

Webb v Webb (PC) - the role of a foreign tax debt in the allocation of matrimonial property

By Maria Hook (University of Otago, New Zealand) and Jack Wass (Stout Street Chambers, New Zealand)

When a couple divorce or separate, and the court is tasked with identifying what property is to be allocated between the parties, calculation of the net pool of assets usually takes into account certain debts. This includes matrimonial debts that are in the sole name of one spouse, and even certain personal debts, ensuring that the debtor spouse receives credit for that liability in the division of matrimonial property. However, where a spouse owes a liability that may not, in practice, be repaid, deduction of the debt from the pool of the couple's property may result in the other spouse receiving a lower share of the property than would be fair in the circumstances. For example, a spouse owes a debt to the Inland Revenue that is, in principle, deductible from the value of that spouse's assets to be allocated between the parties. But the debtor spouse has no intention of repaying the debt and has rendered themselves judgment-proof. In such a case, deduction of the debt from the debtor spouse's matrimonial property would leave the other spouse sharing the burden of a debt that will not be repaid.

This result is patently unfair, and courts have found a way to avoid it by concluding that, in order to be deductible, the debt must be one that is likely to be paid or recovered (see, eg, *Livingstone v Livingstone* (1980) 4 MPC 129 (NZHC)). This enquiry can give rise to conflict of laws issues: for example, there may be questions about the enforceability of a foreign judgment debt or the actionability of a foreign claim. Ultimately, the focus of the inquiry should be on the creditor's practical chances of recovery.

In the relatively recent Cook Islands case of *Webb v Webb*, the Privy Council ([2020] UKPC 22) considered the relevance of a New Zealand tax debt to matrimonial property proceedings in the Cook Islands. The Board adopted a surprisingly narrow approach to this task. It concluded that the term "debts" only included debts that were enforceable *against matrimonial property* (which in this

case was located in the Cook Islands), and that the debts in question were not so enforceable because they would be barred by the “foreign tax principle”. Lord Wilson dissented on both points.

Background

The parties – Mr and Mrs Webb – lived in the Cook Islands when they separated. Upon separation, Mr Webb returned to New Zealand. Mrs Webb commenced proceedings against Mr Webb in the Cook Islands under the Matrimonial Property Act 1976 (a New Zealand statute incorporated into Cook Islands law), claiming her share of the couple’s matrimonial property that was located in the Cook Islands.

Mr Webb, however, owed a judgment debt of NZ\$ 26m to the New Zealand Inland Revenue. He argued that, under s 20(5) of the Act, this debt had to be deducted from any matrimonial property owned by him. Under s 20(5)(b), (unsecured) personal debts had to be deducted from “the value of the matrimonial property owned by” the debtor spouse to the extent that they “exceed the value of any separate property of that spouse”. Given the size of Mr Webb’s debt, the effect of s 20(5)(b) would have been to leave Mrs Webb with nothing. She argued that the debt fell outside of s 20(5)(b) because it was not enforceable in the Cook Islands and Mr Webb was unlikely to pay it voluntarily.

Whether the debt had to be enforceable against the matrimonial property in the Cook Islands

Lord Kitchin, with whom the majority agreed, concluded that s 20(5)(b) only applied to debts that were either enforceable against the matrimonial assets or likely to be paid out of those assets. Debts that were not so enforceable were not to be taken into account when dividing the matrimonial assets (unless the debtor spouse intended to pay them by using those assets in his name). A different interpretation would lead to “manifest injustice”, because if the Inland Revenue “cannot enforce its judgment against those assets, Mr Webb can keep them all for himself” (at [41]). If the Inland Revenue could not execute its judgment against the assets, and Mr Webb did not pay the debt, the reason for applying s 20(5)(b) – which was to protect a debtor spouse’s unsecured creditors – disappeared.

Lord Kitchin considered that this conclusion found support in *Government of India v Taylor*, where Viscount Simonds (at 508) had explained that the meaning

of “liabilities” in s 302 of the Companies Act 1948 excluded obligations that were not enforceable in the English courts. The result in that case was that a foreign government could not prove in the liquidation of an English company in respect of tax owed by that company (at [42]).

In *Webb*, the judgment debt in question was a personal debt incurred by Mr Webb. However, Lord Kitchin seemed to suggest that the outcome would have been no different if the debt had been a debt incurred in the course of the relationship under s 20(5)(a) (at [46]). The word “debts” had the same meaning in s 20(5)(a) and (b), as referring to debts which are enforceable against the matrimonial property or which the debtor spouse intends to pay.

Lord Wilson did not agree with the Board’s interpretation. He considered that it put a gloss on the word “debts” (at [118]), and that it had “the curious and inconvenient consequence of requiring a court ... to determine ... whether the debt is enforceable against specified assets” (at [120]). Rather, a debt was a liability that was “likely to be satisfied by the debtor-spouse” or that was “actionable with a real prospect of recovery on the part of the creditor” (citing *Fisher on Matrimonial Property* (2nd ed, 1984) at para 15.6) – regardless of whether recovery would be against matrimonial or other assets (at [123]).

Applying this interpretation to the tax liability in question, Lord Wilson concluded that the liability was clearly actionable (because it had already been the subject of proceedings) and that the Inland Revenue did have a real prospect of recovery in New Zealand (at [126]-[127]). Mr Webb was living in New Zealand and was presumably generating income there, and the Commissioner had applied for the appointment of receivers of his property. This was sufficient to conclude that the debt was enforceable in New Zealand, “including on a practical level” (at [131]). The facts were different from the case of *Livingstone v Livingstone* (1980) 4 MPC 129, where the New Zealand Court had concluded that a Canadian tax debt could “for practical purposes” be disregarded because the debtor had already left the country at the time the demand was issued, he had no intention of returning and he had removed his assets from the jurisdiction. In such a case, if the debtor spouse were permitted to deduct the foreign tax debt without ever actually repaying it, they could take the benefit of the entire pool of matrimonial assets and thus undermine the policy and operation of the whole regime.

In our view, Lord Wilson’s interpretation is to be preferred. The relevant question

should be whether the debt is one that will be practically recoverable (whether in the forum or overseas). A debt may still be practically recoverable even if it is not enforceable against the matrimonial assets and is unlikely to be paid out of those assets. It is true that, in many cases under s 25(1)(b), the chances of recovery would be slim if the matrimonial assets are out of reach and the debtor spouse has no intention of paying the debt voluntarily (which seemed to be the case for Mr Webb: at [62]). By definition, personal debts are only relevant “to the extent that they exceed the value of any separate property of that spouse”, so in practice their recoverability would depend on future or matrimonial assets. Lord Wilson’s assessment of the evidence – as allowing a finding that there was a real likelihood that Mr Webb would have to repay the debt in New Zealand – is open to question on that basis. But that doesn’t mean that the debts *must* be enforceable against the matrimonial assets. While this interpretation would lead to fairer outcomes under s 25(1)(b) – because it avoids the situation of the debtor spouse not having to share their matrimonial assets even though the debt is recoverable elsewhere – it could lead to strange results under s 25(1)(a), which provides for the deduction of matrimonial debts that are owed by a spouse individually. It would be unfair, under s 25(1)(a), if such debts were not deductible from the value of matrimonial property owned by the spouse by virtue of being unenforceable against that property, in circumstances where the debts are enforceable against the spouse’s personal property.

The Board’s reliance on *Government of India v Taylor* [1955] AC 491 (HL) in this context is unhelpful. The question before the House of Lords was whether a creditor could claim in a liquidation for a debt that would not be enforceable in the English courts (regardless of whether the debt would be enforceable over certain – or any – assets). Under the Matrimonial Property Act, on the other hand, the court is not directly engaged in satisfying the claims of creditors, so the debt need not be an obligation enforceable in the forum court. Neither need it be an obligation enforceable against matrimonial property, wherever located. It simply needs to be practically recoverable.

Whether the debt was enforceable against the matrimonial property in the Cook Islands

As we have noted, Lord Wilson argued that there was a real prospect of the debt being paid – the implication being that this was not a case about a foreign tax debt at all. Mr and Mrs Webb were New Zealanders, and Mr Webb had relocated

to New Zealand before the proceedings were commenced in 2016 and had stayed there. The practical reality was that unless he found a way to meet his revenue obligations he would be bankrupted again. Lord Kitchin noted Mr Webb's apparent determination to avoid satisfying his liabilities to the IRD. Nevertheless, there was no suggestion that Mr Webb would leave New Zealand permanently to live in the Cook Islands and there enjoy the benefits of the matrimonial property.

Nevertheless, the majority's analytical framework required it to consider whether the tax debt was enforceable against the matrimonial property in the Cook Islands. The majority found that for the purpose of the foreign tax principle, the Cook Islands should be treated relative to New Zealand as a foreign sovereign state, despite their close historical and constitutional ties (and found that the statutory mechanism for the enforcement of judgments by lodging a memorial, cognate to the historical mechanism for the enforcement of Commonwealth judgments, did not exclude the foreign tax principle).

It was obvious that bankruptcy was a serious prospect, the IRD having appointed a receiver over Mr Webb's assets shortly before the hearing before the Board. That begged the question whether the IRD could have recourse to the Cook Islands assets, but on this point the case proceeded in a peculiar way. The Board observed that it had been given no details of the steps that a receiver or the Official Assignee might be able to take to collect Cook Islands assets, going so far as to doubt whether the Official Assignee would even be recognized in the Cook Islands "for the Board was informed that there was no personal bankruptcy in the Cook Islands and the position of Official Assignee does not exist in that jurisdiction." Section 655(1) of the Cook Islands Act 1915 states that "Bankruptcy in New Zealand shall have the same effect in respect to property situated in the Cook Islands as if that property was situated in New Zealand", but the Board was not prepared to take any account of it, the provision having been introduced for the first time at the final appeal and there being some doubt about whether it was even in force.

The unfortunate consequence was that the Board gave no detailed consideration to the question of how the foreign tax principle operates in the context of cross-border insolvency, a point of considerable interest and practical significance.

The common law courts have been prepared to recognise (and in appropriate cases, defer to) foreign insolvency procedures for over 250 years, since at least

the time of *Solomons v Ross* (1764) 1 H Bl 131, 126 ER 79 where the Court of Chancery allowed funds to be paid over to the curators of a debtor who had been adjudicated bankrupt in the Netherlands. But the relationship between this principle and the foreign tax principle has never been clear.

The UNCITRAL Model Law on Cross-Border Insolvency 1997 preserves states' ability to exclude foreign tax claims from an insolvency proceeding. As to the common law, the New Zealand Law Commission (expressing what may be the best guide to the content of Cook Islands law) observed in 1999 that the policy justification for refusing enforcement of foreign tax judgments may not apply in the same way in the context of cross-border insolvency where the collective interests of debtors are concerned. It noted that a number of countries (including Australia, the Isle of Man and South Africa) had moved past an absolute forbidding of foreign tax claims where such claims form part of the debts of an insolvent debtor subject to an insolvency regime. It thus concluded that "foreign taxation claims may sometimes be admitted to proof in a New Zealand bankruptcy or liquidation." While the Privy Council had a number of difficult issues to confront, it is perhaps unfortunate that they did not take the opportunity to bring clarity to this important issue.