Obtaining Freezing Injunctions in England in Support of Foreign Litigation: Tax Nous and Policing International Fraud in an Era of Transparency

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ABSTRACT

Following the credit crunch of 2007/2008 many countries are seeking ways to recover unpaid taxes or the proceeds of corruption, crime or fraud from their citizens. The global trend is towards greater tax transparency with moves to readily share information about taxpayers with other countries. This article examines that trend and what it may mean in terms of foreign states making use of the English courts’ extensive powers to grant worldwide freezing injunctions in support of foreign litigation. While those powers are dynamic and English judges will be keen to intervene in cases of fraud, there are some crucial decisions which need to be made in the primary court at the outset in terms of how the claims are framed in order not to fall foul of the strict tests the English courts will apply when considering applications for such worldwide freezing injunctions.

I. FREEZING INJUNCTIONS IN ENGLAND IN SUPPORT OF FOREIGN PROCEEDINGS

From their first outing in 1975, the English High Court’s freezing injunctions have increasingly become the weapon of choice in international fraud cases.1 Described variously as one of the law’s ‘nuclear weapons’2 or even a ‘thermo—nuclear’3 one, English judges have appreciated that their powerful nature can only be unleashed when there are proper grounds for doing so.

The aim of a freezing injunction is to prevent a defendant from dissipating his assets with the intention or effect of frustrating enforcement of a prospective judgment. They are not an end in themselves and are not granted to give security to a claimant for his claim; although in practice they may have that effect.

Freezing injunctions are available in support of foreign litigation. The relevant law in this area will depend to an extent on whether the main claim is in an EU state or not but the starting point is always section 25 of the Civil Jurisdiction and Judgments

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1 The creation of this form of injunction was a judicial innovation in the case of Mareva Compania Naviera SA v. International Bulk Carriers SA (The Mareva) [1975] 2 Lloyd’s Reports 509.

2 Per Donaldson IJ in Bank Mellat v. Nikpour [1985] FSR 87 at 92. The other ‘nuclear weapon’ being the ‘search order’.

3 Per Jacob J in Alliance Resources v. O’Brien (unreported).
Act 1982 as extended by the Civil Jurisdiction and Judgments Act 1982 (Interim Relief) Order 1997 (CJJA). The CJJA gives the English High Court the power to grant interim relief in proceedings that have been, or are about to be, commenced in a foreign court. It is a supporting and ancillary jurisdiction with the aim of ensuring international judicial cooperation to ensure that justice is done.

The English court will be cautious in relation to applications in these circumstances as it is likely to be less well informed of all the facts than if it were the primary court and it will obviously apply the basic requirements for seeking such an order in the first place, e.g. is there a good arguable case and a real risk of dissipation of assets?

Clearly, the section 25 CJJA jurisdiction runs certain risks. The effect of a worldwide freezing order may overlap with or be inconsistent with the approach taken by the domestic court in question. This risk is covered by sub-section 25(2) of the CJJA, which provides that:

On an application for any interim relief under subsection (1) the court may refuse to grant that relief if, in the opinion of the court, the fact that the court has no jurisdiction apart from this section in relation to the subject matter of the proceedings makes inexpedient for the court to grant it (emphasis added).

There is no guidance in the Act as to what ‘inexpediency’ might mean and so the common law has filled the gap, most notably with the decisions of the Court of the Appeal in several cases of which the leading case is Motorola Credit Corp v. Uzan.4

The Court of Appeal gave detailed guidance in the Motorola case about five considerations that any Court hearing a section 25 application should particularly bear in mind:

1. Whether the making of the order will interfere with the management of the case in the primary court (e.g. whether the order is inconsistent with an order made by the primary court or overlaps with it);
2. Whether it is the policy of the primary jurisdiction not itself to make worldwide freezing orders or disclosure orders;
3. Whether there is a danger that the orders made will give rise to disharmony or confusion and/or risk of conflicting inconsistent or overlapping orders in other jurisdictions, in particular the courts of the state where the person enjoined resides or where assets are located;
4. Whether at the time the order is sought there is likely to be a potential conflict as to jurisdiction rendering it inappropriate and inexpedient to make a worldwide order; and
5. Whether, in a case where jurisdiction is resisted and disobedience is to be expected, the court will be making an order, which it cannot enforce.

The English courts will consider the position of each defendant/respondent separately.

a) Real Connecting Link

In practical terms, the courts also apply another test, namely, asking whether there is a ‘real connecting link’ between England and the subject matter of the interim relief sought.5 This has been the test where the primary court is a EU member state. However, while the

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test does not strictly apply to cases where the primary court is outside the EU, if there is no such link there needs to be another compelling factor to justify the worldwide relief.6

The rationale for this further ‘real connecting link’ test is about policing the order. The court that makes the order should be the one best placed to police it and if neither the defendant nor his assets are located in England this may prove impossible.

The Motorola case is an interesting example of how an English court will weigh up some of the relevant factors such as policing the order. In that case, the claimants sought an English freezing injunction against the defendants in support of the main proceedings in the Southern District of New York. Two of the defendants were resident outside the jurisdiction and had no connection with England. As such, the application failed against those two defendants as the Court of Appeal felt that there was no point making an order against them, which it could not police.

However, one of the other defendants was a Turkish national, resident in Turkey. The application was successful against him because he had assets within England and so there was an opportunity therefore for the Court of Appeal to police the order against him if he disobeyed by, for example, granting a sequestration order.

b) The Relevance of the Primary Court’s own Injunctive Powers

The question of whether the primary court has the power to or has/has not elected to order an equivalent injunction will always be of relevance to an English court.

If a primary court (such as the US Federal Court) does not have the power to make the freezing order, then an English court will question whether the primary court would be affronted by such an order. In circumstances where the primary court has indicated that it would welcome an English order, the answer is easy. However, in other cases how the English courts ask and answer that question is quite revealing in terms of the underlying approach they wish to take, particularly in cases of fraud. So, for example, one might suggest that the fact that the US court is constitutionally prohibited from making such worldwide orders would be interpreted as that court being affronted by such an order.7 Instead, it has been interpreted as a situation in which the court would welcome the assistance of an English court.

In large part this approach can be explained by the English courts’ ready willingness to step in where there is a prima facie case of fraud. In such situations, the considerations of comity often take a back seat to a desire to fight or at least mitigate the effect of what appears to be dishonest behaviour which may see assets disappear before a final judgment can be handed down on the merits of the claim.

This practical approach echoes the underlying legal position of ‘fraud’ claims in civil litigation in England. Civil or commercial ‘fraud’ is not a cause of action itself but describes a range of activities in respect of which there are various causes of action. These often include the tort of deceit but the categories are not closed because, as Lord Hardwicke

6 See the case of Mobil Cerro Negro v. Petroleos de Venezuela S.A [2008] EWHC 532 (Comm). Here Walker J set aside a freezing order, which had been granted in support of an arbitration in New York. Although, he was considering the English Court’s powers to intervene to support foreign arbitrations under section 44 of the Arbitration Act 1996, this power is analogous to the section 25 CJJA jurisdiction and similar principles apply.

7 The US Supreme Court notably considered the issue of freezing orders in the case of Grupo Mexicano de Desarrollo, S.A. v. Alliance Bond Fund, Inc 527 U.S. 308 (1999). In a five-four judgment delivered by Justice Scalia, it considered that despite its own equitable powers it had ‘no authority to craft a “nuclear weapon” of the law’ and that the debate over such issues should be resolved not in that Court but by Congress.
said ‘fraud is infinite’.\(^8\) In other words if the courts of equity tried to define fraud they would fetter their jurisdiction and be eluded ‘by new schemes which the fertility of man’s invention would contrive’.\(^9\) So, as the underlying law must be dynamic, so too this feeds through in some ways to the approach of the English judges in their desire to fight fraud, notwithstanding issues of comity.

The high water mark of this dynamic approach may arguably be found in the case of Republic of Haiti \textit{v.} Duvalier in which the Court of Appeal made a worldwide freezing order in support of a fraud claim in France against a non-resident defendant with no assets in England.\(^{10}\) In that case, the defendant had solicitors in England and it was argued that information about the defendant’s worldwide assets was in England. The Court of Appeal felt that the case was ‘most unusual’ and one where it was appropriate to act as an international policeman in relation to assets abroad. However, the ‘real connecting link’ with this jurisdiction is harder to see.

More recent decisions of the English courts have been more cautious and in the case of ICICI Bank UK Plc \textit{v.} Diminico NV, Popplewell J helped to define the limits of the section 25 power.\(^{11}\) In this decision, the judge held that where a defendant is neither resident in England and Wales nor subject to its jurisdiction for some other reason, it will only grant a worldwide freezing order under section 25 in exceptional circumstances, namely where the applicant can persuade the court that there is a ‘real connecting link’ between the order sought and the English court’s jurisdiction; that it is appropriate for the English court to act as an ‘international policeman’ in relation to foreign assets; and it is just and expedient for the English court to grant the order.

In this case as the defendant was a Belgian company with no presence in England, there was no ‘real connecting link’ and a worldwide freezing order would not have been granted.\(^{12}\) There was no effective sanction which the English court could apply to enforce compliance by the defendant with any worldwide order and nothing which made it appropriate for the English court to act as an ‘international policeman’.\(^{13}\)

\textbf{II. GLOBAL TRENDS IN TAX TRANSPARENCY AND THEIR IMPACT ON POLICING FRAUD}\(^{14}\)

For many years, international institutions and organisations, such as the Organisation for Economic Co-operation and Development (OECD) have been pressing member states to develop measures to counter the distorting effects of harmful tax competition and the

\(^8\) Letter from Lord Hardwicke to Lord Kames, 30 June 1759.

\(^9\) \textit{Ibid.}

\(^{10}\) [1990] 1 QB 202 (CA),

\(^{11}\) [2014] EWHC 3124 (Comm).

\(^{12}\) In fact ICICI had withdrawn this part of the application before the hearing. Nevertheless, Popplewell J felt it helpful to clarify this point in his judgment.

\(^{13}\) It is worth noting that the court did grant a domestic ‘English’ freezing injunction over the defendant’s English assets. However, the existence of those assets had no bearing on the consideration of the worldwide order.

\(^{14}\) The author of this article has spent his entire career trying to avoid dealing with tax laws. It is with deep regret that he has realised that in the current climate it is essential for international fraud litigators to have an understanding of tax laws and the trends in global tax transparency.
practices of tax havens and preferential tax regimes. Since the publication of its report in 1998 entitled *Harmful Tax Competition*, the OECD has been urging members to act by basing their tax agreements on models which allow for the exchange of information on request without the carve-out for bank secrecy laws.

While some progress was made in the late 1990s and early 2000, the global credit crunch in 2007/2008 had a dramatic impact on these moves towards tax transparency. In part stimulated by a desire to receive taxes properly due from its citizens overseas and in part due to the revelations about US citizens hiding assets in Swiss bank accounts (and not paying taxes due), the US Congress enacted the Foreign Account Tax Compliance Act (FATCA) which came into force in 2010.

FATCA requires US persons, including individuals who live outside the US (for example in Saudi Arabia or Turkey) to report their financial accounts held outside the US. Crucially it also requires foreign financial institutions such as banks to report to the Internal Revenue Service (IRS) about their US clients.\(^\text{15}\)

Unlike other countries, the US levies income taxes on its citizens regardless of their place of residence and therefore requires Americans living abroad to pay US tax on foreign income. FATCA also makes it more difficult for such US taxpayers to conceal assets held in offshore accounts and shell corporations.

The FATCA legislation has come as a shock to many individuals who are US citizens by birth but who live elsewhere (such as our examples of Saudi Arabia and Turkey) and who have never filed any tax returns or paid any tax to the IRS. Before now, the US had few ways to find out about them but now their banks or other financial institutions will have to report them to the IRS directly or indirectly.

On 6 May 2014, forty-seven major countries and financial centres, including all thirty-four OECD member states such as Turkey and the UK endorsed the *Declaration on Automatic Exchange of Information in Tax Matters*. This commits the countries to implementing a new single global standard on automatic exchange of tax information. There are a number of official acronyms for this process but it is commonly being referred to as ‘GATCA’ or ‘Global FATCA’.\(^\text{16}\) In simple terms, G20 countries other than the US like the idea of being informed about their citizens living abroad so they can monitor whether any tax is payable by them.

Bilateral and multilateral cooperation between tax authorities is on the agenda as part of Turkey’s presidency of the G20 in 2015\(^\text{17}\) and formed part of the agenda at the G20 Finance Ministers’ meetings in February of this year in Istanbul\(^\text{18}\) to be followed by an International Tax Symposium in May in Istanbul.

Some countries have already signed up as ‘early adopters’ of this new regime (the UK is one, Turkey is not) and the OECD has set a very aggressive timetable for them to

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\(^{15}\) In practice the way this legislation achieves its aim is by virtue of the US entering into intergovernmental agreements with countries around the world to aid compliance. Turkey has not signed such an agreement but has agreed to one in substance.

\(^{16}\) The Common Reporting System or ‘CRS’ is one.

\(^{17}\) See *Turkish G20 Presidency Priorities for 2015*.

\(^{18}\) See the report by the OECD Secretary General, found at <www.oecd.org/g20/topics/taxation/g20-remarks-session5-international-tax-issues.html>.
start reporting by the end of 2015. This means that soon, financial institutions around
the world will need to review the tax residency status for over sixty countries (instead of
just US citizens) and start reporting them to the relevant authorities.

**III. COMMENT**

Why then are these moves toward global tax transparency and information sharing
relevant to the policing of international fraud and the English courts’ section 25
jurisdiction? As a matter of public policy, the English courts will not help a foreign state
collect taxes. However, the English courts are willing to help if a civil or criminal fraud
claim in another jurisdiction is framed in the right way.

This is not an easy task as the recent case involving the United States against
the former president of Nigeria (Sani Abacha) and others exemplifies. In that case,
*Blue Holding (t) Pte Ltd and another v. United States of America*, the US government had
commenced forfeiture proceedings against assets of the defendants, which allegedly
derived from the proceeds of corrupt misappropriations carried out by the former
President of Nigeria. Some of those assets were in England.

The defendants argued that the US proceedings were criminal and not civil and
that therefore the section 25 jurisdiction did not apply. At first instance, Field J held that
while it was correct that the US government had first to prove in the US that criminal
offences had been committed, this did not mean the proceedings were criminal. As the
case sought the forfeiture of property (and not the imprisonment) of the defendant they
were civil proceedings. As such a worldwide freezing order was possible.

However, the Court of Appeal disagreed – and discharged the freezing order. It
held that any judgment obtained in the US would be unenforceable in England and there
would be no other utility in granting the order.

The court considered the regime under the Proceeds of Crime Act 2002 (External
Requests and Orders) Order 2005. Foreign authorities can seek assistance from the UK
enforcement authorities to secure the recovery of assets located in the UK to implement
foreign orders. The common law rules that foreign orders of a penal or confiscatory
nature are not enforceable in England are overruled but this statutory scheme and the
court felt that the US government should not be trying to go round this scheme by using
a section 25 application.

This case offers a salutary lesson to foreign governments or authorities seeking to
invoke the section 25 jurisdiction. They should be careful at the outset to ensure that
the civil or criminal complaint framed in the domestic court is one which allows them
to pass the strict tests applied by the English courts in relation to section 25. The global
moves towards tax transparency will only likely continue to encourage governments
to seek ways to recover the proceeds of fraud, tax evasion or corruption. How they
set about recovering those assets from overseas remains to be seen but requires careful
thought at the outset if the ‘international policeman’ is to be encouraged to make a
worldwide freezing order under section 25 CJJA.

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19 [2014] EWCA Civ 1291.
20 Consider Prime Minister Modi of India’s early announcement within 24 hours of his inauguration on
26 May 2014 to appoint a task force to recover $2 trillion in overseas unpaid taxes or proceeds of fraud.