canadian law, “deemed trust” claims are granted a ‘super-priority’ status in that they are
paid before secured and unsecured creditors.

The following hypothetical serves to illustrate why the U.S. government should amend its
tax treaties that provide collection assistance to allow tax claims to retain secured or priority
status in the context of cross-border insolvencies. X, a U.S. multinational operates two factories.
One factory is in the U.S. and owned directly by X. X’s other factory is owned by its wholly
owned Canadian subsidiary, Y. X sponsors a defined employee benefit plan for its U.S.
employees that is subject to ERISA. Simultaneously, Y withholds its employees’ contributions to

(ii) The United States excise taxes imposed with respect to private foundations, to the extent, and only to the extent,
necessary to implement the provisions of paragraph 4 of Article XXI (Exempt Organizations);
(iii) The United States social security taxes, to the extent, and only to the extent, necessary to implement the
provisions of paragraph 2 of Article XXIV (Elimination of Double Taxation) and paragraph 4 of Article XXIX
(Miscellaneous Rules); and
(iv) The United States estate taxes imposed by the Internal Revenue Code of 1986, to the extent, and only to the extent,
necessary to implement the provisions of paragraph 3(g) of Article XXVI (Mutual Agreement Procedure)
and Article XXIX B (Taxes Imposed by Reason of Death). 3. The Convention shall apply also to:
(a) Any taxes identical or substantially similar to those taxes to which the Convention applies under paragraph 2;
and
(b) Taxes on capital;
(c) The term "Canadian tax" means the taxes referred to in Article II (Taxes Covered) that are imposed on income by
Canada;
(d) The term "United States tax" means the taxes referred to in Article II (Taxes Covered), other than in
subparagraph (b)(i) to (iv) of paragraph 2 thereof, that are imposed on income by the United States.”

See supra note 180.
See supra notes 180-185 and accompanying text.
See supra notes 151-154 and accompanying text.
See supra note 241 at 485 n. 152.
See supra at 485, n. 151.
See supra note 241 at 485 n. 152.
See supra note 242.
See supra note 245.
See supra note 244.
See supra note 247.
See supra note 248.
See supra note 249.
See supra note 243.
See id. The only exception to the priority granted “deemed trust” claims are pre-bankruptcy mortgages on real
property.
the Canada Pension Plan but fails to forward such funds to the Canadian government. One year ago, X transferred the bulk of its assets, a portfolio of patents and other intellectual property to Y. Over the past year, X failed to make any contributions to its employee plan, and the PBGC obtains a secured tax claim against X. X subsequently files for bankruptcy in the U.S. For a number of unrelated reasons, Y simultaneously files for bankruptcy protection in Canada. Under the current Canada – U.S. income tax treaty, even if the U.S. obtains Canada’s assistance to collect the secured and unsecured tax claims owed by X, such claims would probably only be satisfied once all of Y’s “deemed trust” and secured claims are paid. In the alternative, Canada would not be able to seek the assistance of the U.S. to collect any “deemed trust” claims owed by Y from X. Thus, in either case, retirees and other taxpayers will bear the burden through no fault of their own.

A. THE REVENUE RULE

The final legal component implicated by the solution proposed in this Article is the common law doctrine known as the revenue rule. In general, the revenue rule provides that the courts of one sovereign will not enforce the “revenue laws,” i.e., the tax claims of another sovereign. U.S. case law and several scholars attribute the ‘creation’ of the revenue rule to dictum from two mid-eighteenth century English decisions by Lord Mansfield, Holman v. Johnson, and Planche v. Fletcher. In both cases, the revenue rule protected British international trade interests. Because English common law is the foundation of the U.S. legal system, U.S. courts have had over two hundred years to consider the function of the revenue rule, and more importantly for the purposes of this Article, its scope. To identify the contemporary purpose and relevance of the revenue rule in the United States, a brief overview of the most recent interpretations of the revenue rule by U.S. courts should prove useful.

1. THE BEARINGPOINT DECISION

In 2010, Judge Gerber of the United States Bankruptcy Court for the Southern District of New York oversaw the chapter 11 cases of the reorganized Debtor, BearingPoint. During the pendency of the case, the Republic of Indonesia filed two tax claims for a combined total of approximately $4 million allegedly owed by BearingPoint’s Indonesian subsidiary, PT Barents

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251 See Her Majesty the Queen ex rel. B.C. v. Gilbertson, 597 F.2d 1161, 1164 (9th Cir. 1979).
256 See supra note 17.
Under Indonesian law, controlling shareholders are held liable for the unpaid tax liabilities of their Indonesian corporate subsidiaries. BearingPoint, the Debtor, held 99% of the stock of PT Barents Indonesia. Thus, BearingPoint qualified as the majority shareholder of PT Barents Indonesia under Indonesian law. The alleged tax liabilities included VAT and/or Sales Taxes, Income Tax, and interest. Rather than object to the Indonesian claims on their merit, the Trustee based his objection to the Indonesian tax claims on the revenue rule. And rather than consider the merits of the Indonesian claims, Judge Gerber disallowed the claims pursuant to the revenue rule. To provide Indonesia some “comfort” that his decision was not “arbitrary,” Judge Gerber volunteers to “discuss the law in greater detail than [he] otherwise might.” Judge Gerber explains that due to Second Circuit precedent, “the Revenue Rule is fully binding” on him, and moreover, the revenue rule “has been laid down by the Supreme Court of the United States.” But, rather than refer to the most recent Supreme Court decision on the revenue rule, Judge Gerber cites dictum from a 1964 decision by the Supreme Court. Furthermore, Judge Gerber makes no mention of the bilateral tax treaty in force Between the United States and Indonesia since 1980. This choice by Judge Gerber is curious, because the term “tax,” other than once in the dissent, appears nowhere in the Supreme Court opinion he cites. To show how the decision in BearingPoint crystallizes the problem this Article seeks to address, a brief overview of the most recent Supreme Court decision on the revenue rule and the related caselaw is necessary.

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258 See id. * 1.
259 See supra note 135 * 2-3.
260 See id.
261 See id.
262 See id. Based on the given facts, the taxes allegedly owed by BearingPoint’s Indonesian subsidiary are analogous to taxes assessed by the United States. Although the United States does not assess a VAT (Value Added Tax), a VAT is essentially a sales tax that is collected in stages rather than just from the final consumer. In the U.S., the majority of states collect some form of sales tax. See eg. Helping U.S. Companies Export, available at: http://export.gov/ (last visited December 20, 2011). Currently, the following states do not assess a sales tax: Alaska, Delaware, Hawaii, Montana, New Hampshire and Oregon. Learn About Your State and Local Tax Obligations available at: http://www.sba.gov/content/learn-about-your-state-and-local-tax-obligations (last visited December 20, 2011).
263 See supra note 253.
264 Id.
265 Id.
266 Id.
267 Id.
268 Id.
269 Id. * 2; The precedent Judge Gerber refers to is the Second Circuit decision in AG of Can. v. R.J. Reynolds Tobacco Holdings, Inc., 268 F.3d 103 (2d Cir. N.Y. 2001).
270 Id. * 3.
271 See supra note 135 *4 (citing Pasquantino v. United States, 544 U.S. 349 (U.S. 2005)).
273 See supra note 181. The Indonesia – U.S.A. Income Tax Treaty also provides for mutual assistance for the collection of taxes via an LOB provision. See supra notes 181-182 and accompanying text.
The United States Supreme Court granted certiorari in *Pasquantino v. United States* to resolve a conflict in the Courts of Appeals. Specifically, the Courts of Appeals differed on whether the revenue rule precluded a prosecution under the U.S. wire fraud statute when the defendants conspired “to defraud a foreign government of tax revenue.” In *Pasquantino*, the defendants smuggled large quantities of alcohol into Canada without paying the applicable Canadian excise taxes. The Supreme Court agreed with the Second Circuit Court of Appeals’ decision in *United States v. Trapilo*, and held that the revenue rule did not preclude prosecution under the wire fraud statute, when the defendants plotted to defraud a foreign government of tax revenue. The Supreme Court found that even in “its earliest days the revenue rule never proscribed all enforcement of foreign revenue law.” Moreover, “[t]he line the revenue rule draws between impermissible and permissible ‘enforcement’ has therefore always been unclear.” But, the Supreme Court explicitly reserved its position on “whether a foreign government, based on wire or mail fraud predicate offenses, may bring a civil action under [RICO] for a scheme to defraud it of taxes.”

In *United States v. Trapilo*, the Second Circuit held that a wire fraud prosecution could proceed regardless of the fact that the Canadian government was the ‘victim’ of the scheme. The Court explains “at the heart of [the] indictment is the misuse of the wires in furtherance of a scheme to defraud the Canadian government of tax revenue, not the validity of a foreign sovereign’s revenue laws.” And perhaps to avoid any possible misinterpretation of its holding, the Court explicitly stipulates “the common law revenue rule is not properly implicated” (emphasis added) by the case. However, the question of whether the revenue rule precluded the prosecution of U.S. defendants for the violation of a U.S. criminal statute proved not to be a foreclosed matter in the Second Circuit.

Eight years after *Trapilo*, the Second Circuit affirmed a district court decision to dismiss three related suits in *European Community v. RJR Nabisco, Inc.* (EC 1). The foreign Plaintiffs in the three suits included the European Community (EC), several member countries of the EC.

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275 See supra note 2.
277 See *Pasquantino v. United States* supra note 17 at 354 (citing (United States v. Boots, 80 F.3d 580, 587 (CA1 1996) (holding that a scheme to defraud a foreign nation of tax revenue does not violate the wire fraud statute), and United States v. Trapilo, 130 F.3d 547, 552-553 (CA2 1997) (held that a scheme to defraud a foreign nation of tax revenue violates the wire fraud statute)).
278 See id. at 352.
279 See id.
280 See id.
281 See supra note 270 at 366.
282 See id. at 367.
283 See id. at 355.
284 See United States v. Trapilo, 130 F.3d 547, 550 (2d Cir. N.Y. 1997)
285 See id. (citing) (United States v. Defiore, 720 F.2d 757, 761-62 (2d Cir. 1983)).
286 See id. at 522-23.
287 See, European Cmty. v. RJR Nabisco, Inc., 355 F.3d 123, 127 (2d Cir. 2004).
individually, and several Columbian states. The Plaintiffs’ complaint alleged that the defendants, U.S. cigarette manufacturers, violated the Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. §§ 1961-1968 (RICO) by conspiring to smuggle cigarettes across their borders. In terms of harm, the Plaintiffs claimed the defendants’ actions caused pecuniary damages in the form of lost tax revenue and the burden of additional law enforcement costs. The district court found that the Plaintiffs’ claims arose from alleged violations of foreign tax laws and dismissed all three cases pursuant to the Revenue Rule and Second Circuit precedent. It is worth noting that all ten of the plaintiff member countries in the three suits are members of the OECD.

Because the Second Circuit affirmed the district court decision, the Plaintiffs filed a petition for a writ of certiorari with the United States Supreme Court. The Supreme Court granted certiorari, vacated the decision, and remanded EC 1 back to the Second Circuit, instructing the Court to reconsider the case in light of Pasquantino v. United States.

On remand, the Second Circuit upheld its decision in EC 1, because Pasquantino “[did] not substantively cast doubt on its previous conclusion (EC 2). The Court emphasizes that in Pasquantino, the Supreme Court explicitly declined to express its view as to “whether a foreign government, based on wire or mail fraud, may bring a civil action under [RICO] for a scheme to defraud it of taxes.” As a result, rather than consider the merits of the Plaintiffs’ claim, the Court looks to its earlier decision in Attorney General of Canada v. R.J. Reynolds Tobacco Holdings, Inc. (Canada) for guidance. In Canada, the Second Circuit considered whether to allow the Canadian government to recover tax revenue and additional enforcement costs related to smuggling under RICO. The Court responded in the negative, and held that because

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288 Besides the European Community itself, the plaintiffs-appellants include: the Kingdom of Belgium, Republic of Finland, French Republic, Hellenic Republic, Federal Republic of Germany, Italian Republic, Grand Duchy of Luxembourg, Kingdom of the Netherlands, Portuguese Republic, and Kingdom of Spain. The Colombian plaintiffs include the following Departments: Amazonas, Antioquia, Atlanticco, Bolivar, Caqueta, Casanare, Cesar, Choco, Cordoba, Cundinamarca, Huila, La Guajira, Magdalena, Meta, Narino, Norte De Santander, Putumayo, Quindio, Risaralda, Santander, Sucre, Tolima, Valle Del Cauca, Vaupes, and Santa Fe De Bogota, Capital District. See European Cmty. v. RJR Nabisco, Inc., 355 F.3d 123, 127 (2d Cir. 2004).
289 See id.
290 Id.
291 See supra note 17.
293 See supra note 18.
294 List of OECD Member countries - Ratification of the Convention on the OECD, available at: <http://www.oecd.org/document/58/0,3746,en_2649_201185_1889402_1_1_1_1,00.html> (last visited December 20, 2011).
296 See European Cmty. v. RJR Nabisco, 125 S. Ct. 1968 (2005).
297 See European Cmty. v. RJR Nabisco, 424 F.3d 175, 179 (2d Cir. 2005).
298 See id. (citing) (United States v. Pasquantino, 125 S. Ct. At 1771 n. 1.) (2005).
299 See id. (citing) (Attorney General of Canada v. R.J. Reynolds Tobacco Holdings, Inc., 268 F.3d 103 (2d Cir. 2001)).
300 See id. at 131-132.
recovery of Canada’s lost taxes “would constitute “direct enforcement””\textsuperscript{301} and recovery of additional law enforcement costs “would constitute “indirect enforcement””\textsuperscript{302} of a foreign sovereign’s tax laws, the revenue rule bared the prosecution of the defendants.\textsuperscript{303} The Second Circuit found the facts in \textit{EC I} and \textit{Canada} similar and upheld its decision to deny the Plaintiffs’ claims.\textsuperscript{304} To explain, the Court emphasizes that the intended purpose of the revenue rule is twofold:

first that policy complications and embarrassment may follow when one nation's courts analyze the validity of another nation's tax laws; and second, that the executive branch, not the judicial branch, should decide when our nation will aid others in enforcing their tax laws.\textsuperscript{305}

The Second Circuit found these two concerns indicate possible exceptions to the revenue rule. One exception is when the government consents to prosecution, \textit{i.e.}, the U.S. government is the plaintiff, \textit{e.g.}, \textit{Pasquantino}.\textsuperscript{306} In such cases, the likelihood that the judiciary will infringe upon the rights of the executive branch is minimal.\textsuperscript{307} But, when the Plaintiffs in a civil suit are foreign governments, rather than the United States government, a court has no such assurance.\textsuperscript{308} Thus, the Second Circuit concluded, “\textit{Pasquantino} casts no doubt on the reasoning or the result of \textit{EC I}.”\textsuperscript{309} In response, the Plaintiffs again requested certiorari; however, the United States Supreme Court refused to honor their request.\textsuperscript{310}

\section*{VI. PROPOSED SOLUTION TO RESOLVE THE TREATMENT OF TAX CLAIMS IN CROSS-BORDER INSOLVENCIES}

The insolvency laws of different countries can treat the same issue quite differently; however, there are some principles that are shared by the majority of the world’s insolvency regimes.\textsuperscript{311} One such example is the “Principle of Collectivity.”\textsuperscript{312} The Principle of Collectivity “[recognizes] that insolvency constitutes an example of the so-called ‘common pool problem’ which arises whenever conditions are such that more than one person has rights over the same

\begin{itemize}
\item \textsuperscript{300} See id.
\item \textsuperscript{301} See id.
\item \textsuperscript{302} See id.
\item \textsuperscript{303} See id.
\item \textsuperscript{304} See id.
\item \textsuperscript{305} See \textit{id. at} 131.
\item \textsuperscript{306} See \textit{id}.
\item \textsuperscript{307} See \textit{id}.
\item \textsuperscript{308} See \textit{ supra} note 290 at 181.
\item \textsuperscript{309} See \textit{id. at} 182.
\item \textsuperscript{310} See European Cmty. v. RJR Nabisco, Inc., 546 U.S. 1092 (U.S. 2006).
\item \textsuperscript{311} See \textit{ supra} Clark & Goldstein, note 29 at 515, n. 8.
\item \textsuperscript{312} See \textit{id. n} 9 (citing) (Ian F. Fletcher, Insolvency in Private International Law 8, para. 1.07 (James J. Fawcett ed., 2d. ed. 2005)).
\end{itemize}
finite fund of resources." If the insolvency laws of a country include a priority scheme for creditors’ claims, and a debtor only has assets in that country, the ‘common pool problem’ is less acute. But, in the context of cross-border insolvencies, the ‘common pool problem’ is usually exacerbated by local priority schemes. Because, even when the insolvency laws of two countries grant creditors the same priority status, the satisfaction of such claims are still limited to the “same finite fund of resources.” Today, the predominant doctrines that seek to address this “tension in the cross-border context” are universalism and territorialism.

Universality generally recommends that any and all claims asserted against a debtor in bankruptcy be administered for distribution through one proceeding in the debtor’s country of residence (a main proceeding). Therefore, the administration of a proceeding under territorialism would require the forum court to acquire jurisdiction over all of the assets held by a debtor worldwide. In contrast, territorialism provides no deference to a foreign proceeding. Moreover, under territorialism, “a bankruptcy proceeding under domestic law may be initiated against a foreign debtor and his domestically held assets without regards for concurrent insolvency proceedings or judgments of other countries.”

A comparison of universalism and territorialism or their various permutations is beyond the scope of this Article. Rather, they are discussed here because neither doctrine resolves the primary concern of this Article. In a global economy with competing creditors holding equally legitimate interests, what are the best practices governments should adopt to administer their mutual tax claims in a cross-border insolvencies? This Article seeks to answer this question from the perspective of the United States. And recommends measure the U.S. government could take to ensure its secured tax claims will be respected in cross-border insolvencies.

The sheer effort and “consensus-building” required to draft and then pass the Model Law “was formidable, and not likely to be repeated.” Therefore, any proposed solution for the treatment of assets subject to secured tax claims in cross-border insolvencies is more likely to be adopted, if such solution can “be done within the existing statutory schemes available to courts, creditors, and counsel.” Thus, the solutions proposed by this Article endeavor to operate within the framework of the Model Law, in-force bilateral tax treaties, and the OECD, and

313 See id. (para. 1.08 at 9).
314 See id.
315 See supra note 115.
317 Id.
318 See supra note 29 at 516, n. 13.
320 Id.
321 See Desai supra note 54, at 523.
COE/OECD conventions. It is irrelevant that every country does not follow the Model Law or provide mutual assistance in the collection of tax claims at this time. Because, a principled resolution of this issue can still provide much needed guidance and perhaps even encourage countries that do not follow the Model Law to adopt it or enact legislation that in substance will produce the same results.

The first recommendation this Article makes is to revoke the common law doctrine of the revenue rule. If complete revocation of the revenue rule proves unfeasible, then an explicit exclusion should be provided for secured pension based and other tax claims in the context of a cross-border insolvency. Other authors have expended significant energy parsing case law and the historical record to legitimize the continued relevance of the revenue rule. However, a common and critical flaw shared by such arguments is that they refuse to account for the significant changes in how the world interacts and conducts business today. Moreover, not even the progenitor of the revenue rule, the legal system of the United Kingdom, enforces the revenue rule as expansively as the Second Circuit does today. For example, the United Kingdom has agreed to enforce the mutual assistance in the collection of taxes provisions of the COE/OECD Convention. Simply put, the deference U.S. courts continue to award the revenue rule is clearly wrong because it upsets the legislative intent of diverse areas of law. For example, in BearingPoint Judge Gerber denied Indonesia’s tax claims for one reason, the revenue rule. But, the Bankruptcy Code clearly allows the tax claims of foreign governments. Query, what level of legitimacy should a foreign government grant the United States Bankruptcy Code in light of BearingPoint? More importantly, it is impossible to reconcile the asserted purpose of the revenue rule advanced by the Second Circuit and the implications of the BearingPoint decision.

The contemporary legitimacy of the revenue rule is further questioned by the United States Treasury Department technical explanation (Report) of the OECD/CE Convention. The Report “reflects the United States’ understanding of the meaning and application of [its]
Thus, the Report provides insight into the reason behind the U.S.’ position on Articles 11 through 16 of the Convention. The Report first establishes that at that time (June 1990), there were bilateral tax treaties with provisions for mutual assistance in tax collection in force between the U.S. and four other countries. And according to the Report, neither the I.R.S. nor its analog in the other four countries had “made any significant use of the collection assistance provisions” in the treaties. And for that sole reason, the U.S. Treasury Department reserved its position on Articles 11 through 16, the mutual assistance in the collection of taxes provisions, of the COE/OECD Convention. In conclusion, the Report emphasizes that the reservation can be re-evaluated or withdrawn at any time, and that such action may very well be required “after experience is gained under bilateral agreements, such as the four tax treaties mentioned above or under new provisions in new or revised bilateral tax treaties.” Furthermore, neither the Explanatory Report nor the Joint Committee report on the Convention makes any reference to or causal link between the U.S. reservation on Articles 11 through 16 and the revenue rule.

The second step of the solution proposed by this Article is for the U.S. to amend its existing network of bilateral tax treaties to allow the collection of secured and priority tax claims in a cross-border insolvency regardless of the citizenship status of the tax-debtor. Rather than create entirely new provisions, the U.S. can negotiate with its treaty partners to amend the treaties that are currently in force. One option is to incorporate Article 27 of the OECD Convention, and include provisions to allow secured tax claims to retain their status in cross-border insolvencies. Or, as an alternative, the United States could withdraw its reservation on Articles 11 through 16 of the COE/OECD Convention and negotiate with the other signatories to incorporate provisions that require nations to respect the secured status of tax claims in cross-border insolvencies.

An added benefit of the United States enacting the proposed changes to either the COE/OECD Convention or Article 27 of the OECD Model Convention is that the either plan of action would contemporaneously address the supposed function of the revenue rule. Because the enforcement of a treaty provision by a court is not a “judicial evaluation of the policy-laden enactments of other sovereigns,” nor does it infringe upon the “separation of powers” mandated by the United States Constitution.

The task of evaluating the tax laws of a foreign jurisdiction would not be imposed upon the United States judiciary by virtue of Article 27. Because only tax claims that meet the criteria

331 OECD/CE: 1988 Administrative Assistance Convention, Doc 93-31219, INTRODUCTION.
333 Id. The four countries include: Sweden (Article XVII), effective March 23, 1939; Netherlands (Article XXII), effective April 29, 1948; Denmark (Article XVIII), effective May 6, 1948; and France (Article 27), effective July 28, 1967.
334 Id.
335 Id.
336 Id.
337 See Pasquantino V. United States supra note 17, at 1779.
338 See European Cmty. v. RJR Nabisco supra note 296 at 180.
discussed above, and are mutually agreed upon by both States are eligible for such assistance. And since tax treaties are negotiated and entered into exclusively by the executive branch of the United States, Article 27 indirectly performs the other primary function of the revenue rule as well.

The clear disconnect between the interpretation of the revenue rule adopted by the Second Circuit and the contemporary Congressional view of cross-border co-operation is evident in the enactment of Chapter 15. The ‘expansive’ view Congress envisioned courts to adopt within the scope of Chapter 15 is reflected by Congress’ directive that if a particular term or clause of the statute is deemed ambiguous, a court is to refer to the Model Law, and if necessary, how foreign courts interpret the provisions of the Model Law. Proponents of the revenue rule should also take note that the provisions of Chapter 15 clearly require a bankruptcy court to assess ‘matters of foreign law and policy.’ Because a U.S. court could not determine how the claims of local creditors would fair in a foreign insolvency without conducting a comparison of the laws of the foreign jurisdiction to the laws of the United States. Congress’ confidence in the bankruptcy courts to conduct such assessments is further supported by the enactment of section 1520 of the Bankruptcy Code. Pursuant to section 1520, if a U.S. bankruptcy court determines a foreign insolvency proceeding is not a main proceeding (ancillary), the court can still provide relief, up to and including the same assistance granted to a main proceeding. Again, in such instances, the U.S. court must interpret and compare U.S. and foreign law.

This Article also recommends that the United States could limit assistance in collection of tax claims to governments that qualify as equivalent to U.S. law. This guideline would address at least two potential counterarguments to this change. One, it would avoid the imposition on U.S. courts of enforcing foreign laws that conflict with U.S. legal principles and public policy. Two, because any agreement to provide mutual assistance in tax collection would be enacted as amendments to tax-treaties there would be no concern that the courts of either country must adjudicate the public policy of the other.

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10. Assistance in tax collection may be comprehensive and cover taxes of every kind owed by residents or non-residents as is the case in Article 27 of the OECD Model Convention or more limited and cover only the taxes owed by residents and covered by the bilateral tax convention, e.g. direct taxes. Before agreeing to provide each other assistance in the collection of taxes, states will in particular consider whether their protection of fundamental taxpayers’ rights is similar (e.g. timely and adequate notice of claims against the taxpayer, the right to confidentiality of taxpayer information, the right to appeal, the right to be heard and present argument and evidence, the right to be assisted by a counsel of the taxpayer’s choice, the right to a fair trial, etc.)(emphasis added)) Available at: <http://www.oecd.org/dataoecd/44/41/39261429.pdf> (last visited December 21, 2011).
340 See OECD Commentary on Article 27 note _ supra at 413-420.
341 U.S. Const. art. II, § 2, cl. 2 (“[The President] shall have Power, by and with the Advice and Consent of the Senate to make Treaties, provided two thirds of the Senators present concur…”).
343 See id.
Chapter 15 instructs courts to refer to the UNCITRAL Legislative Guide on Insolvency Law\(^\text{345}\) to determine whether the insolvency regime adopted by a foreign government is equivalent to the laws of the United States.\(^\text{346}\) The UNCITRAL Legislative Guide provides that characteristics of an insolvency regime equivalent to the U.S. system would include: “a transparent rule of law, supervised by a judicial or administrative system designed to assure due process and fair treatment, and at least a moderately developed commercial law regime (one that may, but need not necessarily, include a scheme for security interests).”\(^\text{347}\)

Section 1522 of Chapter 15, provides bankruptcy courts "broad latitude to mold relief to meet specific circumstances."\(^\text{348}\) Section 1522 is based on article 22 of the Model Law.\(^\text{349}\) The drafters of the Model Law provide the following explanation for their decision not to limit Article 22 relief to "local creditors":

In many cases the affected creditors will be "local" creditors. Nevertheless, in enacting article 22, it is not advisable to attempt to limit it to local creditors. Any express reference to local creditors in paragraph 1 would require a definition of those creditors. An attempt to draft such a definition (and to establish criteria according to which a particular category of creditors might receive special treatment) would not only show the difficulty of crafting such a definition but would also reveal that there is no justification for discriminating [sic] creditors on the basis of criteria such as place of business or nationality.\(^\text{350}\)

The Drafters explanation of why it is not advisable to limit relief to local creditors in a cross-border insolvency rings quite true in today’s global economy. Moreover, investment by and into the United States is likely to increase rather than decline. Thus, it is in the best interest of the United States to take the initiative to resolve the matter of secured claims in cross-border insolvencies.

\(^\text{345}\) See Desai \textit{supra} note 54 at 540-541, n. 162. Desai provides the following synopsis of the contents of the UNCITRAL Model Guide: The text represents a five-year effort to derive a best practices guide for the enactment of a modern insolvency law, as an aid to countries engaged in just such a task. Because the text was the result of input from a number of expert groups and non-governmental organizations, as well as healthy debate among delegates from the thirty-six member nations of UNCITRAL, representing countries around the globe, both common law and civil, both developed and developing, its provisions are drafted with sufficient breadth to encompass a fairly wide variety of insolvency systems, while still offering concrete recommendations that, in the aggregate, could serve as a template for a modern insolvency law to be enacted by a country that never before had such a law.


\(^\text{347}\) See Desai \textit{supra} note 54 at 542-543 n. 163 (citing) (UNCITRAL Model Guide. at 2, para. 5 (discussing how the proper implementation of an insolvency regime requires establishment of underlying factors that go beyond which is focused upon in the guide); see generally Cambridge Gas Transp. Corp. v. The Official Comm. of Unsecured Creditors of Navigator Holdings PLC, [2006] UKPC 26, [15], [2007] 1 A.C. 508 (appeal taken from Isle of Man) (U.K.) ("The important point is that bankruptcy, whether personal or corporate, is a collective proceeding to enforce rights and not to establish them.").


\(^\text{349}\) See \textit{supra} note 26.

\(^\text{350}\) See id. at ¶ 163.
Critics of the solutions proposed in this Article are likely to question why the United States should respect the secured status of foreign tax claims absent a promise of reciprocity. Such critics should consider the following.

Comment (a) of the Restatement provides that the rationale for the revenue rule in the context of foreign tax judgments is not universally accepted.\(^{351}\) The Restatement further provides that a U.S. court would not violate U.S. law by enforcing a foreign court’s tax judgment, provided such judgment will not conflict with sections 481 and 482 of the Restatement of Foreign Laws. The Drafters point out that regardless of these exclusions, pursuant to section 11 of the UFM-JRA, courts may enforce such judgments under principles of “comity or otherwise.”\(^{352}\) Thus, even in instances where the U.S. has acted unilaterally to encourage reciprocity, adherence to the revenue rule continues to counteract legislation enacted to advance cross-border co-operation.

**CONCLUSION**

Economically, the United States is clearly not an island entirely unto itself.\(^{353}\) This Article shows that the treatment of a U.S. secured tax claim in cross-border insolvencies implicate a nexus of laws, bilateral, and multilateral treaties. A conflict in law may exist between the jurisdiction administering the bankruptcy (**lex concurus**) and the laws of the jurisdiction where the secured claim arose (the United States). A further conflict may arise if the physical location of the secured asset (**situs**) is in a jurisdiction that does not follow the law of the **lex concurus**.

In the case of secured assets such as real property, the situs is unlikely to change. However, in the case of easily moved assets such as intangibles, a sophisticated debtor could change the situs of such assets quietly and quickly. Thus, a number of unfavourable outcomes may arise, that the current laws and active treaties fail to address.

When a conflict of law arises between the **lex concurus** and the **lex situs**, courts are put in the difficult position of making a decision that is contrary to local law and interests. For example, if a U.S. court grants a foreign representative’s request to administer a debtor’s assets under a foreign proceeding, and such assets are also subject to an ERISA secured claim, how will it affect how closely ERISA monitors other foreign owned entities? Therefore, the likelihood that a foreign court would reject a tax claim arising from such benefits raises important public policy concerns that the United States and its trading partners must address.

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\(^{351}\) **RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW OF THE UNITED STATES** § 483, Reporter’s Note 2 (1987).

\(^{352}\) See supra note 356. Section 11 of the Act provides: “This [act] does not prevent the recognition under principles of comity or otherwise of a foreign-country judgment not within the scope of [the Act]. See id. at 21.

\(^{353}\) Attributed to poet John Donne.