PASQUANTINO V. UNITED STATES: THE SUPREME COURT'S MISSTEP IN PROSECUTING INTERNATIONAL TAX FRAUD UNDER THE WIRE FRAUD STATUTE – A BRUISE AND A BAND-AID

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I. INTRODUCTION

You probably can't recall reading a news article about Houston prosecutors going after suspects for violating criminal laws unique to Mexico. There is a common sense reason for this—while local authorities enforce local law and Federal authorities enforce Federal law, neither enforces the criminal laws of another country for acts committed on U.S. soil. The tradition of refusing to enforce another country's tax laws follows a similar rationale and is based on what one modern commentator calls the "public law taboo."[1] The taboo against enforcement of foreign tax law is based on the common law revenue rule, which dates back to the decisions of courts in eighteenth century England.[2] Despite this deeply entrenched legal concept, the United States Department of Justice in 2003 reached beyond its usual jurisdiction and prosecuted a team of liquor smugglers for violating a Canadian excise tax law.[3] This article criticizes the Supreme Court for rubber-stamping the prosecution in the 2004 case *Pasquantino v. United States* and articulates the policy problems the opinion may create for tax practitioners and clients alike in the years to come.

The question in *Pasquantino* was whether the United States could prosecute U.S. subjects under the federal wire fraud statute[4] for executing a plan to defraud Canada of excise taxes.[5] Justice Clarence Thomas answered the question in the

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1. William S. Dodge, *Breaking the Public Law Taboo*, 43 HARV. INT'L L.J. 161, 161 (2002) (defining the "public law taboo" as the "nonenforcement of foreign public law") (citing Andreas F. Lowenfeld, *Public Law in the International Arena: Conflict of Laws, International Law, and Some Suggestions for Their Interaction*, 163 RECUEIL DES COURS 311, 322-26 (1979-II)).

2. *See* Brenda Mallinak, *The Revenue Rule: A Common Law Doctrine for the Twenty-First Century*, 16 DUKE J. COMP. & INT'L L. 79, 80 (2006) (citing Att'y Gen. v. Lutwydge, (1729) 145 Eng. Rep. 674 (Exch. Div.)). The English court refused to enforce a Scottish tax obligation. *Lutwydge*, 145 Eng. Rep. at 674; *see* Mallinak, *supra* this note, at 80.

3. *See* Pasquantino v. United States, 544 U.S. 349, 353 (2005).

4. 18 U.S.C. § 1343 (Supp. III 2003).

5. *Pasquantino*, 544 U.S. at 353.

affirmative for the Court's five-member majority in 2005.[6]

His opinion stated that prosecution for international tax fraud in a U.S. court was possible under the federal wire fraud statute.[7] A few observers believed the decision disregarded bedrock principles of international law such as the revenue rule, which ordinarily prevents one country from enforcing the tax laws of another.[8] Other commentators saw the decision as a step in the right direction.[9] Both sides of the debate might be correct and incorrect in part. The *Pasquantino* debacle bruised and battered the procedural framework for prosecuting acts of international tax fraud, but the wound will heal. The band-aid is described in Parts II through VI below.

Part II of this paper introduces the distinction between public law and private law, focusing on the historic underpinnings. It discusses the importance of maintaining that distinction and posits that international treaties and deference to the common law revenue rule are methods of preserving it.

Part III discusses the revenue rule in more detail, as well as the rule's role in ensuring the separation of public and private law. Specifically, Part III seeks to establish that U.S. prosecutors who use the wire fraud statute in a *Pasquantino*-type enforcement action do not automatically violate the revenue rule. The Court implied prosecutors can avoid committing a violation by ensuring that the foreign country adjudicates whether and to what extent taxes are due before the criminal prosecution begins.[10] Oddly, this step was not taken by prosecutors nor

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6. *Id.* at 352-53. The majority consisted of Justices Thomas, Stevens, O'Connor, Kennedy and Chief Justice Rehnquist; Justices Ginsburg, Breyer, Scalia, and Souter dissented. *Id.* at 352.

7. *Id.* at 372 ("It may seem an odd use of the Federal Government's resources to prosecute a U.S. citizen for smuggling cheap liquor into Canada. But the broad language of the wire fraud statute authorizes it to do so . . . ."). By contrast, Justice Ginsburg's dissent said the wire fraud statute "does not extend to schemes to evade foreign tax and customs laws." *Id.* at 384 (Ginsburg, J., dissenting).

8. *E.g.*, Joshua Shore, Case Note, *The Pasquantino Plea: The Unfortunate Decline of the Revenue Rule and the Imprudent Extraterritorial Expansion of the American Wire Fraud Statute to Enforce Foreign Tax Law*, 37 U. MIAMI INTER-AM. L. REV. 197, 202 (2005) ("By discarding the revenue rule absent a clear manifestation of congressional intent to abandon it, the Supreme Court [in *Pasquantino*] overstepped its constitutional mandate.").

9. *See, e.g.*, Joseph M. West, *Federal Fraud Prosecutions of Schemes to Defraud Foreign Sovereigns of Import Taxes*, 50 WAYNE L. REV. 1061, 1061, 1073-80 (2004) ("*Pasquantino* ha[s] it right, that a wire fraud prosecution can ensue where the defendants engage in a scheme to defraud a government of foreign government of foreign government of import taxes," and that the Court "came to the correct conclusion," with the aforementioned result "consistent with both statutory language and purpose, and . . . not precluded by prudential or other considerations.").

10. *Pasquantino*, 544 U.S. at 375.

required by the courts in the *Pasquantino* matter.[11] Regardless, it is an important step to follow out of respect for foreign governments and their tax laws. Such action is inferred from the purpose of the revenue rule and finds support in the framework of the U.S. Constitution.[12] Discussion in Part III includes: (1) a history of the revenue rule and the development of its definitions; (2) an analysis of procedural requirements overlooked in the *Pasquantino* prosecution; and (3) a description of steps which should have been taken by the *Pasquantino* prosecutors to avoid a revenue rule violation.

Part IV of the paper discusses the Convention Between the United States of America and Canada with Respect to Taxes on Income and on Capital (the "Treaty")[13] and introduces a subsequent provision added in the Protocol Amending the U.S.-Canada Tax Treaty on Income and Capital (the "Protocol")[14] that applies in tax collection matters similar to *Pasquantino*. The Protocol requires that Canada determine as a final matter whether and to what extent Canadian income taxes are owed before the United States initiates collection activity through the Department of the Treasury.[15] The Supreme Court did not make a final determination of tax liability in *Pasquantino*,[16] but it is important to note that the tax involved in that case was an *excise* tax, rather than an *income* tax.[17] However, it is unclear whether

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> Petitioners used U.S. interstate wires to execute a scheme to defraud a foreign sovereign of tax revenue. Their offense was complete the moment they executed the scheme inside the United States; "[t]he wire fraud statute punishes the scheme, not its success." This domestic element of petitioners' conduct is what the Government is punishing in this prosecution, no less than when it prosecutes a scheme to defraud a foreign individual or corporation, or a foreign government acting as a market participant.

Id. (quoting United States v. Pierce, 224 F.3d 158, 166 (2d Cir. 2000)) (citations omitted); *see* United States v. Durland, 161 U.S. 306, 313 (1896).

11. *See generally* Pasquantino v. United States, 544 U.S. 349, 353 (2005).

12. *See, e.g.*, Her Majesty the Queen v. Gilbertson, 597 F.2d 1161, 1164 n.7 (9th Cir. 1979) (stating the revenue rule was so engrained that this was the first time a foreign country attempted to use U.S. courts to collect a foreign tax); *see also* U.S. CONST. art. IV, § 4; Milwaukee County v. White Co., 296 U.S. 268 (1935) (holding the full faith and credit clause mandates that states recognize tax judgments of courts in other states).

13. Convention Between the United States of America and Canada with Respect to Taxes on Income and on Capital, U.S.-Can., June 14, 1983, T.I.A.S. No. 11,087 [hereinafter U.S.-Can. Tax Treaty].

14. *See* Protocol Amending the Convention Between the United States of America and Canada with Respect to Taxes on Income and on Capital, U.S.-Can., Mar. 17, 1995, 2030 U.N.T.S. 237, art. 15 [hereinafter Protocol Amending U.S.-Can. Tax Treaty].

15. *Id.* art. 15, ¶¶ 2-3.

16. *Pasquantino v. United States*, 544 U.S. 349, 377 n.4 (2005) ("[T]he Government did not proffer evidence of the precise rate at which Canada taxes liquor imports, or reference any provisions of Canadian law.").

17. *Id.* at 353. An excise tax is "[a] tax imposed on the manufacture, sale, or use of

the Protocol applies to excise taxes as a matter of law.[18] Regardless, the courts in the *Pasquantino* matter should have fulfilled the requirements as a matter of prudence. Discussion in Part IV includes a detailed analysis of the Protocol and the *Pasquantino* opinion itself. It concludes by suggesting that prosecutors incorporate Protocol requirements into future *Pasquantino*-type enforcement actions pursued under the wire fraud statute.

Part V of this paper discusses how the Protocol will apply as a matter of law in situations where the United States uses the wire fraud statute to prosecute evasion of Canadian *income* tax. A hypothetical international income tax dispute is proposed, followed by application of the Protocol provisions and revenue rule limitations to the proposed situation. Analysis of the hypothetical scenario highlights the continued ability of the U.S. government to assist in international tax enforcement within a defined set of limitations.

Lastly, Part VI presents policy problems that may arise when prosecuting Canadian tax fraud under the wire fraud statute in the future. Even where revenue rule and Protocol safeguards are respected, there are times when the benefits of a *Pasquantino*-type enforcement action will be outweighed by the political and economic costs of international tax fraud prosecution. This final part identifies these potential costs and proposes a balancing test for deciding when such efforts are politically and economically feasible.

II. THE DISTINCTION BETWEEN PUBLIC AND PRIVATE LAW

A given nation's public and private laws are easily distinguished, but the distinction is rarely given a second thought because the question seldom arises. Both legal scholars and average citizens know the local police will never travel to a foreign country to arrest a suspect for committing a crime in that foreign country. Likewise, most people would probably agree that the Internal Revenue Service ("IRS") will never collect taxes owed to a foreign government on behalf of that government. This thought process is instinctive and the reasoning is rarely questioned.

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goods . . . or on an occupation or activity . . . ." BLACK'S LAW DICTIONARY 605 (8th ed. 2004). By contrast, an income tax is a tax imposed "on an individual's or entity's net income." *Id.* at 1497.

18. *See generally* Protocol Amending U.S.-Can. Tax Treaty, *supra* note 14, art. 15, ¶ 9. The Protocol provides that it applies to "all categories of taxes," and makes no specific reference to its application to all categories of *excise* taxes as such. *See id.*

Local police only investigate local matters and U.S. revenue agents only collect U.S. taxes, based on the characterization of laws as either public or private. Public laws are laws enforced by a government to protect the domestic environment and include criminal, antitrust, and tax laws.[19] Private laws include the laws of contracts or torts, which are enforceable by private party plaintiffs.[20] Accordingly, private lawsuits often extend across borders because there is no "domestic environment" limitation.[21]

Public laws are generally not enforceable by parties other than the governments that create them.[22] This prohibition separating public and private law dates back to eighteenth century England.[23] For example, in the 1776 case of *Rafael v. Verelst*, Chief Justice De Grey stated that "[c]rimes are in their nature local, and the jurisdiction of crimes is local."[24] The foundation for declining to enforce the public laws of another country is:

> [L]argely historical, having to do with the medieval idea that a community was directly responsible for offenses committed within its borders and with the origin of the jury as a body of men who would decide cases on the basis of their knowledge of the facts and their sense of the community.[25]

As governments became more sophisticated and began to create tax and revenue laws, the public law concept was extended to the

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19. *See* Philip J. McConnaughay, *The Scope of Autonomy in International Contracts and Its Relation to Economic Regulation and Development*, 39 COLUM. J. TRANSNAT'L L. 595, 627 (2001) (noting that the driving factor behind these "regulatory laws" is the effectuation of public interest, achieved by "regulat[ing] private conduct in order to prevent public or societal harm"); *see also* Randy E. Barnett, *Four Senses of the Public Law-Private Law Distinction*, 9 HARV. J. L. & PUB. POL'Y 267, 269 (1986) ("'[P]ublic law' causes of action are . . . usually brought by governmental ('public') authorities.").

20. *See* McConnaughay, *supra* note 19, at 627; *see also* Barnett, *supra* note 19, at 269 ("'Private law' actions are . . . usually brought by the private individual who was harmed . . . .").

21. *See* McConnaughay, *supra* note 19, at 630-31 ("[P]ublic law claims traditionally may be adjudicated only in the national courts of the nation supplying the public law . . . . The opposite is true of most private law claims . . . . National courts ordinarily do not refrain from hearing and resolving claims arising under the [private] law of another nation, thus dramatically increasing the number of possible forums in which a [private] claim arising out of an international transaction might be filed.").

22. *See* Barnett, *supra* note 19, at 269.

23. Dodge, *supra* note 1, at 166 (citing Rafael v. Verelst, (1776) 96 Eng. Rep. 621, 622 (K.B.); Folliott. V. Ogden, (1789) 126 Eng. Rep. 75 (Ct. Com. Pl.), *aff'd*, (1790) 100 Eng. Rep. 825 (Ch.); Wolff v. Oxholm, (1817) 105 Eng. Rep. 1177 (K.B.)).

24. (1776) 96 Eng. Rep. 621, 622 (K.B.).

25. Dodge, *supra* note 1, at 166.

new legislation.[26] Public tax and revenue laws, discussed further below, are generally characterized as being unenforceable by nations other than those which create them.[27] This specific prohibition has become known as the common law revenue rule.[28] When international tax disputes arise, the revenue rule and delicately crafted tax treaties ensure that the distinction between public and private law is maintained.

III. *PASQUANTINO*-TYPE ENFORCEMENT ACTIONS ARE POSSIBLE IF COMMON LAW REVENUE RULE SAFEGUARDS ARE RESPECTED

The definition of the revenue rule is not perfectly clear. At least three separate definitions are discernable from cases spanning the last two hundred years.[29] Application of the revenue rule is even less clear. This is evident from action taken by the Court in *Pasquantino*, which applied only the modern definition of the revenue rule, the only definition considered by U.S. courts in reported cases.[30] The Court refused to look beyond that definition and concluded that there was no revenue rule violation.[31] However, the Court might have reached a different conclusion had it considered the other two definitions and incorporated them into its analysis. The Court could have determined that prosecutors ignored important safeguards required by the rule. These safeguards, if followed, prevent

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26. *See, e.g.*, Wisconsin v. Pelican Ins. Co., 127 U.S. 265, 290 (1888) ("The rule that the courts of no country execute the penal laws of another applies, not only to prosecutions and sentences for crimes and misdemeanors, but to all suits in favor of the state for the recovery of pecuniary penalties for any violation of statutes for the protection of its *revenue* . . . .") (emphasis added); *see also* Dodge, *supra* note 1, at 167 n.28 (citing *Pelican Ins. Co.*, 127 U.S. at 290) (observing the "blending of the prohibition against enforcing penal laws and the prohibition against enforcing revenue laws").

27. *See* Ellen S. Podgor, *A New Dimension to the Prosecution of White Collar Crime: Enforcing Extraterritorial Social Harms*, 37 MCGEORGE L. REV. 83, 90 (2006) (quoting Pasquantino v. United States, 544 U.S. 349, 381 (2005) (Ginsburg, J., dissenting)) (explaining that the common law revenue rule "historically held that 'one nation generally does not enforce another's tax laws'").

28. Mallinak, *supra* note 2, at 79 ("[T]he revenue rule generally allows courts to decline entertaining suits or enforcing foreign tax judgments or foreign revenue laws . . . .").

29. *Id.* at 115 & n.237 (listing "three bases for the revenue rule: historical precedent, tax rulings, . . . and judicial scrutiny of foreign revenue laws") (punctuation altered) (citing Barbara A. Silver, *Modernizing the Revenue Rule: The Enforcement of Foreign Tax Judgments*, 22 GA. J. INT'L & COMP. L. 609, 612 (1992)); *see* discussion *infra* Part III.A (categorizing the three revenue rule definitions as "historical," "modern," and "anti-adjudication").

30. *See* Pasquantino v. United States, 544 U.S. 349, 360-68 (2005).

31. *See id.*

automatic violations of the revenue rule from occurring.[32] Generally, when foreign tax fraud is prosecuted under the U.S. wire fraud statute, courts should consider all three revenue rule definitions and ensure that their decisions respect the required safeguards discussed below. Otherwise, the revenue rule will be violated and the resulting decisions cannot stand.

A. *History of the Revenue Rule and its Possible Definitions*

The revenue rule is traditionally traced to Lord Mansfield's claim in *Holman v. Johnson* that "no country ever takes notice of the revenue laws of another."[33] Brought in an English court, *Holman* involved a French contract of sale for a shipment of tea between an English plaintiff and a French defendant.[34] The Frenchman intended to smuggle the shipment into England.[35] To avoid paying for the tea, he tried to invalidate the contract on grounds of illegality, but Lord Mansfield found for the Englishman on the theory that English customs laws have no effect on the illegality of a French contract.[36] The rule was expanded soon thereafter by Lord Mansfield in case concerning a shipping declaration.[37] The declaration document was designed to evade French tax, and the court was called upon to determine whether such design was indicative of fraud.[38] Ultimately, Lord Mansfield reasoned that the document was not fraudulent because the evaded tax was imposed by a foreign revenue law.[39] This brief history provides a *historical definition* for the revenue rule—namely, that the existence of foreign revenue or criminal laws is to be ignored in domestic commercial cases.[40]

The revenue rule began to expand into the area of international tax enforcement in the English case of *Municipal Council of Sydney v. Bull* in 1909.[41] The court held that foreign tax authorities could not use English courts to enforce their foreign tax laws.[42] This limitation was exported to the United

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32. *See* discussion *infra* Part III.B.

33. Holman v. Johnson, (1775) 98 Eng. Rep. 1120, 1121 (K.B.).

34. *Id.* at 1120.

35. *Id.*

36. *Id.* at 1120, 1122.

37. *See* Planche v. Fletcher, (1779) 99 Eng. Rep. 164, 164-65 (K.B.).

38. *Id.*

39. *Id.* at 165 (noting that "[o]ne nation does not take notice of the revenue laws of another").

40. *See* Silver, *supra* note 29, at 612.

41. (1909) 1 K.B. 7.

42. *See id.* at 12 ("Some limit must be placed upon the available means of enforcing the sumptuary laws enacted by foreign States for their own municipal purposes.").

States, where it now provides the backbone for the *modern definition* of the revenue rule.[43] The modern definition prevents "courts of one sovereign [from] enforc[ing] final tax judgments or unadjudicated tax claims of other sovereigns."[44] As mentioned above, it is the only revenue rule definition referenced in cases reported by U.S. courts, who have invoked it to prevent foreign tax authorities from using U.S. courts to enforce foreign tax laws.[45]

The purpose of the modern revenue rule is rooted in the separation of powers doctrine.[46] Judge Learned Hand articulated this purpose in *Moore v. Mitchell*, where he explained:

> To pass upon the provisions for the public order of another state is, or at any rate should be, beyond the powers of a court; it involves the relations between the states themselves, with which courts are incompetent to deal, and which are intrusted [sic] to other authorities. It may commit the domestic state to a position which would seriously embarrass its neighbor. Revenue laws fall within the same reasoning; they affect a state in matters as vital to its existence as its criminal laws.[47]

In *Moore*, an Indiana county treasurer attempted to collect a tax in a New York court from the executors of an Indiana taxpayer's will.[48] The court found the action to collect the tax "repugnant to the settled principles of private international law, which preclude one state from acting as a collector of taxes for a sister state, and from enforcing its penal or revenue laws as such."[49] Although such actions between parties from different U.S. states are now

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43. Att'y Gen. of Can. v. R.J. Reynolds Tobacco Holdings, Inc., 268 F.3d 103, 110 (2d Cir. 2001). The Second Circuit observed that the revenue rule originated in English courts in the eighteenth century and that the "rule has entered United States common law [and] international law." *Id.* at 110-11 n.4 (citing numerous cases applying the revenue rule).

44. *Id.* at 109.

45. *See, e.g.*, Honduras v. Phillip Morris Cos., 341 F.3d 1253, 1256 (11th Cir. 2003); *R.J. Reynolds*, 268 F.3d at 109; Her Majesty the Queen v. Gilbertson, 597 F.2d 1161, 1163 n.1, 1164 (9th Cir. 1979) (stating that the revenue rule was "so well recognized that this [case] appear[ed] to be the first time that a foreign nation ha[d] sought to enforce a tax judgment in the courts of the United States").

46. *See R.J. Reynolds*, 268 F.3d at 113-14; Moore v. Mitchell, 30 F.2d 600, 604 (2d Cir. 1929) (Hand, J., concurring), *aff'd on other grounds*, 281 U.S. 18 (1930); Mallinak, *supra* note 2, at 100.

47. *Moore*, 30 F.2d at 604.

48. *Id.* at 601.

49. *Id.* at 602.

deemed permissible under the Full Faith and Credit clause[50] and by statute,[51] courts continue to rely upon Judge Hand's articulation of the purpose of the revenue rule in international tax disputes.[52] His rationale emphasized the separation of powers issue and asserted that the courts are not the appropriate entity to adjudicate the statutes of a foreign state.[53] This expansion of the revenue rule effectively creates a third definition: the *anti-adjudication definition.*[54]

It may seem odd that U.S. courts have not considered the historical or anti-adjudication definitions of the revenue rule. However, there are two reasons why they have not. First, modern courts have departed from the historical definition of the revenue rule in favor of the modern definition.[55] "[E]arly English cases rest on a far different foundation from that on which the revenue rule came to rest."[56] Accordingly, as articulated by Justice Thomas in *Pasquantino*, the historical definition might only be useful today in commercial cases where the concept of illegality is at issue.[57]

Second, the anti-adjudication definition has never been cited because it is only relevant when a U.S. subject is prosecuted under a foreign criminal or tax law.[58] It appears the

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50. U.S. CONST. art. IV, § 1; *see also* Milwaukee County v. M. E. White Co., 296 U.S. 268, 279 (1935) (holding that state tax judgments do not escape the reach of the Full Faith and Credit clause).

51. 28 U.S.C. § 1738 (2000) ("[J]udicial proceedings . . . shall have the same full faith and credit in every court within the United States . . . as they have by law or usage in the courts of such [s]tate . . . from which they are taken.").

52. Her Majesty the Queen v. Gilbertson, 597 F.2d 1161, 1164-65 n.8 (9th Cir. 1979). Even today, "Hand's reasoning is often quoted by domestic and foreign courts to support application of the revenue rule in the international context." Mallinak, *supra* note 2, at 86.

53. *See Moore*, 30 F.2d at 604 (Hand, J., concurring).

54. Although the anti-adjudication definition has never been directly considered in U.S. courts, Judge Hand's reasoning indicates a belief that foreign revenue law matters should not be adjudicated unless a court can determine "whether those laws are consonant with its own notions of what is proper." *See id.*

55. Pasquantino v. United States, 544 U.S. 349, 366 (2005) ("By the 20th century . . . [the historical] rationale for the revenue rule had been supplanted. . . . [C]ourts had begun to apply the revenue rule to tax obligations on the strength of the analogy between a country's revenue laws and its penal ones, superseding the original promotion-of-commerce rationale for the rule.") (citation omitted).

56. *Id.*

57. *Id.* at 365-66 (noting that the historical definition was derived from "cases involv[ing] contract law, [which] held that contracts executed with the purpose of evading the revenue laws of other nations were enforceable, notwithstanding the rule against enforcing contracts with illegal purposes").

58. *Cf.* Silver, *supra* note 29, at 612 ("[A]s illustrated by Judge Learned Hand's concurring opinion in *Moore v. Mitchell*, . . . judicial scrutiny of foreign law is incompatibly injurious to international relations.") (footnote omitted).

Pasquantino effort was the first time such prosecution has ever been attempted.[59] Neither *Pasquantino* nor the cases on which it relied identified any similar situations.[60] *Pasquantino* is therefore the first time U.S. courts have had occasion to rely on the anti-adjudication definition of the revenue rule.

B. *Effect of the Revenue Rule in* Pasquantino*-Type Wire Fraud Matters*

The Learned Hand excerpt above suggests domestic adjudication of foreign tax matters is not justiciable in U.S. courts.[61] This suggestion hits the mark: constitutional limitations should prevent U.S. courts from interpreting foreign tax law for purposes of determining whether and to what extent a tax is due in a foreign country.[62] Again, this limitation is rooted in the separation of powers model, which requires that foreign tax enforcement be handled, if at all, by the executive or legislative branches.[63]

The executive branch of the United States government can assist foreign countries with their tax enforcement issues through diplomacy, the treaty power, and extradition.[64] It cannot, however, ask the judicial branch to interpret foreign tax law or determine whether and to what extent a foreign tax is owed.[65] Article II, § 3 of the U.S. Constitution, which states that the President "shall take Care that the Laws be faithfully executed,"[66] limits the executive's power. The executive can

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59. *See Pasquantino*, 544 U.S. at 365-66 (The majority observed that none of the cases presented by the petitioner "involved a domestic sovereign acting pursuant to authority conferred by a criminal statute," and that the revenue rule had never been extended to mean that the United States was not expressly forbidden from enforcing its own criminal laws absent authority to enforce the criminal laws of another country.).

60. *Id.*

61. *See supra* text accompanying note 47 (quoting Moore v. Mitchell, 30 F.2d 600, 604 (2d Cir. 1929) (Hand, J., concurring), *aff'd on other grounds*, 281 U.S. 18 (1930)).

62. The *Pasquantino* court recognized the problem with courts evaluating "foreign law to determine whether the defendant violated U. S. law." *Pasquantino*, 544 U.S. at 369. However, the Court "assume[d] that by electing to bring this prosecution, the Executive has assessed this prosecution's impact on this Nation's relationship with Canada." *Id.*

63. *See* Att'y Gen. of Can. v. R.J. Reynolds Tobacco Holdings, Inc., 268 F.3d 103, 113-14 (2d Cir. 2001); Will Rearden, *"A Delicate Inquiry": Foreign Policy Concerns Revive the Revenue Rule in the Second Circuit and Bar Foreign Governments from Suing Big Tobacco*, 51 ST. LOUIS U. L.J. 203, 214 (2006); West, *supra* note 9, at 1077.

64. *See* Rearden, *supra* note 63, at 211-12.

65. *See id.* (noting that because tax enforcement concerns matters of public law, "questions regarding whether and to what extent the federal government should provide for the enforcement of foreign tax laws in domestic courts are necessarily allocated to the [executive and legislative] branches for resolution").

66. U.S. CONST. art. II, § 3.

request that the judicial branch assist in enforcing U.S. laws and its treaties with foreign nations, but those laws do not include the tax laws of a foreign nation.[67] Judge Hand probably had this prohibition in mind when he created the anti-adjudication definition of the revenue rule by stating that adjudication of another state's tax laws were beyond the powers of the courts.[68]

Does this mean the revenue rule was violated in the *Pasquantino* prosecution? Only slightly. The Supreme Court's *Pasquantino* decision referenced the modern definition of the revenue rule and ignored the more expansive anti-adjudication definition proposed by Learned Hand.[69] As a result, the Court simply dismissed the revenue rule as inapplicable.[70] It concluded that no violation was at issue because U.S. prosecutors, rather than Canadian officials, brought the prosecution.[71] However, if the Court had properly considered the anti-adjudication definition of the revenue rule, it would have remanded the case and required that the trial court consider the offense without evidence of whether or to what extent Canada was defrauded of taxes, or else abstained from the prosecution until Canada made the tax determination on its own.

It should be evident from the discussion above that prosecuting U.S. subjects for evading foreign taxes under the wire fraud statute can be accomplished without violating the revenue rule. The violation is avoided in a *Pasquantino*-type situation by ensuring that the foreign country interprets and applies its own tax law rather than allowing a U.S. criminal court to interpret it for purposes of completing an evidentiary record.[72] A brief explanation of the way this should work is

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67. *See* Made in the USA Found. v. United States, 242 F.3d 1300, 1313-14 (11th Cir. 2001) (observing that the judiciary has a "narrowly circumscribed role" in foreign affairs and that "[m]atters relating to the conduct of foreign relations . . . are so exclusively entrusted to the political branches of the government as to largely be immune from judicial inquiry or interference") (internal quotation marks omitted); *see also* Kucinich v. Bush, 236 F. Supp. 2d 1, 16 (D.D.C. 2002) (noting that matters regarding treaties are "largely political questions best left to the political branches of the government, not the courts, for resolution").

68. *See* Moore v. Mitchell, 30 F.2d 600, 604 (2d Cir. 1929) (Hand, J., concurring), *aff'd on other grounds*, 281 U.S. 18 (1930).

69. Pasquantino v. United States, 544 U.S. 349, 366 (2005). The Court commented that the revenue rule, "at its core . . . prohibited the collection of tax obligations for foreign nations"; accordingly, the rule "prohibit[s] the collection of foreign tax claims." *Id.*

70. *Id.* at 368.

71. *Id.* at 362. The Court noted that the *Pasquantino* action was "unlike [the] classic examples of actions traditionally barred by the revenue rule." *Id.* Further, the Court stated that the action was not one seeking to "recover[] a foreign tax liability . . . . [but was] a criminal prosecution brought by the United States in its sovereign capacity to punish domestic criminal conduct." *Id.*

72. Adjudication by the Canadian court would prevent the separation of powers

helpful and follows in the next section, which first introduces more facts surrounding the *Pasquantino* prosecution and the requirements of the wire fraud statute itself.

C. *How to Avoid a Revenue Rule Violation When Prosecuting Foreign Tax Fraud Under the Wire Fraud Statute*

Pasquantino involved a liquor smuggling operation[73] that defrauded Canada of taxes and excise duties associated with importing and selling liquor.[74] The defendants ordered large volumes of liquor over the phone from a discount liquor store in Maryland, implicating the wire fraud statute,[75] then transferred it to New York for storage.[76] They concealed smaller quantities of the liquor in the trunk of a vehicle and drove into Canada without declaring the imported goods.[77] The Federal Bureau of Alcohol, Tobacco, Firearms, and Explosives ("ATF"), an agency that protects domestic liquor companies and state tax revenues from individuals who traffic in illegal liquor,[78] discovered the operation and opened an investigation.[79] As the investigation moved forward, the ATF learned that the defendants were smuggling alcohol out of the country,[80] which did not violate any federal alcohol statute.[81] It did implicate an anti-smuggling statute, but one which was unenforceable because there was no reciprocal agreement with Canada.[82] Thus, the defendants were

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issue and avoid the problem of U.S. courts adjudicating the statutes of a foreign state. *See Moore*, 30 F.2d at 603-04 (Hand, J., concurring).

73. United States v. Pasquantino, 336 F.3d 321, 324 (4th Cir. 2003). A case with almost an identical set of facts—defendants tried to smuggle tobacco into Canada to avoid paying taxes and coordinated parts of the operation over the phone—was oppositely decided in favor of the defendants. *See* United States v. Boots, 80 F.3d 580, 583-84, 587 (1st Cir. 1996) (holding that prosecution for foreign tax fraud exceeded the scope of the wire fraud statute because the U.S. court would have to "effectively pass[] on the validity and operation of the revenue laws of a foreign country" and would thereby violate the revenue rule).

74. *Pasquantino*, 336 F.3d at 325. A veteran employee of Canadian Customs testified that the amount of taxes due on an imported case of liquor is generally "twice the purchase price of the case of liquor in the United States." *Id.* at 326.

75. 18 U.S.C. § 1343 (Supp. III 2003).

76. *Pasquantino*, 336 F.3d at 325.

77. *Id.* at 325, 333.

78. ATF Online – Bureau of Alcohol, Tobacco and Firearms, About ATF, http://www.atf.treas.gov/about/mission.htm (last visited Apr. 23, 2007).

79. *Pasquantino*, 336 F.3d at 325.

80. *Id.*

81. *See* Pasquantino v. United States, 544 U.S. 349, 374 (2005) (Ginsburg, J., dissenting).

82. *See* 18 U.S.C. § 546 (2000); *see also* Alan R. Johnson, *Systems for Tax Enforcement Treaties: The Choice Between Administrative Assessments and Court*

only indicted under the wire fraud statute rather than under any anti-smuggling provision.[83]

The wire fraud statute does not directly address liquor regulation.[84] Its development began 130 years ago with the creation of the mail fraud statute, which was later expanded to apply to a greater number of activities.[85] One such activity was criminal behavior involving interstate electronic communications among conspirators.[86] That expansion provision officially became known as the wire fraud statute in 1952.[87] It proscribes using wires, radio, or television in interstate or foreign commerce to "devise any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises."[88] Accordingly, it requires prosecutors to prove that: (1) the party devised a scheme to defraud, and (2) the scheme was designed to defraud another of money or property.[89] The value of money or property at issue in the scheme determines the extent of punishment suffered by individuals convicted under the statute.[90]

In *Pasquantino*, prosecutors were able to fulfill these two broad requirements with ease.[91] They satisfied the first

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Judgments, 10 HARV. INT'L L.J. 263 (1969). Congress enacted an anti-smuggling statute, 18 U.S.C. § 546, for domestic prosecution of smuggling activity where items are smuggled from the U.S. to a foreign country. *Pasquantino*, 544 U.S. at 374. A reciprocity clause was included stating that the statute was not enforceable in a case where items are smuggled into a foreign country which does not similarly criminalize smuggling into the United States. 18 U.S.C. § 546; *Pasquantino*, 544 U.S. at 374. Canada does not have a reciprocal smuggling statute, so the U.S. statute was unenforceable in the *Pasquantino* matter. *Pasquantino*, 544 U.S. at 374.

83. *Pasquantino*, 336 F.3d at 325.

84. *See generally* 18 U.S.C. § 1343 (Supp. III 2003).

85. Nirav Shah, *Mail and Wire Fraud*, 40 AM. CRIM. L. REV. 825, 825-26 (2003) (citing Durland v. United States, 161 U.S. 306, 314 (1896)). The mail fraud statute was enacted "with the purpose of protecting the public against all such intentional efforts to despoil, and to prevent the post office from being used to carry them into effect." *Durland*, 161 U.S. at 314.

86. Shah, *supra* note 85, at 825-26 ("A violation of [the wire fraud statute] can provide the unlawful act necessary to establish a RICO or money laundering violation. Once a mail fraud or wire fraud offense is established, both the RICO and the money laundering statutes allow for more severe penalties.") (footnotes omitted).

87. *See* Act of July 16, 1952, ch. 879, § 18(a), 66 Stat. 722 (codified as amended at 18 U.S.C. § 1343 (Supp. III 2003)); *see also* Pasquantino, 544 U.S. at 360 (looking to common law relating to the wire fraud statute in the year of its enactment).

88. 18 U.S.C. § 1343.

89. *See id.*; *Pasquantino*, 544 U.S. at 355 (quoting Cleveland v. United States, 531 U.S. 12, 26 (2000)).

90. *See* 18 U.S.C. § 1343 ("Whoever, having devised or intending to devise any scheme or artifice to defraud . . . shall be fined under this title or imprisoned not more than 20 years, or both. If the violation affects a financial institution, such person shall be fined not more than $1,000,000 or imprisoned not more than 30 years, or both.").

91. *Pasquantino*, 544 U.S. at 355, 357.

requirement by presenting evidence that the defendants "routinely concealed imported liquor from Canadian officials and failed to declare those goods on customs forms."[92] The second requirement was met by providing evidence of the amount of money or property avoided in the scheme.[93] This final bit of evidence led to the revenue rule problem.[94] The prosecutors in *Pasquantino* violated the revenue rule because the money or property they alleged was the object of the fraud was an *unadjudicated* Canadian tax claim.[95] Canada had indicted the men for tax fraud but had not yet determined whether or to what extent taxes were due.[96] However, before Canada could reach a final determination, the U.S. criminal court interpreted and applied Canadian tax laws and made the determination itself.[97] That action violated the revenue rule.[98]

The U.S. criminal court should have either abstained from making a tax determination and waited for Canada to finish the task or completed the prosecution as if no tax were due to Canada. Either action would have given the defendants a day in Canadian court to defend themselves against the tax charges and ensured that the Canadian government maintained complete sovereignty over its own tax laws. Furthermore, it also would have guaranteed that the revenue rule requirements were satisfied. Finding that a scheme to defraud a foreign government could be brought via the wire fraud statute "not only improperly enmesh[es] U.S. courts in interpreting and applying those foreign tax laws . . . but also risks turning federal prosecutors and investigators into de facto criminal law enforcement agents for foreign tax authorities."[99]

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92. *Id.* at 357 (concluding that such conduct constituted a "scheme or artifice to defraud Canada of taxes due on the smuggled goods") (punctuation omitted).

93. *Id.* at 356 (noting that the defendants' smuggling operation sought to "deprive Canada of money legally due, and their scheme thereby had as its object the deprivation of Canada's 'property'").

94. The Supreme Court implicated the revenue rule once it concluded that "the right to tax revenue is property in Canada's hands." *See id.*

95. *See id.* at 375 (Ginsburg, J., dissenting) ("Canadian courts are best positioned to decide 'whether, and to what extent, the defendants have defrauded the governments of Canada and Ontario out of tax revenues owed pursuant to their own, sovereign, excise laws.'") (quoting United States v. Pasquantino, 336 F.3d 321, 343 (4th Cir. 2003) (en banc) (Gregory, J., dissenting)).

96. *See id.* at 375 n.3.

97. *See id.* at 375 ("The defendants' conviction for wire fraud therefore resulted from, and could not have been obtained without proof of, their intent to violate Canadian revenue laws.").

98. *Id.* at 382 (stating that the implication of the revenue rule is "unavoidably obvious").

99. Kathryn Keneally, *The U.S. Prosecutes Foreign Tax Evasion as a Domestic Crime—with Far Reaching Consequences*, 88 J. TAX'N 224, 229 (1998).

IV. THE U.S.-CANADA TAX TREATY INCORPORATES REVENUE RULE SAFEGUARDS

The revenue rule is not the only obstacle requiring U.S. courts to refrain from adjudicating Canadian tax claims. The Protocol amending the U.S.-Canada Income Tax Treaty, mentioned above, contains a similar limitation.[100] The Protocol was negotiated to establish guidelines for collecting foreign taxes owed in one country by taxpayers residing in the other country.[101] To this end, the Protocol includes a provision that prevents the adjudication of tax claims in a country other than the one where the taxes are due.[102] Though it remains unclear whether the Protocol applied to the excise tax in *Pasquantino* as a matter of law, it should have been applied as a matter of principle. Discussion in this Part covers: (1) an introduction of the collection provisions in the Protocol; (2) an analysis of how the courts should have applied the Protocol in the *Pasquantino* case; and (3) a discussion of the Protocol's role in future income tax cases brought under the wire fraud statute.

A. *Introduction to the U.S.-Canada Income Tax Treaty*

As discussed above, the separation of powers doctrine requires that international tax matters be handled by the political branches.[103] In response to this constitutional requirement, the office of the President (with the advice and consent of the Senate) has entered into tax treaties with numerous countries to avoid creating conflicts with U.S. neighbors over tax issues.[104] Several tax treaties include

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100. *See* Protocol Amending U.S.-Can. Tax Treaty, *supra* note 14, art. 15, ¶¶ 2-4; *see also* Mallinak, *supra* note 2, at 96-97 (observing that the U.S.-Can. Treaty "does not provide a mechanism for collecting taxes owed to the foreign government by a citizen of the other State").

101. *See* Protocol Amending U.S.-Can. Tax Treaty, *supra* note 14, art. 15, ¶ 1; *see also* Mallinak, *supra* note 2, at 94.

102. *See* Protocol Amending U.S.-Can. Tax Treaty, *supra* note 14, art. 15, ¶ 3 ("A revenue claim of the [State requiring collection assistance] that has been *finally determined* may be accepted for collection by the competent authority of the requested State . . . .") (emphasis added). A claim is finally determined "when the applicant State has the right under its internal law to collect the revenue claim and all administrative and judicial rights of the taxpayer to restrain collection in the applicant State have lapsed or been exhausted." *Id.* art. 15, ¶ 2; *see also* STAFF OF J. COMM. ON TAX'N, 104TH CONG., EXPLANATION OF PROPOSED PROTOCOL TO THE INCOME TAX TREATY BETWEEN THE UNITED STATES AND CANADA 41-42 (Comm. Print 1995), *available at* http://www.house.gov/jct/s-15-95.pdf [hereinafter PROPOSED PROTOCOL EXPLANATION].

103. *See* Mallinak, *supra* note 2, at 100 (citing Att'y Gen. of Can. v. R.J. Reynolds Tobacco Holdings, Inc., 268 F.3d 103, 113-14 (2d Cir. 2001)); Silver, *supra* note 29, at 612 n.25; *see also supra* text accompanying notes 61-65.

104. *See* Mallinak, *supra* note 2, at 94.

provisions for reciprocal assistance in collecting foreign taxes.[105] Because foreign countries cannot use the U.S. court system to enforce their tax laws, a country will use these reciprocal collection provisions to request that the United States simply collect the tax on its behalf.[106]

The Convention establishing the U.S.-Canada Income Tax Treaty took place on September 26, 1980, with the Treaty entering force on August 16, 1984.[107] It includes the reciprocal collection provision[108] and clearly applies to income taxes.[109] However, it is unclear whether it applies to excise taxes such as the tax on liquor in *Pasquantino*.[110] The Treaty was amended by the Protocol of March 17, 1995, which added Article XXVIA on "assistance in collection."[111] The collection provisions include the following:

1. The United States and Canada reciprocally agree to help each other collect unpaid taxes, together with interest, penalties, and other costs due.[112]
2. Neither country can request collection assistance until it reaches final judgment in the country in which the tax is owed and the taxpayer has exhausted all judicial remedies.[113]
3. The country providing collection assistance should collect the tax as if it were its own, but no rights of administrative or judicial review should be given.[114]

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105. *Id.* at 94-95. U.S. treaties with four countries—France, Denmark, Sweden, and the Netherlands—provide for assistance in collecting revenue claims. *R.J. Reynolds*, 268 F.3d at 115-16.

106. *See, e.g.*, Tesher v. United States, 246 F. Supp. 2d 297, 300 (S.D.N.Y. 2003) (discussing a Canadian revenue claim accepted for collection by the United States under Article XXVIA ¶ 7 of the U.S.-Canada Tax Treaty).

107. U.S.-Canada Tax Treaty, *supra* note 13. The Treaty was signed June 14, 1983 and March 28, 1984. *Id.*; *see also* Kappus v. Comm'r, 337 F.3d 1053, 1057 (D.C. Cir. 2003).

108. *See* Protocol Amending U.S.-Can. Tax Treaty, *supra* note 14, art. 21, ¶ 3.

109. *See id.* art. 1, ¶ 2.

110. While the Treaty specifically addresses only a limited class of excise taxes, it does state that "[n]otwithstanding the provisions of Article II (Taxes Covered), the provisions of this Article shall apply to *all categories of taxes* collected by or on behalf of the Government . . . ." Protocol Amending U.S.-Can. Tax Treaty, *supra* note 14, art. 15, ¶ 9 (emphasis added).

111. *Id.* art. 15, ¶¶ 1-3; *see also* PROPOSED PROTOCOL EXPLANATION, *supra* note 102, at 41.

112. *See* Protocol Amending U.S.-Can. Tax Treaty, *supra* note 14, art. 15, ¶ 1.

113. *See id.* art. 15, ¶ 2.

114. *See id.* art. 15, ¶ 3.

These provisions respect both the modern and anti-adjudication revenue rule definitions in several ways. First, neither country's courts are allowed to adjudicate a tax issue involving the other's tax laws.[115] This is accomplished by first requiring the taxing country to make a final determination that the tax is due.[116] The taxing country therefore retains sovereign power over its tax laws and ensures proper execution of them.[117] Second, the non-taxing country provides collection assistance without involving its court system.[118] In the United States, the executive agencies (including the IRS) collect the tax as if it were owed domestically.[119] There is no right to a hearing, because judicial remedies available in the taxing country would have been exhausted.[120] This ensures the collection process is controlled by the political (rather than judicial) bodies in the non-taxing country.[121] The parties to a collection assistance tax treaty do not opt out of the revenue rule in the true sense—rather, they agree to respect the prohibition on using the others' court system to enforce their tax laws, and accomplish collection goals with the treaty.[122]

A final provision of the treaty requires mention. The collection assistance option is not available when the taxpayer resides in and is a citizen of the country from which assistance is requested.[123] To illustrate, Canada could not request that the United States collect a finally determined Canadian tax from a U.S. citizen residing in Houston, Texas. This provision results from a highly negotiated decision by both countries to exempt

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115. Pasquantino v. United States, 544 U.S. 349, 381 (2005) (Ginsburg, J., dissenting) ("The Protocol does not call upon either nation to interpret or calculate liability under the other's tax statutes . . . .").

116. *See* Protocol Amending U.S.-Can. Tax Treaty, *supra* note 14, art. 15, ¶ 2.

117. Because there is no right of administrative or judicial review, the taxing country can be certain that their judgment will not be overruled. *See id.* art. 15, ¶ 5.

118. *See id.*

119. *See id.* art. 15, ¶ 3.

120. *See id.* art. 15, ¶ 2.

121. *See supra* text accompanying notes 61-65.

122. *See* Att'y Gen. of Can. v. R.J. Reynolds Tobacco Holdings, Inc., 268 F.3d 103, 111 n.5 (2d Cir. 2001) ("As evidenced by a more recent decision of the Supreme Court of Canada, . . . [the revenue rule] is still vigorous in this country in spite of the modern spirit of international co-operation in the field of taxation. In the absence of specific treaty provisions, no matter how conscious and deliberate the tax evasion, there are no judicial or administrative remedies available to the defrauded state or province outside its territorial jurisdiction.") (second alteration on original) (citation omitted) (quoting J.G. CASTEL, CANADIAN CONFLICT OF LAWS 63-64 (1975)).

123. Protocol Amending U.S.-Can. Tax Treaty, *supra* note 14, art. 15, ¶ 8 ("No assistance shall be provided under this Article for a revenue claim in respect of a taxpayer to the extent that the taxpayer can demonstrate that . . . the revenue claim related to a taxable period in which the taxpayer was a citizen of the requested State . . . .").

their citizens from the extraterritorial reach of the other country's collection power.[124] Although the Treaty expressly symbolizes the reciprocal decision to loosen the restrictions imposed by the revenue rule, both countries reserve full protection of the rule for their own citizens.[125] This gap in the tax collection process is bridged with extradition rights in certain cases.[126]

B. *The U.S.-Canada Income Tax Treaty Incorporates Common-Law Revenue Principles and Limits* Pasquantino-*Type Enforcement Measures to Cases Where Foreign Taxes Have Been Finally Determined*

As mentioned above, it is unclear whether the Protocol expressly applies to excise taxes.[127] This section seeks to establish that the courts in *Pasquantino* should have applied the Protocol's *income tax* collection provisions to the *excise tax* in that case.[128] This step should have been taken because the Protocol serves as a written memorial of the revenue rule safeguards owed to Canada by the United States in all tax situations. When a collection action involves income taxes, Canada can rely on express language in the Protocol to ensure its revenue rule rights are protected.[129] In all other tax collection matters, including

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124. *See* Mallinak, *supra* note 2, at 97 (The Protocol "disallows the collection of foreign tax debts or foreign tax judgments against United States citizens. . . . This reluctance may be due, in part, to the reasons that support the revenue rule . . . ."). The argument has been made that the Protocol should be expanded to include collection assistance for judgments against their own citizens and "reciprocal application of each other's tax laws . . . to cover situations where domestic courts cannot exercise personal jurisdiction over the taxpayer." Dodge, *supra* note 1, at 234. It is reasoned that this reciprocal enforcement increases cooperation and would make "tax systems more effective internationally." *Id.* at 235.

125. *See* Mallinak, *supra* note 2, at 97 ("[T]he executive and legislative branches working together could abrogate the revenue rule through treaties yet they are unwilling to do so.").

126. *See* Pasquantino v. United States, 544 U.S. 349, 375 (2005) (Ginsburg, J., dissenting) ("United States citizens who have committed criminal violations of Canadian tax law can be extradited to stand trial in Canada."); *see also* Protocol Amending the Extradition Treaty, U.S.-Can., art. 2(2)(ii), Jan. 11, 1988, S. TREATY DOC. No. 101-17 (providing that "[a]n offense is extraditable notwithstanding . . . that it relates to taxation or revenue . . . .").

127. *See* discussion *supra* Part IV.A.

128. *See* Protocol Amending U.S.-Can. Tax Treaty, *supra* note 14, art. 15, ¶ 9 ("Notwithstanding the provisions of Article II (Taxes Covered), the provisions of this Article shall apply to *all categories of taxes* collected by or on behalf of the Government.") (emphasis added). *But see* Terry Haggerty Tire Co. v. United States, 899 F.2d 1199, 1201 n.3 (Fed. Cir. 1990) (refusing to extend the United States-Canada Income Tax Convention, which involves the "reciprocal taxation of *income*" to include excise taxes).

129. *See* Protocol Amending U.S.-Can. Tax Treaty, *supra* note 14, art. 15, ¶¶ 3, 5 (stating that collection efforts are limited to those that have been "finally determined" and

those that involve excise taxes, Canada can use the Protocol as a reminder of the revenue rule protections that are owed in the absence of a written agreement. Analysis on this point follows below, with discussion of the *Pasquantino* parties' positions on the application of the Protocol and the proper application of the Protocol in *Pasquantino*.

1. Defendants' Position on the Treaty

The Treaty and subsequent Protocol were not ignored by the parties in the *Pasquantino* dispute. Counsel for defendants brought the collection provisions to the Court's attention in its brief:

> In light of the common law rule that nations do not, absent express agreement, assist one another with tax enforcement efforts, the United States has negotiated several bilateral and multi-lateral international agreements governing the extent of tax assistance that this nation is willing to provide to other nations on reciprocal terms.[130]

The brief went on to describe the agreements as "generally sensitive to the difficulties that our courts would face in interpreting foreign tax laws and for that reason commitments of collection assistance generally do not extend to *unadjudicated* tax claims."[131] Highlighting that the Treaty prevents collection assistance unless the other nation certifies the revenue claim as "finally determined," the brief further stated the rule is far from "accidental" and "instead must reflect the considered policy of the political branches of our government" who "have clearly expressed their intention to define and strictly limit the parameters of any assistance given with regard to the extraterritorial enforcement of a foreign sovereign's tax laws."[132]

The petitioner-defendants also noted that the new Article XXVIA does not provide for assistance in collection of a revenue

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that the judgment cannot be administratively or judicially reviewed).

130. Brief for the Petitioners at 46, Pasquantino v. United States, 544 U.S. 349 (2005) (No. 03-725) (citing Dennis D. Curtin, *Exchange of Information Under the United States Income Tax Treaties*, 12 BROOK. J. INT'L L. 35, 35 (1986) (describing tax treaty collection provisions as bilateral decisions to work around the revenue rule); Alan R. Johnson, *Systems for Tax Enforcement Treaties: The Choice Between Administrative Assessments and Court Judgments*, 10 HARV. INT'L L. J. 263, 263 (1969)).

131. Brief for the Petitioners, *supra* note 130, at 46-47 (emphasis added).

132. *Id.* at 47-48 (quoting Att'y Gen. of Can. v. R.J. Reynolds Tobacco Holdings, Inc., 268 F.3d 103, 119 (2d Cir. 2001)).

claim[133] where the "revenue claim relates to a taxable period in which the taxpayer was a citizen of the requested State," here, the United States.[134] They argued that because they were citizens of New York,[135] the United States should be barred from assisting Canada with collection efforts on its claim against them.[136] Moreover, the petitioner-defendants argued that permitting prosecution "would grant Canada greater enforcement assistance than [the U.S.] government would likely receive in return" and thereby violate the Protocol.[137] The petitioner-defendants observed that the United States and Canada have "expressed a policy preference for reciprocity in the level of enforcement of each other's tax judgments and claims."[138] This is established by a provision in the Protocol which states that the United States and Canada agree "to ensure comparable levels of assistance to each of the Contracting States."[139]

2. Prosecutor's Position on the Treaty

The government's prosecutorial team dismissed the defendants' three arguments regarding the Treaty with little fanfare.[140] Buried in the final sentences of its brief, it argued the defendants' position was flawed because "the present prosecution is not designed to serve as a means for Canada to collect taxes on its own behalf."[141] The prosecution stated it indicted the defendants to "prevent criminals based in the United States from using this country as a means of victimizing foreign governments" without affecting "the extent to which petitioners owe taxes to the Canadian government."[142] This, it reasoned, rendered the Treaty wholly inapplicable.[143]

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133. Brief for the Petitioners, *supra* note 130, at 48.

134. Protocol Amending U.S.-Can. Tax Treaty, *supra* note 14, art. 15, ¶ 8.

135. United States v. Pasquantino, 336 F.3d 321, 325 (4th Cir. 2003).

136. *See* Pasquantino v. United States, 544 U.S. 349, 381 (2005) (Ginsburg, J., dissenting) (stating that this provision "would preclude Canada from obtaining . . . assistance in enforcing its claims against the [defendants]"); *see also supra* notes 118-22 and accompanying text.

137. Brief for the Petitioners, *supra* note 130, at 48-49.

138. *Id.* at 48 (quoting Att'y Gen. of Can. v. R.J. Reynolds Tobacco Holdings, Inc., 268 F.3d 103, 121-22 & n.20 (2d Cir. 2001)).

139. Protocol Amending U.S.-Can. Tax Treaty, *supra* note 14, art. 15, ¶ 11.

140. *See* Brief for the United States at 38, Pasquantino v. United States, 544 U.S. 349 (2005) (No. 03-725).

141. *Id.*

142. *Id.*

143. *See id.* ("The domestic criminal prosecution in this case is therefore authorized by the provisions of the wire fraud statute, and nothing in the [Treaty] detracts from that conclusion.").

3. The Court's Response and Why It Is Flawed

The prosecutor's position articulated above is proper in at least one respect: the *Pasquantino* prosecution had, as its principle purpose, the protection of the interstate wires from activity that "victimiz[ed] foreign governments."[144] However, it does not automatically follow that the Treaty or the revenue rule safeguards it memorializes become inapplicable, as Justice Thomas determined in the *Pasquantino* majority opinion.[145] Instead, the Treaty should be examined for purposes of answering questions concerning unadjudicated tax claims in an independent inquiry.

These tax questions arise in a *Pasquantino*-type wire fraud prosecution because the statute requires prosecutors to provide evidence that defendants deprived the victim of money or property.[146] An unadjudicated Canadian tax claim does not sufficiently satisfy this requirement, and Treaty provisions and revenue rule safeguards prevent a U.S. court from adjudicating the claim on Canada's behalf.[147] Instead, prosecutors must defer adjudication to Canadian courts, who must determine as a final matter whether and to what extent taxes are due under Canadian law.[148] Once evidence of tax liability is established, the prosecution can move forward.[149]

As mentioned above, it is unclear whether the Treaty applied as a matter of law to the *excise* tax in *Pasquantino*.[150] Arguably, the Treaty applied as a theoretical matter, because its requirement that taxing nations adjudicate their own tax claims reiterates a basic revenue rule principle.[151] This is the same principle Learned Hand incorporated into his anti-adjudication

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144. *See id.*

145. Pasquantino v. United States, 544 U.S. 349, 358 (2005) ("Neither the antismuggling statute, nor U.S. tax treaties, convince us that petitioners' scheme falls outside the terms of the wire fraud statute. Unlike the treaties and the antismuggling statute, the wire fraud statute punishes fraudulent use of domestic wires, whether or not such conduct constitutes smuggling, occurs aboard a vessel, or evades foreign taxes.") (internal citations and footnotes omitted).

146. *See* 18 U.S.C. § 1343 (Supp. III 2003).

147. *See Pasquantino*, 544 U.S. at 381 (Ginsburg, J., dissenting) (noting the Treaty and revenue rule provisions that prohibit adjudication of the claims of a foreign state).

148. *Id.* at 374.

149. *See id.*

150. *See* U.S.-Can. Tax Treaty, *supra* note 13, art. 15, ¶¶ 1, 9; *see also supra* note 110 and accompanying text.

151. *See* Att'y Gen. of Can. v. R.J. Reynolds Tobacco Holdings, Inc., 268 F.3d 103, 109 (2d Cir. 2001) ("The revenue rule is a longstanding common law doctrine providing that courts of one sovereign will not enforce . . . unadjudicated tax claims of other sovereigns.").

definition of the revenue rule.[152] In sum, the *Pasquantino* court should have cited Treaty requirements as additional support for a revenue rule-based decision to defer adjudication of the excise tax claim to Canadian authorities. This practice should be followed in future Canadian and other foreign excise tax matters which involve criminal prosecution under the wire fraud statute.

V. ROLE OF REVENUE RULE AND TAX TREATIES IN FUTURE INTERNATIONAL INCOME TAX MATTERS

This Part demonstrates how the Treaty will apply in future cases where individuals are prosecuted under the wire fraud statute for *income* tax fraud. Discussion on this point covers the Treaty's modification of the wire fraud statute and the procedural requirements courts should follow when faced with this issue in the future.

A. *In an Income Tax Fraud Case the Treaty Modifies the Wire Fraud Statute as a Matter of Law*

Treaties and their role in the U.S. legal system are often overlooked.[153] In fact, the Treaty was almost ignored by the *Pasquantino* parties in respective court briefings and by the Court itself in its opinion.[154] This result is surprising, considering the great weight accorded to treaties in the hierarchy of legal authority.[155] This subsection seeks to show how the Treaty should apply in future wire fraud cases where the evaded tax is an income tax. In such matters, the Treaty should apply as a matter of law and expressly modify the wire fraud statute.

Article VI of the United States Constitution, the Supremacy Clause, declares: "This Constitution, and the Laws of the United

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152. *See* Moore v. Mitchell, 30 F.2d 600, 604 (2d Cir. 1929) (Hand, J., concurring) (observing that courts are not the proper entity to adjudicate the claims of another state), *aff'd on other grounds*, 281 U.S. 18 (1930).

153. *See* Michael P. Van Alstine, *The Death of Good Faith in Treaty Jurisprudence and a Call for Resurrection*, 93 GEO. L.J. 1885, 1893 (2005) ("The Constitution's description of the legal force of treaties is . . . expansive. Although sometimes famously overlooked, the familiar Supremacy Clause in Article VI includes treaties made by the United States within the 'supreme Law of the Land.'") (footnote omitted); Alex Glashausser, *What We Must Never Forget When It Is a Treaty We Are Expounding*, 73 U. CIN. L. REV. 1243, 1293 (2005) ("[S]tatutes are more relevant to the day-to-day governing of the country and are therefore less likely to be overlooked than treaties.").

154. The only mention of the Treaty in the Court's opinion was mentioned in the dissent. *See Pasquantino*, 544 U.S. at 374, 381 (Ginsburg, J., dissenting). The United States' brief merely dedicated two paragraphs to dismissing the Treaty's applicability. *See* Brief for the United States, *supra* note 140, at 37-38.

155. *See infra* text accompanying notes 156-158; *see also* Van Alstine, *supra* note 153, at 1893-94.

States which shall be made in Pursuance thereof; and all *Treaties* made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land."[156] The Supremacy Clause has been interpreted as placing a treaty "on the same footing, and made of like obligation, with an act of legislation. Both are declared by that instrument to be the supreme law of the land, and no superior efficacy is given to either over the other."[157] "When the two relate to the same subject, the courts will always endeavor to construe them so as to give effect to both, if that can be done without violating the language of either; but, if the two are inconsistent, the one last in date will control the other . . . ."[158]

As conceded by the parties and recognized by the Supreme Court, the Treaty originated in 1980 and was modified by new collection provisions in 1995.[159] This supreme pronouncement of law falls later in time than the wire fraud statute, enacted in 1952,[160] as well as the revenue rule, which has been evolving since 1775.[161] It should therefore follow that any interpretation of the wire fraud statute, in light of the revenue rule, should give effect to the collection provisions in the later adopted Protocol. These provisions include those which require "final determination" of tax liability in Canada and should be respected regardless of whether they conflict with the wire fraud statute or its original intent.[162]

B. *Treaty Requirements Will Apply in Future Income Tax Fraud Cases Prosecuted Under the Wire Fraud Statute*

In a hypothetical income tax fraud prosecution brought in the United States under the wire fraud statute sometime in the future, two provisions should be addressed. First, the U.S. court

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156. U.S. CONST. art. VI (emphasis added).

157. Reid v. Covert, 354 U.S. 1, 18 n.34 (1957) (quoting Whitney v. Robertson, 124 U.S. 190, 194 (1888)).

158. *Whitney*, 124 U.S. at 194; *accord* United States v. Yousef, 327 F.3d 56, 110 (2d Cir. 2003), *and* Square D Co. v. Comm'r, 118 T.C. 299 (2002) (citing *Whitney* for the proposition that "[t]reaties and statutes are viewed under the Constitution as on the 'same footing'").

159. Both parties referenced the Protocol in their briefs. *See* Brief for the Petitioners, *supra* note 130, at 39 n.44 (citing Protocol Amending the Convention Between the United States of America and Canada with Respect to Taxes on Income and on Capital, U.S.-Can., Mar. 17, 1995, 2030 U.N.T.S. 237, art. 15); Brief of the United States, *supra* note 140, at 35-38 (same).

160. *See* 18 U.S.C. § 1343 (Supp. III 2003); *see also* Pasquantino v. United States, 544 U.S. 349, 360 (2005) (stating that Congress enacted the wire fraud statute in 1952).

161. *See* Holman v. Johnson, (1775) 98 Eng. Rep. 1120, 1121 (K.B.).

162. *See, e.g.*, Protocol Amending U.S.-Can. Tax Treaty, *supra* note 14, art. 15, ¶ 3.

should take note of the wire fraud statute, which requires that prosecutors demonstrate that the criminal defendants intended to defraud the victim of money or property.[163] Second, the court should review the Treaty, which requires that unadjudicated Canadian tax claims be finally resolved by Canadian authority.[164] Accordingly, the U.S. court should abstain from making the Canadian tax determination on its own and request that Canada complete the adjudication in the meantime.

To the extent the Treaty and the wire fraud statute are seen as complementary, the U.S. court should accept Canada's certification of the amount and extent of tax liability for purposes of the evidentiary record in the wire fraud case. These steps should still be taken where the court determines the two provisions are found to conflict in some way. This is because the court is required to construe the earlier law (wire fraud statute) with the later law (Treaty) to the extent that the two provisions conflict.[165]

VI. CONSIDERATION OF THE PUBLIC POLICY IMPLICATIONS OF *PASQUANTINO*-TYPE TAX ENFORCEMENT MEASURES

In today's global economy, liabilities for international taxes are almost unavoidable. Businesses and individuals may owe income taxes on income earned abroad, excise taxes on imported goods, and property taxes on land, equipment, intellectual property, or inventory located in a foreign country. In addition, transactions may include special international components to minimize tax liability. As attorneys and taxpayers work together to structure a business arrangement, they often try to take into account all the things that could go wrong. Historically, this has involved measuring the likelihood of liability to the taxing authority to which taxes are owed.[166] In *Pasquantino* however, taxpayers were liable to authorities other than those to whom taxes were owed.[167]

Measuring the likelihood of liability to countries other than those where taxes are due can be problematic. The standards by which these other countries calculate liability may be different,

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163. *See* 18 U.S.C. § 1343.

164. *See* Protocol Amending U.S.-Can. Tax Treaty, *supra* note 14, art. 15, ¶ 3 ("finally determined in accordance with laws applicable").

165. *See* Whitney v. Robertson, 124 U.S. 190, 194 (1888).

166. *See* Henry P. Bubel, *Avoiding Penalties with Tax Opinions after Long Term Capital*, at 701, 740-41 (PLI Tax Law and Estate Planning Course Handbook Series No. 9068, 2006), WL 706 PLI/Tax 701.

167. Pasquantino v. United States, 544 U.S. 349, 352-55 (2005).

and may conform to each country's individual tax collection policies. This creates great uncertainty for taxpayers, attorneys, and parties to business deals. It also increases the transaction cost of doing business. Future court decisions in *Pasquantino*-type enforcement actions should incorporate the revenue rule and any applicable treaty requirements into the procedural template. If not mentioned in a specific treaty, courts should add the requirement that foreign tax authorities certify whether and to what extent taxes are owed in order to minimize the policy problems mentioned above. The additional certainty will allow individuals and their advisors to adapt business decisions to a definable set of rules.

Another thought requires mention. With foreign tax determination shifted to authorities in the taxing country, a *Pasquantino*-type enforcement action, while legal, still might not be a good idea. It is expensive for the accused, costly for the government, and frustrating given the multiple layers of penalties which may accrue. The decision to prosecute, ultimately lying with the executive, should be made after considering policy implications, diplomatic alternatives, and political liability. Only when the integrity of the nation's communications system outweighs the enormous costs of such a prosecution should charges be filed for international tax violations under the wire fraud statute.

VII. CONCLUSION

Despite the bedrock principles of public and private law, the revenue rule, and international law and treaties, the Supreme Court in *Pasquantino* permitted prosecution under the wire fraud statute, which required interpretation of foreign revenue law. U.S. courts can prevent similar future violations of these longstanding principles by waiting for foreign courts to complete tax adjudications before making their own foreign tax determinations. In the meantime, tax practitioners should be mindful of the potential problems and uncertainty associated with measuring the likelihood of liability to countries other than those where taxes are due. The bruises caused by the *Pasquantino* decision will heal if the band-aid—the incorporation of the revenue rule and treaty requirements—is applied in future court decisions.