From the Revenue Rule to the Rule of the “Revenuer”: A Tale of Two Davids and Two Goliaths

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Traditionnellement, les tribunaux refusent d'accueillir les réclamations des gouvernements étrangers, selon la doctrine de la « revenue rule ». Avec l'accélération du rythme du commerce international à la fin du 20e siècle et la prolifération des stratégies d'évasion fiscale outre-frontières, les États ont constaté qu'il était à leur avantage respectif d'inclure, dans les conventions fiscales bilatérales, des dispositions permettant à chaque État de soumettre certaines réclamations fiscales internes aux tribunaux de l'autre État. À un moment où, compte tenu de la mondialisation de l'économie, la reconnaissance réciproque des lois étrangères devant les tribunaux nationaux est devenue chose courante, la « revenue rule » est de plus en plus perçue comme un vestige d'une époque révolue. Une telle réciprocité ne fait que renforcer la dimension internationale de l'application des lois. Des partenariats formels et informels des autorités chargées de l'application des lois opèrent à leur avantage mutuel de la même façon que le commerce international renforce les économies locales. Comme la portée de la législation nationale s'est élargie au point où à peu près chaque opération transfrontalière est régie par une variété de lois internes et étrangères, les autorités chargées de l'application des lois qui sont frustrées par la « revenue rule » évoquent les violations de lois et de règlements criminels ou quasi-criminels dans un effort pour contrer l'évasion fiscale. Dans deux causes avec des circonstances fort différentes, David McNab et David Pasquintino ont été poursuivis devant des tribunaux criminels américains pour une prétendue violation de lois étrangères. L'arrêt Pasquintino portait sur une prétendue évasion des lois fiscales canadiennes. Ces causes ont montré que les autorités canadiennes chargées de l'application des lois peuvent dorénavant contourner la « revenue rule » en demandant aux autorités américaines chargées de l'application des lois de porter des accusations de fraude criminelle ou de conspiration criminelle, même si l'évasion fiscale au Canada est l'activité illégale de prédicat qui constitue le fondement sous-jacent de l'accusation et qu'aucun tribunal au Canada n'a conclu à l'évasion fiscale. Pour que le droit criminel américain s'applique, les autorités chargées de l'application des lois n'ont qu'à montrer qu'il y a eu virement électronique de fonds par l'intermédiaire d’une banque américaine ou qu'Il

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Domestic courts have traditionally refused to enforce the tax claims of foreign governments, under the doctrine known as “the revenue rule.” With the accelerating pace of international trade in the late 20th century and the proliferation of cross-border tax evasion strategies, countries found it mutually advantageous to include provisions in their bilateral tax treaties allowing each treaty partner to assert certain domestic tax claims in the other country’s courts. At a time when, as a result of global trade, reciprocal recognition of foreign laws in domestic courts has become routine, the revenue rule is increasingly perceived as a relic of a bygone era. Such reciprocity only reinforces the international nature of law enforcement. Formal and informal partnerships of law enforcement officials operate to their mutual advantage in the same way that international trade enhances domestic economies. Given that the scope of domestic legislation has broadened to the point where virtually every cross-border transaction implicates a variety of domestic and foreign laws, law enforcement officials who are frustrated by the revenue rule have relied on breaches of criminal or quasi-criminal laws and regulations in an effort to thwart tax evasion. In two cases involving widely differing circumstances, David McNab and David Pasquantino were prosecuted in American courts under U.S. criminal statutes for alleged breaches of foreign laws; the Pasquantino case involved the alleged evasion of Canadian tax laws. These cases have shown that Canadian tax law enforcement officials can now circumvent the revenue rule by asking American law enforcement officials to lay charges for criminal fraud or conspiracy, even though Canadian tax evasion is the predicate illegal activity that forms the underlying basis of the charge and no finding of tax evasion has been made in a Canadian court. To engage American criminal law, enforcement officials only have to show that there was a wire transfer of funds through an American bank, or some other tenuous connection to the United States, as part of what may otherwise be a transaction between Canadians or other nationals. Since there is some difference of opinion as to where the line between lawful tax avoidance and illegal tax evasion should be drawn, Canadian tax advisers and their clients should be concerned about American criminal courts interpreting Canadian revenue laws.

This article examines the historical reasons for the judicial recognition of the revenue rule, the recent case law that has signalled its erosion, and the public policy reasons for and against the continued recognition of the rule in a world of globalized trade, e-commerce,
and widespread international tax treaties. The author concludes, contrary to the recent trend in academic and judicial opinion, that there remain strong policy reasons to maintain the revenue rule with all its force and vigour.

KEYWORDS: TAX COLLECTION AGREEMENTS ■ CANADA-US ■ SOVEREIGNTY ■ INCOME TAX TREATIES ■ GLOBALIZATION ■ EXTRATERRITORIAL

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[I]t is a well-settled principle of international law that one nation’s courts will not enforce the tax claims of another jurisdiction.

In re Guyana Development Corp., 189 BR 393, at 396 (Bankr. SD Tex. 1995)

In an age when . . . instantaneous transfers of assets can be easily arranged, the rationale for not recognizing or enforcing tax judgments is largely obsolete.


I N T R O D U C T I O N
Many people are familiar with the story of David and Goliath, but not everyone remembers its tax aspect: King Saul promised a tax exemption to the father of the man who slew Goliath.1 In modern times, the use of tax exemptions to achieve government policy goals has become so widespread that it has led to the growth of a vast

1 Holy Bible, 1 Samuel 17:25. See also Harold L. Wilmington, Wilmington’s Bible Handbook (Carol Stream, IL: Tyndale, 1997), 155.
tax-planning and tax-avoidance industry—a veritable Goliath, pitted against the Goliath of the state. Revenue authorities in a number of Western democracies have expressed concern, if not outright alarm, about the resulting erosion of their tax base. Some have laid the blame at the door of large law and accounting firms that devise and promote tax-avoidance schemes. One British Treasury official, commenting on the situation in 2004, described tax avoidance as “an urgent and escalating problem in terms of the scale, aggression and speed at which schemes are being marketed [by the big accounting firms],” and observed that such practices could undermine the integrity of the accounting profession. A growing concern in recent years is the proliferation of sophisticated cross-border arrangements designed to divert otherwise taxable income to low-tax or no-tax jurisdictions. Domestic anti-avoidance legislation has proved inadequate to discourage such tax planning or the steady leakage of tax revenues. Many tax enforcement officials have come to believe that they are engaged in a David versus Goliath struggle, and that the only way to succeed in combatting tax avoidance is through cooperation between national revenue authorities. A number of countries have therefore joined forces in developing new mechanisms for the mutual protection of their national tax bases. A recent example is the Joint International Tax Shelter Information Centre (JITSIC), established in 2004 by the tax administrations of Australia, Canada, the United Kingdom, and the United States, to supplement their ongoing efforts to identify and curb cross-border tax-avoidance schemes. In 2006, the Canada Revenue Agency (CRA) reported that this initiative is producing results, and warned tax “evaders” that their activities will not be tolerated:

Tax administrations in many parts of the world are working together to detect and shut down abusive tax schemes. Promoters who believe they can play one country against another in developing tax schemes should beware. . . . Promoters and participants engaged in abusive schemes have routinely been subjected to strict enforcement action by both [the Canadian and US] tax administrations.3

The US Internal Revenue Service (IRS) is a strong advocate of cooperation between national tax authorities. It views JITSIC as “an important part of efforts to combat abusive schemes.”4 As the commissioner of the IRS has observed,

[t]ax administration is being increasingly challenged by globalization, the mobility of capital, the immediacy and fluidity of information and knowledge transfer, and the access individuals and businesses have to sophisticated tax planning and, in some cases,

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4 Ibid.
tax avoidance advice and products. These developments pose a direct challenge to national tax administrations that act in isolation.\(^5\)

The IRS has declared its intention to pursue a strategy of attacking cross-border tax evasion and improving international compliance. With its new focus on coordinated international enforcement, the IRS will target high net worth individuals, business taxpayers, and their advisers, assisted by parallel civil and criminal investigations of the promoters of abusive tax transactions.\(^6\)

A major obstacle to national tax enforcement is the inability of revenue officials to enforce their tax claims across national borders. Domestic courts have long upheld a doctrine known as the revenue rule, refusing to enforce the revenue laws of other countries. In English common law, the original basis for this rule dates back to the 18th century, when international commerce was subject to a policy of economic protectionism; it was in England’s interests to turn a blind eye to violations of foreign tariff laws, in order to maintain a steady flow of imports and prevent encroachment on national revenues by the governments of other nations. Reciprocal treatment of English laws by other countries ensured entrenchment of the revenue rule. So firm was the courts’ adherence to the rule that, when it was to the mutual advantage of trading nations to recognize certain foreign tax judgments, their governments found it necessary to provide for such exceptions in formal treaties or reciprocal domestic statutes.

This approach to cross-border tax enforcement prevailed for many years, providing opportunities for tax avoidance that multinational enterprises and investors, with the help of their professional advisers, have been all too willing to exploit. Large transnational law and accounting firms have been able—at least until recently—to devise aggressive foreign tax-planning schemes, international tax arbitrage transactions, and treaty-shopping plans, secure in the knowledge that domestic laws would not be used to enforce foreign tax laws.\(^7\) Even if a particular treaty or statute recognized certain foreign tax judgments, tax advisers could rely on the precedential interpretation of the applicable domestic statutes in the domestic courts, while the reluctance of foreign courts to enforce extraterritorial tax claims provided an additional level of safety for cross-border tax-avoidance schemes. The resulting loss of tax revenues has raised questions about the rationale for preserving the revenue rule in the 21st century, when tariff protectionism has been largely abandoned as a viable policy for the conduct of international commerce.

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Faced with the rapid growth of the Internet, e-commerce, and the volume of international transactions, courts have recognized the need to give effect to the laws of other countries so that international commerce and law enforcement can proceed in tandem. Thus, the concept of comity—mutual respect for the laws of another country—has become ensconced as a judicial doctrine in international law. Courts appear to be ever more willing to give a narrow interpretation to the revenue rule or even, on occasion, to set it aside altogether. In this respect, two recent decisions of the US courts—United States v. McNab⁸ and Pasquantino v. United States⁹—are of particular significance. In these cases, the courts extended the doctrine of comity, not merely recognizing foreign laws, but adopting the interpretation of those laws by foreign enforcement officials to support the prosecution of charges brought under US criminal statutes. As a result of these decisions (and in particular Pasquantino, which involved evasion of Canadian tax laws), Canadian tax enforcement officials may be able to bypass Canadian courts and have their interpretation of Canadian revenue laws, and their view of cross-border tax evasion, enforced in American courts in the guise of enforcing American criminal legislation. In other words, they may have found a way to use the penal consequences of American legislation to deter what they consider to be tax evasion, instead of applying for extradition and proceeding to a Canadian trial. It is likely that US prosecutors will be open to collaboration with Canadian tax authorities, given the public statements of support for international cooperation in combatting tax avoidance issued by the CRA and the IRS.

While many may welcome this development as part of the process of globalization, and necessary to protect the international tax base from being ravaged by multinational enterprises and their advisers, here it is argued that allowing enforcement officials to pursue the application of domestic tax laws through criminal prosecution in a foreign jurisdiction vitally implicates national sovereignty, democratic accountability, and the protection of our personal rights and freedoms. Mechanisms for the exchange of tax information and limited recognition of domestic tax judgments already exist under a number of tax treaties—including the Canada-US income tax convention¹⁰—and these agreements, negotiated between sovereign states, provide the constitutional framework for cross-border tax enforcement. It is suggested in this article that underlying the issue of tax avoidance, there is another, more fundamental challenge to be addressed: the preservation of the rule of law within a national democratic framework in the face of the increasing influence of unelected officials (in informal American usage, “revenuers”) and the danger that, for reasons of expediency, they are overriding or circumventing the elected branches of government.

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⁸ United States v. McNab, 331 F. 3d 1228 (11th Cir. 2003).
The growing reliance of governments on international law enforcement networks has been described as “a key feature of the world order in the twenty-first century.” While these networks may as yet be “under-appreciated, under-supported, and underused,” governments “increasingly exchange information and coordinate activity to combat global crime and address common problems on a global scale.” When courts recognize the use of such information in enforcing foreign tax claims, the judicial doctrine of comity is extended to “expand the regulatory reach and in effect allow governments to close the gaps between their jurisdictions.” If international law enforcement networks are considered to “contribute to world order by helping nations [to] enforce law [that] they have individually or collectively determined to serve the public good,” ultimately (it is argued) they will dominate international relations. Democratic sovereignty, although continuing to act as the “junior partner” in a confederation of international states, will be checked by courts and bureaucratic actors with a globalized sense of obligation; as a result, perhaps even legislators will transcend the parochialism of specifically representing their constituents. In that case democracy and democratic accountability will cease to be issues.

Given these trends, and the importance we place on the privacy of tax information, it is necessary to consider anew the underlying principles governing the extraterritorial application and enforcement of tax laws. Clearly, the world today is quite different from that in which the revenue rule was conceived. In the “new world order,” where revenue authorities are engaging in various formal and informal arrangements to enforce domestic laws—in effect, presupposing the existence of an international tax order and an international tax administration—the judiciary will increasingly be called upon to re-examine the validity of traditional common-law principles.

Recent case law—notably the McNab and Pasquantino decisions—indicates a shift away from the revenue rule and toward an expanded concept of comity in adjudicating tax matters. Indeed, McNab and Pasquantino (which have been dubbed “the two Davids,” in reference to the appellants, David McNab and David Pasquantino) raise the possibility that the revenue rule could be replaced by “the rule of the revenue,” substituting an interpretation of the law favoured by enforcement officials

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12 Ibid.
14 Ibid., at 1272.
15 Ibid., at 1302.
for the will of the legislature as expressed in domestic statutes and interpreted by domestic courts. As a result, tax enforcement officials may be encouraged to engage in some forum-shopping of their own, in an effort to gain a favourable interpretation of domestic tax legislation, and to use the criminal law as a device to deter tax practices that they consider to be offensive, unlawful, or abusive.

This article will explain how this shift in judicial doctrine has come to pass and explore its far-reaching implications for tax practitioners, taxpayers, and citizens in general. I will argue that the decisions in “the two Davids” raise a challenge not only to the Goliath tax-avoidance industry but to the Goliath of the modern democratic nation-state as well.

**TAX SOVEREIGNTY AND INTERNATIONAL COMMERCE: A HISTORICAL OVERVIEW**

*Where the state is, there is the power to tax; for rulers cannot rule without taxation.*


The notion of tax sovereignty is deeply embedded in the history of Western democracies. Indeed, several defining events in the evolution of the modern nation-state had their origins in disputes over the right to levy taxes. By the end of the Middle Ages, the feudal system had evolved into a myriad of secular and ecclesiastical authorities, which shared the tax base by way of a variety of levies, tithes, tariffs, and other revenue laws. The conflict that arose between these competing interests was resolved by the Peace of Augsburg of 1555 and the Peace of Westphalia of 1648. Together these treaties formally recognized the division of the Holy Roman Empire into autonomous fiefdoms or nation-states, each ruled by a prince who held supreme authority over all forms of taxation. Thus, the modern concept of sovereignty was born: in any given territory or nation-state, there was one sovereign authority, which had the exclusive power to govern that territory, independent of any other sovereign state, whether that power be vested in a monarch, a dictator, or a constitutional democracy.

The creation of the nation-state effectively eliminated internecine disputes over the revenue base. In their relations with each other, sovereign states asserted their tax jurisdiction by imposing customs duties and tariffs on imports. Thus, when the

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17 To cite just three examples, the dispute between the feudal lords and King John in England over the king’s right to levy taxes in order to maintain a national army resulted in Magna Carta (1215); the king’s right to tax without the approval of Parliament was an important cause of the English Civil War (1642-1648); and the English Parliament’s imposition of taxes on the North American colonies (“taxation without representation”) sparked the American Revolution in 1765. See Peter Leyland, *The Constitution of the United Kingdom: A Contextual Analysis* (Oxford: Hart Publishing, 2007), 9-11 and 20.

English courts developed the revenue rule, the intent was to protect British privateers from foreign taxation, in a world where mercantilism and commercial protectionism were the order of the day. However, justification of the revenue rule was often expressed in terms of the protection of sovereign interests.19

As sovereigns consolidated their rule over their respective territories, it became increasingly clear that a nation’s security depended on the strength of its economy. The costs of maintaining an army, a navy, and civil militias or police—which were essential to the protection of national interests at home and abroad—were paid out of domestic tax revenues, and those revenues depended on the health of domestic commerce. It also became apparent that international trade in goods and technology encouraged domestic commerce and provided opportunities for economic growth, contributing to the flow of revenues to the state. Thus, sovereign nations began to view international trade not as a threat, but rather as a means of enhancing their power. In this respect, they were influenced by Adam Smith’s Wealth of Nations, published in 1776. Smith promoted the idea that more liberalized trade between nations would strengthen their domestic economies, whereas protectionism inhibited economic growth. To protect domestic commerce and the national revenue base, governments should rely on the rule of law.

As policies of economic protectionism yielded to economic cooperation founded on mutual self-interest, international trade and the flow of revenues to national treasuries steadily increased. At the same time, governments recognized the need for international rules to govern the conduct of trade between sovereign states. For trade to flourish, payment in exchange for goods and property or services must be assured; inability to collect monies owed resulted in the loss, not only of income to traders, but also of tax revenues to the government. Accordingly, to secure the mutual benefits of trade, in the late 19th century, sovereign states began to enter into bilateral and multilateral trade agreements (“friendship, commerce, and navigation” treaties). These agreements were the predecessors to today’s tax treaties, which establish the limits of taxing powers between autonomous states where competing claims may arise.

In the early 20th century, the growing complexity of international commerce made it difficult for countries to assert their right to tax on the basis of traditional definitions of sovereign authority. Cross-border transactions, business arrangements, and ownership structures often involved multiple jurisdictions, each of which might have a legitimate claim to a share of the associated tax revenues. Countries therefore began to negotiate rules for determining tax jurisdiction and the equitable allocation of tax revenues arising from commercial activities conducted within their respective borders. To assist the process of formulating these rules, the leading industrial nations established multilateral organizations—notably the League of Nations and the Organisation for Economic Co-operation and Development (OECD)—which provided a forum for negotiation as well as assistance in drafting treaty provisions. The model

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tax conventions resulting from these cooperative efforts, and particularly the OECD model convention and commentary in their various iterations, have provided the framework for the great majority of tax treaties now in effect around the globe.20

Tax treaties assure the signatories of reciprocal treatment in tax matters and thus establish a codified exception to the revenue rule. The treaty process ensures the preservation of sovereignty and the protection of citizens’ rights. While there are differences in the procedures followed by particular countries, according to the requirements of the country’s constitution, generally treaties are considered to be legislated acts; they differ from other laws only in that a treaty, being a contract between nations, is subject to the mutual consent of the governing bodies of those nations. In Canada, the authority to initiate treaty negotiations resides in the executive branch (the governor in council, or Cabinet); in the United States, it resides with the president and administration. However, approval of the draft treaty agreed upon by the negotiators is in the hands of the legislature—in Canada, Parliament; in the United States, the House of Representatives—subject to the consent of the Senate.21 Treaties thus reflect government policy in respect of competing jurisdictions, and ensure that any accommodation of another country’s tax law is granted in accordance with the rule of law.

Treaties narrow the scope of application of the revenue rule by the courts, but—at least in theory—they also reinforce that doctrine as a limitation on judicial recognition of foreign tax laws. The problem is that the world has become much more complicated in the last 40 years, and the roles of the separate branches of government in resolving issues of tax jurisdiction have become blurred.

Advances in technology since the 1960s have stimulated a huge increase in economic activity in all sectors, all over the world. Leading industrialized nations have seen their revenues from international trade skyrocket.22 At the same time, the


21 In Canada, the executive can enter into treaties without the consent of the legislature; however, no treaty can impinge on the rights and obligations of Canadians without enabling legislation passed by Parliament and approved by the Senate: see Baker v. Canada (Minister of Citizenship and Immigration), [1999] 2 SCR 817, at paragraphs 79 and 80; and Suresh v. Canada (Minister of Citizenship and Immigration), [2002] 1 SCR 3, at paragraph 60. If the subject matter of a treaty falls within the constitutional responsibility of a province, the implementing legislation must be passed by the provincial legislature: see Attorney-General for Canada v. Attorney-General for Ontario, [1937] AC 326, at 347 (PC). The Canadian constitutional process for tax treaties is reviewed in Chua v. MNR, [2000] 4 CTC 159 (FCTD). For discussion of the US constitutional process, see infra note 39 and the accompanying text.

structures and schemes for conducting cross-border commerce have become even more complex, creating serious tax collection problems for revenue authorities. Inevitably, the number and complexity of tax treaties have grown exponentially as countries have tried to keep pace with these developments.

Treaty negotiations are often difficult and protracted, and may involve multiple parties; as a result (to borrow from the lexicon of law and economics), the “transaction costs” of entering into and constantly revising treaties to keep up with trade and technology improvements are relatively high.\(^{23}\) Theory states that, where gaps occur, private law should step in by providing for judicial discretion; that is, domestic courts may choose to recognize and enforce foreign laws in the hope of reciprocal treatment for transactions conducted abroad, rather than wait for their government to negotiate the appropriate treaty apparatus. Where international transactions are few, there is little need for treaties—and little hope of reciprocity—because the opportunities for reciprocation are few and far between. However, as the volume of international transactions increases, there is a corresponding increase in the motivation of the courts to “follow the golden rule”—or, in the language of game theory, to employ a “tit-for-tat” strategy. In international law, this policy of treating foreign laws as one would wish domestic laws to be treated in another jurisdiction is called comity. The advantages of this approach are clear: the international cooperation required for international trade is fostered by a mutual respect for foreign laws;\(^{24}\) and when the courts of trading nations respect foreign laws and judgments, the laws governing international trade become more certain. The benefits of trade can thus be obtained without requiring formal treaty negotiations to secure reciprocity.\(^ {25}\) Sovereignty is preserved by the revenue rule, which serves as a constraint on comity: domestic recognition of foreign laws and judgments ceases at the point where enforcement of a foreign claim would allow a foreign government, directly or indirectly, to collect foreign taxes from the domestic tax base. The problem in drawing the line between a general rule of comity and the exception mandated by the revenue rule has two aspects. First, what is an “indirect” form of foreign tax collection? And second, what are the boundaries of the domestic tax base in a global economy increasingly dominated by e-transactions? As we shall see, these issues are a central concern for international tax theorists and tax practitioners, and will likely remain so for some time to come.

Further complications arise in the application of comity where the tax regimes and judicial views prevailing in the two states reflect divergent policies, as is the case with Canada and the United States. Certainty in the rules governing cross-border commerce is particularly important for Canada in its dealings with the United States.


\(^{24}\) Judicial comity thus serves as a lubricant for international relations. See Anne-Marie Slaughter, “Court to Court” (1998) vol. 92, no. 4 *The American Journal of International Law* 708-12, at 708.

Close to 80 percent of Canadian exports are shipped to the United States, representing about 35 percent of Canada’s gross domestic product. Despite attempts to diversify to other export markets, the draw of the large market to the south persists, owing to the lower cost of transportation and telecommunications, the low cultural barriers to entry, and the extent of related-party production and trade with American companies. In other words, Canada and the United States have a tightly integrated economic relationship, in which multinational corporations and cross-border financing play a substantial role.

At the same time, there are significant differences in the policy choices made by the Canadian and US governments, which affect the application of tax laws in the two countries. It is widely believed that Canada has a very different social model than the United States, and that among the enduring elements of this difference, Canada has a more even distribution of both earnings and after-tax (disposable) income. The narrower distribution of earnings in Canada is attributed to greater unionization of the workforce, somewhat higher minimum wages, and a smaller gap between the middle and upper ranges of the earnings spectrum. The more even distribution of after-tax incomes, and lower rates of poverty in Canada compared with the United States, reflect the impact of a more “generous” system of transfers acting upon the distribution of market income. Publicly funded services are also more widely available in Canada than in the United States, reducing dependence on market income for some basic needs (notably health care). In short, there is a widespread belief in Canada that greater income equality has sustained better social outcomes in terms of health, crime, and educational attainment—in other words, that Canadians are willing to accept higher taxes in exchange for more government services, while Americans prefer lower taxes and less government intervention.

In a global economy, where there are divergent tax burdens, there are incentives to create tax-minimization schemes that will direct taxable transactions to a jurisdiction with a lower effective tax rate—in our case, away from Canada and toward the United States. Thus, there is a strong motive for aggressive tax planning to take advantage of the differing tax rates between countries. Added to the equation is the factor of differing levels of efficacy between countries with respect to tax collection. Law enforcement in America is reputed to be quite aggressive and effective. Assuming that the long reach of the IRS is not a myth, Canadian tax officials may be encouraged to ask the US “revenuers” to collect unpaid taxes on their behalf, if the United States is willing to bear the expense of prosecuting foreign claims in its domestic courts.

Finally, different jurisdictions have different judicial systems. Even those with similar systems have differing views about the interpretation of revenue laws and revenue law enforcement. Consider the divergent views of the supreme courts in Canada.

and the United States on how to interpret tax laws and conceptualize tax avoidance. The Supreme Court of Canada has taken a restrictive view of both common-law doctrines and legislative provisions that attempt to eliminate aggressive tax-avoidance schemes. By contrast, the US Supreme Court, and lower courts as well, have proved quite receptive to common-law doctrines and legislative provisions that are designed to curb such schemes.

These differences exacerbate the enforcement problems faced by Canadian revenue officials. Given the task of ensuring tax compliance in a high-tax jurisdiction with an avoidance-tolerant judiciary, what can the CRA do to deter the “paper entrepreneurs” in law and accounting firms from thwarting its tax collection efforts?

This article suggests that the CRA will put the US decisions in McNab and Pasquantino to good use by employing a form of tax jurisdiction arbitrage to enforce its views of Canadian revenue laws in foreign courts, and in the process circumvent domestic legislative and judicial safeguards. It is argued that “the two Davids” pose a serious threat that revenue officials will be able to forum-shop to impose their dictates where domestic courts will not allow them to go, foreshadowing the rule of the “revenuer”—unless something is done soon. To understand why this opportunity has arisen at this particular time, we need to examine the traditional rationale for the revenue rule and the arguments against it.

**THE “STRONG FORTRESS”: THE TRADITIONAL ARGUMENT FOR THE REVENUE RULE**

Whether influenced as schoolboys by English history classes about the need for trade by “the island nation,” the evils of protectionist tariffs, and the privateering exploits of Sir Francis Drake, or by a fondness for tea, English judges have not traditionally

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28 For example, see Stubart Investments Ltd. v. The Queen, [1984] 1 SCR 536; and The Queen v. Canada Trustco Mortgage Co., [2005] 2 SCR 601. The Supreme Court succinctly expressed the prevailing judicial attitude to tax avoidance in Shell Canada Ltd. v. The Queen, [1999] 3 SCR 622, at paragraph 45: “[A]bsent a specific provision to the contrary, it is not the courts’ role to prevent taxpayers from relying on the sophisticated structure of their transactions, arranged in such a way that the particular provisions of the Act are met, on the basis that it would be inequitable to those taxpayers who have not chosen to structure their transactions that way.” The court’s continued adherence to this view is evidenced by its decision in Canada Trustco, the first case in which it was called upon to consider the application of the general anti-avoidance rule (GAAR) (section 245 of the Income Tax Act, RSC 1985, c. 1 (5th Supp.), as amended). In Canada Trustco, the court all but ignored a legislated amendment to address tax avoidance, and applied the common-law principles that it had expounded in Stubart as if GAAR had no effect on how tax-avoidance schemes should be viewed. For commentary on the implications of the decision in this case, see “Policy Forum: Canada Trustco and Beyond” (2005) vol. 53, no. 4 Canadian Tax Journal 1007-52.


taken a dim view of domestic commercial ventures conducted in breach of foreign revenue laws. In the 18th century, for example, smuggling contracts that involved the illegal export of Portuguese gold in breach of Portuguese law, the importation of tea in violation of a tea tax, or the circumvention of French customs duties on durable goods were not considered to offend the public policy of England; therefore, these contracts were not void on the ground of illegality or as being contrary to public policy. As Lord Mansfield put it, evasion of a foreign tax is irrelevant because “no country ever takes notice of the revenue laws of another.” This is the traditional rationale for the doctrine of non-recognition that we call the revenue rule. The rule was thought to be universal because, just as English courts disregarded foreign tax laws in examining the validity of contracts, the same was also true of foreign courts with respect to their treatment of English tax laws. The refusal of England and its trading partners to recognize each other’s revenue laws created a vicious circle that has perpetuated the revenue rule throughout the modern era.

When we move from private international law to the recognition of foreign legislation at the behest of foreign public authorities, additional considerations buttress the continuation of the revenue rule—for example, the protection of sovereignty. In a 1729 decision, Attorney General v. Lutwydge, the English Exchequer Court refused to enforce import duties on tobacco sold at Dumfries, Scotland because an English court would not enforce a foreign tax obligation against an Englishman. Similarly, state governments in America long refused to recognize estate or other tax claims of neighbouring states, considering such claims to be “foreign” overreaching into their sovereign jurisdiction.

As discussed above, by the 20th century, countries often found that it was in their mutual interest to include provisions in their domestic statutes or treaties agreeing to reciprocal recognition of domestic judgments; however, such provisions did not extend to the enforcement of foreign tax laws. The willingness of sovereign states to agree to formal recognition of domestic judgments served notice of a competing public policy concern that weighed against the revenue rule, expressed in the principle of comity. As applied by the courts, comity means that a domestic court should show some respect for the laws of foreign states. It is neither an absolute obligation

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31 Boucher v. Lawson (1734), 95 ER 53 (KB).
32 Holman v. Johnson (1775), 98 ER 1120 (KB).
33 Planche v. Fletcher (1779), 99 ER 164 (KB).
34 Holman v. Johnson, supra note 32, at 1121.
35 (1729), 145 ER 674 (Ex. Ct.). Despite the Act of Union of Great Britain, enacted in 1707, for English tax purposes Scotland remained a foreign jurisdiction.
36 This practice was stopped by the US Supreme Court’s decision in Milwaukee County v. White Co., 296 US 268 (1935), which held that the “full faith and credit” provision of the US constitution required sister states to recognize each other’s tax laws and judgments (see infra note 175).
37 See, for example, Foreign Judgments (Reciprocal Enforcement Act) 1933 (UK), 1933, c. 13; S.B. section 1(2) (1977) in the State of Oregon; and virtually all US tax treaties.
nor a matter of mere courtesy or goodwill. While no law has any legal effect beyond the sovereign jurisdiction in which it was enacted, the administrative need for finality to litigation, combined with the hope of reciprocal treatment in other sovereign states, encourages a judicial policy of recognizing foreign judgments and laws.\textsuperscript{38} However, the courts have traditionally held that comity cannot overcome the revenue rule. Indeed, the option of providing for a negotiated exception to the revenue rule in treaties or reciprocity legislation has lent additional weight to the arguments in favour of its preservation by the courts.

The authority of the executive and legislative branches of government to bargain for and legislate the recognition of foreign tax laws and judgments, through treaties or reciprocity statutes, has been a mainstay of the United States’ support of the revenue rule. Enforcement of a foreign tax claim in an American court, in contravention of the revenue rule and in the absence of reciprocal recognition through a treaty or domestic legislation, would intrude on the treaty-making authority of the executive branch\textsuperscript{39} and obstruct the government’s policy objectives as reflected in its treaties. In addition, judicial recognition would provide no assurance that the United States would enjoy a reciprocal privilege in the foreign country’s courts, and would deprive the executive branch of the leverage to secure such reciprocity through negotiation.\textsuperscript{40} As the US Department of Justice has emphasized, “the revenue rule has served as the foundation for United States treaties,”\textsuperscript{41} and thus should be respected by the courts.

\textsuperscript{38} See \textit{Hilton v. Guyot}, 159 US 113 (1895); and \textit{Johnston v. Compagnie Generale Transatlantique}, 152 NE 121 (NYCA 1926).

\textsuperscript{39} The US constitution imposes constraints on the power of the executive to enter into tax treaties through the powers accorded to the legislative branch (Congress): before a treaty can take effect, it must be ratified by the Senate in consultation with the House of Representatives (Constitution of the United States of America, article II, section 2: “[the President] shall have the Power, by and with the Advice and Consent of the Senate, to make Treaties, provided two thirds of the Senators present concur”). In practice, Congress has traditionally acted on revenue treaties concluded by the executive branch. (This summary of the US constitutional framework and arguments in support of the revenue rule is based on Bill Maurer, “Revenue, Rule, and the Revenue Rule: Toward an Anthropology of Taxation” (unpublished draft), at 1-2, 5, and 9 (online: http://law.usc.edu/assets/docs/Maurer.pdf ).

\textsuperscript{40} These arguments served as the ratio in \textit{Her Majesty, Queen in Right, etc. v. Gilbertson}, 597 F. 2d 1161 (9th Cir. 1979), a decision of the United States Court of Appeal that denied British Columbia’s claim for recovery on a judgment of taxes owing under provincial logging tax legislation. The court found that Canada’s tax treaty with the United States did not provide for reciprocal recognition of tax judgments; and that Canadian common-law courts consistently applied the revenue rule to prevent enforcement of American tax judgments. Therefore, in the court’s view, there was no prospect of reciprocal treatment of American tax laws and hence no basis for the application of comity (reciprocity being the hallmark of comity, if not a strict requirement for its application: \textit{United States of America v. Harden}, infra note 53). The \textit{Gilbertson} case arose before Canada and the United States amended their tax treaty to include a limited recognition provision: see infra note 140 and the accompanying text, and the appendix to this article.

\textsuperscript{41} Brief for the United States as amicus curiae filed by the US attorney general in \textit{Attorney General of Canada v. R.J. Reynolds Tobacco Holdings Inc.}, infra notes 74 and 85, at 11.
The leading American case in support of the revenue rule is the 1929 decision in *Moore v. Mitchell*.42 The appellate court in this case set forth the following reasons for applying the revenue rule in dismissing an attempt by Indiana to collect estate taxes from a New York resident:

1. It is repugnant to domestic sovereignty for a foreign state to try to enlist a domestic court to collect foreign taxes.
2. Revenue laws are analogous to penal laws and, as such, can be enforced in the foreign jurisdiction only through extradition. The domestic state is jealous of its sovereignty over such sensitive matters of public law. The courts should therefore not, directly or indirectly, assist foreign authorities seeking to extend their jurisdiction beyond their borders.
3. The domestic courts only have jurisdiction to enforce domestic taxes.43
4. In determining whether to apply foreign laws domestically, the domestic court always has to confirm that those laws are consistent with the public policy of the domestic state:

   This is not a troublesome or delicate inquiry when the question arises between private persons, but it takes on quite another face when it concerns the relations between the foreign state and its own citizens or even those who may be temporarily within its borders. To pass upon the provisions for the public order of another state is . . . beyond the powers of a court; it involves the relations between the states themselves, with which courts are incompetent to deal. . . . 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.44

In other words, the enforceability of a foreign state’s tax laws is a matter left to the executive’s treaty-making powers, subject to legislative ratification of such treaties, and not to revenue courts. Determining whether a foreign revenue law is contrary to domestic public policy has foreign relations implications that the judiciary has neither the competence nor the authority to address.

The English courts have firmly supported the revenue rule in the face of tax claims asserted by Australian,45 Greek,46 Indian,47 Dutch,48 and Irish49 authorities.

42 30 F. 2d 600 (2d Cir. 1929).
43 Ibid., at 601-2 (per Manton J).
44 Ibid., at 604 (per Hand J).
46 King of the Hellenes v. Brostrom (1923), 16 Lloyds LR 190 (KB).
48 Queen of Holland v. Drukker, [1928] 1 Ch. 877 (Ch. D.).
49 Buchanan, Ltd. and Another v. McVey, [1954] Ir. 89 (SC).
In the *Government of India* case, Lord Keith confirmed that national sovereignty precluded the use of domestic courts as an instrument for the extension of a foreign jurisdiction’s tax collection powers.\(^{50}\) Lord Somerville offered a further rationale to support the revenue rule: Why should a foreign jurisdiction be allowed to avoid the considerable administrative costs and difficulties of tax assessment and collection, and shift these burdens to the domestic jurisdiction by means of having its claim adjudicated in the domestic court?\(^{51}\) In the *Buchanan* case, the court emphasized the sensitive political issues that underline the importance of the revenue rule:

Nor is modern history without examples of revenue laws used for purposes which would not only affront the strongest feelings of neighbouring communities, but would run counter to their political aims and vital interests. Such laws have been used for religious and racial discrimination; for the furtherance of social policies and ideals dangerous to the security of adjacent countries; and for the direct furtherance of economic warfare. So long as these possibilities exist, it would be equally unwise for Courts to permit the enforcement of the revenue claims of foreign States.\(^{52}\)

In Canada, the leading case in support of the revenue rule is the 1963 decision of the Supreme Court of Canada in *United States of America v. Harden*.\(^{53}\) In that case, the taxpayer consented to judgment in an American court in respect of her liability for US income tax. The US government then tried to enforce its claim against the taxpayer in Canada, on the basis that it was a judgment and not a tax claim, or, in the alternative, that it arose in respect of a contract between the parties, and was enforceable as such. The Supreme Court of Canada held that a foreign state cannot escape the application of the revenue rule, which prevents a court from directly or indirectly enforcing the revenue laws of another country, by using a judgment in its own courts to bring suit in Canada on that judgment. The court found that the claim asserted by the US government remained a claim for taxes. The court also held that any argument that the claim asserted was simply for the performance of a contract must fail for the same reason. The domestic court was concerned not with form but with substance, and if it could properly be said that the defendant made an agreement, it was simply an agreement to pay taxes that, under the laws of the foreign state, she was obligated to pay. Neither the foreign judgment nor the agreement did more than make certain the fact and the amount of the defendant’s liability to the plaintiff. The nature of the liability was not altered: it was a liability to pay income tax. Further, the court noted that it lacked jurisdiction to enforce foreign tax

\(^{50}\) Supra note 47, at 511-12.

\(^{51}\) Ibid., at 514.

\(^{52}\) *Buchanan*, supra note 49, at 107.

\(^{53}\) *United States of America v. Harden*, [1963] SCR 366. See also *Re Dwelle Estate* (1969), 69 WWR 212 (Alta. SC). These cases preceded the addition of an assistance-in-collection article to the Canada-US treaty, which could have allowed the US government to pursue its claim through the treaty mechanism: see the text infra at note 140 and the appendix to this article.
laws. In the court’s view, the decision to recognize another state’s tax regime is a matter of foreign policy, similar to the decision to recognize the criminal sanctions of another state. As the US court had stated in Moore v. Mitchell,

[r]evenue laws affect a State in matters as vital to its existence as its criminal laws. No court ought to undertake an inquiry which it cannot prosecute without determining whether those laws are consonant with its own notions of what is proper.54

Moreover, citing Government of India, the court agreed that

it would be remarkable comity if State B allowed the time of its courts to be expended in assisting in this regard the tax gatherers of State A.55

Thus, for many years, the English, US, and Canadian courts staunchly upheld the revenue rule, despite attempts to argue that tax laws were not analogous to penal laws and that, for reasons of comity, the application of the revenue rule between friendly countries ought to be mitigated. Such arguments were dismissed as “frail weapons with which to attack a strong fortress.”56 As we shall see, recent challenges to the revenue rule suggest that the fortress is no longer as strong, nor the weapons as frail, as they used to be.

THE REVENUE RULE UNDER SIEGE

Questions have been raised about the efficacy of traditional restrictions on the enforcement of foreign tax laws, given growing concerns over the loss of tax revenues through cross-border commerce and investment. The issue has become more pressing in recent years as a result of a combination of factors: the proliferation of multinational enterprises with interests in many jurisdictions; the multiplicity of taxpayers’ contacts with different countries (even in the context of a single transaction); the blurring of the distinction between foreign and domestic transactions as a result of the Internet; and the inadequacy of domestic information systems to monitor and trace the movement of funds through the conduct of e-commerce. Frustrated by the complexity of this environment, and by frequent and rapid changes in the means of conducting business across borders, revenue authorities have increasingly turned to the development of interjurisdictional mechanisms, outside the established process of treaty negotiation (with its constitutional safeguards), to address the perceived threat to the domestic tax base. Through multilateral organizations such as the OECD and the Financial Action Task Force of the Group of Seven (G7) nations,57

55 Harden, supra note 53, at 372, quoting Government of India, supra note 47, at 514.
56 Government of India, supra note 47, at 506, per Viscount Simonds.
57 The Financial Action Task Force is an international watchdog group formed by the G7 countries in 1989 to fight money laundering.
government representatives have worked together to design and put in place various instruments, agreements, memorandums of understanding, and cooperative practices—all adopted without parliamentary (or congressional) review and consent—to combat the erosion of tax revenues through international commerce. These formal mechanisms have evolved into bureaucratic arrangements between revenue authorities for information sharing and other anti-avoidance strategies (the creation of JITsIC being one recent example).

In parallel with these developments on the administrative front, the judiciary in both Canada and the United States has shown a growing inclination to favour comity over the revenue rule; in the McNab and Pasquantino cases, as we shall see, the US courts went even further in lowering the traditional barriers to cross-border enforcement by revenue officials. The challenge to the revenue rule has been noted in the academic literature, and various arguments have been made for narrowing its application or discarding it altogether. Here, I will assess the merits of these arguments, and then review recent US and Canadian cases in which the courts have chosen to depart from the revenue rule.

**Criticisms in the Academic Literature**

Prior to the McNab and Pasquantino decisions, there was little discussion in the academic literature on the continuing relevance of the revenue rule. Those decisions appear to have prompted a re-evaluation of traditional restrictions on cross-border enforcement and the application of comity in tax matters. Generally, the weight of opinion has fallen on the side of comity, with some writers taking a strongly critical view of the revenue rule.

In a 1992 article, Barbara Silver argues that the revenue rule is an obsolete doctrine, founded in a nationalist, mercantilist age and having no basis other than historical precedent to support it. In her view, the need for the revenue rule as an assertion of sovereignty has long since passed; the demands of international commerce have resulted in the recognition of foreign laws and judgments as a matter of

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58 In the late 1980s, for example, the OECD conducted a series of studies and discussions among its members on the problem of international tax avoidance; and in recent years, OECD members have cooperated in a number of other initiatives, including the development of guidelines for transfer pricing within multinational enterprises, measures to address the problem of tax havens and “harmful” tax practices, and a model agreement for tax information sharing between countries: see, respectively, *Transfer Pricing for Multinational Enterprises and Tax Administrations* (Paris, OECD) (looseleaf); *Harmful Tax Competition: An Emerging Global Issue* (Paris: OECD, 1998) and subsequent progress reports under the title *The OECD’s Project on Harmful Tax Practices*; and *Agreement on Exchange of Information on Tax Matters* (Paris: OECD, April 2002). The OECD has also initiated studies on e-commerce issues, with a view to updating the model tax convention and commentary, and it is working with the G7’s Financial Action Task Force on money laundering.

course. While Silver allows that an exception may still be required for the enforcement of foreign criminal laws, she maintains that there are no longer policy grounds for extending the exception to tax laws. Therefore, she argues, the revenue rule should be drastically altered to recognize foreign tax judgments (if not tax claims). In her view, such recognition would promote comity (reciprocal treatment) without interfering with the sovereignty of the foreign jurisdiction.

Silver expressed these views before Canada and the United States amended their tax treaty to provide for limited recognition of their respective tax judgments.\(^\text{60}\) The fact that this exception to the revenue rule was negotiated, rather than judicially imposed for reasons of comity, provides one of the strongest reasons for continuing the revenue rule: to ensure that sovereign states, and their democratically elected governments, retain the ultimate decision-making authority over when, and under what circumstances, it is in their best interests to recognize the tax laws of another jurisdiction. When countries have tax treaties in place and (like Canada and the United States) are comfortable with the process and results of each other’s tax judgments, and with the methods by which these judgments may be enforced domestically, they can amend their treaties accordingly. Unlike most areas of the law, tax laws are a predominant part of any nation’s public policy agenda, and thus are likely to be uppermost in the formulation of foreign relations policies. Therefore, it is neither necessary nor appropriate for courts to intervene by assuming comity considerations. Judicial reliance on comity in preference to the revenue rule where there is a tax treaty is much the same as inferring unwritten terms to a contract where the parties have negotiated a complex commercial agreement: it invites criticism as unwarranted judicial intervention. In cases involving countries with less compatible tax regimes and collection processes, the application of comity may result in judicial intrusion into the domestic affairs of a sovereign state, as some courts have already noted.\(^\text{61}\)

Furthermore, the dichotomy between criminal and revenue laws suggested by Silver is a false one. As we shall see, revenue laws can result in custodial sentences and forfeiture of property, either directly or in combination with more classic penal legislation. Thus, the enforcement of both revenue and criminal laws implicates the sovereignty of a nation in a direct and fundamental way. One cannot dismiss this fact by simply asserting that because two states have similar revenue laws, mutual enforcement of those laws does not risk intrusion into matters of public policy. Even the assertion of similarity is not empirically correct. As governments respond to the needs and conditions of modern commerce, they must make decisions as to what constitutes active and passive income, the source of that income, the residence and citizenship of the taxpayer, the use of consumption taxes, and various methods

\(^{60}\) Article XXVI A, Assistance in Collection, was added by article 15 of the Third Protocol to the Canada-US tax treaty, signed on March 17, 1995. Article XXVI A is reproduced in the appendix to this article and discussed in the text below, at note 140 and following.

\(^{61}\) See, for example, supra notes 42 (Moore v. Mitchell) and 49 (Buchanan) and the accompanying text.
of collecting both taxpayer information and taxes owed—all of which engage national policy objectives. Underlying these decisions is the central legal question of how the tax base should be allocated between competing jurisdictions, a question that is now more complicated than it has ever been. International commerce in the 21st century requires sovereign states to re-examine such fundamental matters as which countries are affected by cross-border transactions, which of those countries has the primary taxing jurisdiction, and how taxing jurisdiction can be exercised harmoniously in this complex environment. How can domestic courts weigh all of these foreign policy implications?62

William Kovatch,63 like Silver, is unconcerned with the foreign policy implications that revocation of the revenue rule might entail. In his view, comity in the form of enforcement of foreign tax judgments is simply part and parcel of the burden of conducting business across borders, just like the application of other laws that may promote or impede international commerce. Denying comity effectively makes every country a tax haven. In making this argument, Kovatch too ignores the fact that if countries wish to cooperate in sharing tax information and collection, they will contract to do so; in the absence of a formal agreement, comity invites the judiciary to intervene in matters of foreign policy, which fall within the constitutional authority of the executive and legislative branches.

While Silver and Kovatch want to recognize tax judgments but not tax claims, Philip Burgess64 makes no such distinction. Burgess discusses the benefits that would accrue if tax claims were enforced directly in the jurisdiction best able to collect them without the administrative burden of obtaining a domestic judgment. He believes that a court should treat a tax claim like any other claim, and that the domestic court’s right to withhold domestic enforcement of such a claim on the traditional ground of public policy is sufficient protection. He does not address in any coherent fashion the fact that such a residual ground would involve the domestic court in judging the revenue laws of a foreign state against domestic standards, and thus plunge the domestic court into the “troublesome” inquiry of whether those foreign tax laws dovetailed with domestic tax and other policies. We should take heed, where Burgess does not, of Judge Hand’s warning in Moore v. Mitchell65 that the traditional application of foreign law recognition in the area of revenue laws would make the judiciary an unwelcome partner with the legislature and the executive in formulating and implementing foreign policy.

65 See the quotation in the text above at note 44.
Will Rearden invites US courts to engage in the “delicate inquiry” that Judge Hand warns us to avoid, on the ground that the Bush administration’s public commitment to fight organized crime, terrorism, and (allegedly) the ill-effects of tobacco use on a global scale warrants the use of foreign tax laws as an instrument of domestic policy. In Rearden’s view, comity and American sovereignty interests work together to support the demise of the revenue rule. Even if this is true, it is at best an argument based on historical contingency—namely, that American courts should suspend the operation of the revenue rule on the basis of a set of circumstances prevailing at a particular moment in US history. One cannot avoid the implication that American foreign policy seeks to use foreign tax (or for that matter any foreign law) as a pretext to grant domestic courts jurisdiction over matters that a foreign sovereign may not wish them to delve into. Rearden’s proposal does not require the foreign sovereign to invite American assistance with enforcement; if it did, the relationship could be governed by treaty. Instead, without the consent and perhaps contrary to the wishes of other sovereign nations, foreign law, as interpreted and enforced by American courts, becomes an instrument of American foreign policy.

Contrary to Rearden’s assertion, both comity and sovereignty concerns are complicated by the approach he advocates. This is made clear in an article by Jaime Guttman that addresses the problem of tax fraud in Latin America. Guttman welcomes American intervention into Latin American tax collection as a way of thwarting tax evaders who hide unpaid taxes in the United States and thereby deprive developing countries of funds needed to support their social programs. Guttman glosses over the fact that governments in Latin America range across the political spectrum, from far right to far left, and use tax revenues for a variety of causes, which may or may not accord with US public policy objectives. Are American courts to decide which of these countries have compatible public policies and which do not? Would the judicial view agree with that of the US executive as endorsed by the Senate? If other governments wish to cooperate in tax collection, why is this not spelled out in a treaty? What if the Department of Justice takes a different view than the State Department? Clearly, the broad application of comity proposed by Rearden and Guttman implicates the courts in issues of foreign policy, an extension of judicial discretion that cannot be justified on the basis of historically contingent circumstances or isolated cases involving “friendly” neighbours.

Vitaly Timokhov attacks the revenue rule because it suggests a judicial predilection against the domestic enforcement of foreign tax laws that might implicate

the interpretation of tax treaties. It is suggested here that the revenue rule is purely a default position adopted by the courts in the absence of a treaty. Since that position is well known to those who negotiate tax treaties, treaty provisions can be drafted with it in mind, just as commercial contracts are drafted with certain established principles of contract law in mind. As long as the rule is certain to be applied, it can be dealt with as part of the subject matter of the treaty. Treaties protect courts from involving themselves in complex public policy issues unless the answers to how those issues should be addressed are set out in the tax treaty itself.

In an article that provides a detailed analysis of the McNab and Pasquantino decisions, Ellen Podgor\(^{69}\) acknowledges that certain concerns may arise where comity is extended to cases involving criminal prosecution under domestic legislation for extraterritorial violations of foreign laws. However, she accepts that domestic courts may disregard the revenue rule in such cases, where the foreign jurisdiction seeks assistance with enforcement. In her view, “[c]omity concerns are not implicated when a country experiencing a social harm specifically requests that the United States proceed.”\(^{70}\) Even so (as Podgor notes), questions remain about the exercise of judicial discretion in specific cases. For example, which branch of government should speak for the foreign state when it makes the request—the administration via tax enforcement officials, or the executive branch via the foreign embassy? Whose view of the tax law should be enforced—that of the tax officials, the executive, the foreign court, or the domestic court? And what if enforcement of the foreign tax law would impose a tax that conflicted with a domestic policy competing for a share of the same tax base?

Adrian Briggs\(^{71}\) advocates a limited application of the revenue rule, on the basis of a dichotomy between private disputes where the revenue rule might be implicated as part of a plea of *ex turpi*, and litigation that would allow a foreign state to collect its taxes directly. While we might agree that private-law rights should not be tainted by a public-law interest, it is important to ensure that there is a bright line for determining the private-law/public-law aspects of a case if the revenue rule is to be narrowed in this fashion. For example, if the foreign government is suing for unpaid taxes as a form of damages in civil court, is this a matter of public law or private law? What about a government department? What about a “privatized” government function where the suit is at the behest of a private corporation that has paid a licensing fee to collect revenue?

The revenue rule evolved in a historical context where it was apparent to the courts that, absent a clear prohibition against domestic recognition of foreign tax laws, they would fall into an abyss in which any limitations on extraterritorial enforcement might disappear altogether. It is argued here that the courts are on the

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69 Podgor, supra note 16.

70 Ibid., at 102.

verge of sliding into that abyss. As we shall see, they are already invoking the kind of foreign policy concerns that are latent in the academic arguments against the revenue rule.

**Erosion of the Revenue Rule in the Courts**

**US Case Law**

*Scarcely any political question arises in the United States that is not resolved, sooner or later, into a judicial question.*

Alexis de Tocqueville, *Democracy in America* (1835), book 1, chapter 16

Revenue laws come in many forms. Income taxes, tariffs, sales and excise taxes, surcharges—all attract the revenue rule. In deciding whether the revenue rule applies in a particular case, the domestic court must look at the object of the foreign legislation and the basis for extraterritorial enforcement of that law. In a 1963 case, *Banco do Brasil*, for example, the New York Court of Appeals considered Brazilian legislation that required foreign buyers to pay in advance for Brazilian coffee exports through the country’s national bank. The bank exchanged 90 units of the domestic currency for each US dollar, when the market exchange rate was 220:1. The court found that the legislation was a disguised form of tax on Brazilian exports, that the national bank was an instrument of the Brazilian government, and that the action against the respondent was an attempt by that government to use allegations of fraud on the part of the foreign buyer to enforce a revenue law outside its territorial jurisdiction.

**R.J. Reynolds**

The Canadian government has traditionally had trouble enforcing high domestic taxes on alcohol and cigarettes (so-called sin taxes), particularly in the face of the claims of Canadian First Nations on border reserves that they are exempt from such taxes. In the *R.J. Reynolds* case, the Canadian government sought to recover unpaid revenues on cross-border trade in cigarettes, by bringing a civil action under the US Racketeer Influenced and Corrupt Organizations Act (RICO), which provides for treble damages where a person suffers harm at the hands of a criminal enterprise. In this case, the “criminal enterprise” involved the RJR-MacDonald family of companies (“RJR”). In 1991, Canada had doubled its cigarette taxes, and as a result, RJR had lost a substantial market share. RJR decided to export its cigarettes to the United States under a false declaration that they were not destined for consumption in

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72 Harden, supra note 53; and R.J. Reynolds, infra note 74.
73 Banco do Brasil, SA v. AC Israel Commodity Co., 190 NE 2d 235 (NYCA 1963).
75 18 USC sections 1961-65.
76 R.J. Reynolds, supra note 74, at 136.
Canada, and then ship the cigarettes to its distributors for sale to residents of the St. Regis/Akwesasne border reserve, knowing that they would resell the cigarettes without paying the Canadian sin tax. When a Canadian export tax was later imposed, the scheme became more complex, but in substance remained the same. Several individuals were convicted of wire fraud and criminal RICO violations, leaving Canada to sue for unpaid taxes in civil court under the civil RICO provisions. In doing so, Canada relied on *US v. Trapilo*, which involved a similar scheme that had resulted in a criminal conviction under RICO.

In *Trapilo*, the Second Circuit court held that RICO attacks domestic criminal enterprises regardless of the identity of the enterprise or the success of the scheme to defraud. On that basis, the court found that the enterprise in question was an illegal RICO enterprise, and held that because the legislation prohibited schemes to defraud regardless of their success, it was not necessary to delve into the intricacies of Canadian tax law to determine whether a criminal act had taken place. The revenue rule therefore had no application in the case. The court also noted, as an ancillary effect, that “our decision today indirectly assists our Canadian neighbors in keeping smugglers at bay or assists them in the collection of taxes,” but, owing to the domestic object of RICO, concluded that such assistance “is not our Court’s concern.”

The court in *R.J. Reynolds* rejected the argument of the Second Circuit in *Trapilo*, relying on *US v. Boots* (a previous case from the First Circuit court that involved a similar smuggling scheme), and applied the revenue rule to bar a civil RICO claim. More significantly, the court in *R.J. Reynolds* distinguished *Trapilo* on the following basis:

> [T]here is a critical difference between this civil suit brought by a foreign sovereign and the criminal actions previously considered by the panels of this court. In *Trapilo* [as well as *Boots* and other similar cases] the executive branch of the United States brought the case, while here, Canada is the plaintiff. When the United States prosecutes a criminal action, the United States Attorney acts in the interest of the United States, and his or her conduct is subject to the oversight of the executive branch. Thus, the foreign relations of the United States may be accommodated throughout the litigation. In contrast, a civil RICO case brought to recover tax revenues by a foreign sovereign to further its own interests may be, but is not necessarily, consistent with the policies and interests of the United States.

The court thus acknowledged that, although it may be dealing with Canadian tax legislation that could harm the interests of American tobacco-growing states, “which might vehemently object to Canada’s taxation scheme,” it would be willing to enforce

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77 130 F. 3d 547 (2d Cir. 1997).
78 Ibid., at 553.
79 80 F. 3d 580 (1st Cir. 1996).
80 *R.J. Reynolds*, supra note 74, at 123.
81 Ibid., supra note 74, at 123.
RICO and circumvent the revenue rule as long as the US attorney general supported the litigation.

The “strong fortress” of the revenue rule now rested on a shaky foundation, set to be toppled by one more smuggling case. Civil claims for lost tax revenues may still be prevented, but criminal cases prosecuted by the US attorney general at the instigation of foreign revenue officials, in an attempt to deter what they consider to be domestic tax evasion by using US criminal statutes, could allow indirect enforcement of foreign tax legislation.

**Pasquantino**

*R.J. Reynolds* suggested that the support of the US attorney general in litigation involving domestic criminal legislation may be enough to avoid the revenue rule. Even the dissent in *R.J. Reynolds* recognized that any rule designed to avoid the intricacies of foreign revenue laws was, “to put it mildly, dubious in a global economy which requires a great amount of interpretation of foreign laws.” In *Pasquantino*, Canada, with the assistance of the US attorney general, finally found the formula to evade the revenue rule in seeking to recover lost tax revenues through American courts.

In *R.J. Reynolds*, the US attorney general had submitted a brief arguing in favour of the application of the revenue rule. It pointed out that if the court recognized Canada’s claim, the executive branch would be robbed of the opportunity to bargain for reciprocal treatment in Canada by way of treaty. Moreover,

if Canada’s RICO suit were deemed permissible here, the doors to United States courts would also apparently be open to RICO treble damages by countries far less friendly to the United States, based on tax systems of questionable compatibility with our own, and perhaps against a background in which the political branches had rejected or been unable to secure reciprocal treaty obligations to assist in tax collection efforts.

In *Pasquantino*, on the other hand, the US attorney general argued that the revenue rule did not apply, and that the *Boots* decision, which applied the revenue rule to overturn a conviction under domestic criminal legislation, was “clearly incorrect.” The only difference between *R.J. Reynolds* and *Pasquantino* that appears to account for these different positions on the application of the revenue rule is that the prosecution was conducted by the attorney general of Canada in the former case and by the US attorney general in the latter.

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82 Supra note 9.
84 *R.J. Reynolds*, supra note 74, at 137, note 4.
Boots involved a federal prosecution of Native Americans in Maine who used their reserve as a staging ground for smuggling liquor into Canada without paying Canadian excise and sales taxes. The First Circuit of the Federal Court of Appeals ruled that although the conviction did not directly constitute extraterritorial enforcement of the revenue laws of Canada, upholding the conviction “would amount functionally to penal enforcement of Canada customs and tax laws.” 87 The revenue rule was therefore implicated, particularly since the court would have to adjudicate on aboriginal challenges to the law, and then discern how to apply the law to the facts of the case. Comity did not require recognition of the Canadian law because, whereas smuggling is an offence under US criminal law, Canada has no reciprocal smuggling legislation. 88

In Pasquantino, David Pasquantino and his brother, Carl, devised a scheme to smuggle liquor into Canada from their home in Niagara Falls, New York. They would order crates of liquor by telephone from various discount liquor stores in Hagerstown, Maryland, which their friend Arthur Hilts would pick up, using a rental truck. Some of the liquor was stored with the Pasquantinos and some was transported across the border, concealed in vehicles driven by Hilts and other accomplices. The CRA alleged that, over a four-year period, approximately 39,000 crates of alcohol had been smuggled into Canada, thereby avoiding more than $5.8 million in Canadian taxes. Evidence on the Canadian tax law was provided by a CRA special intelligence officer, who testified that the combined effect of federal excise and sales taxes was to nearly double the price of a crate of liquor in Canada over the price paid in the United States. 89 A federal grand jury convicted the Pasquantinos of using the telephone to defraud Canada of tax revenue under US wire fraud legislation. 90 The court imposed a five-year jail term.

On appeal, in a decision that was later vacated, a panel of the Fourth Circuit court overturned the convictions, 91 on the basis that the revenue rule precluded prosecution of the alleged offence under the wire fraud legislation. A conviction for wire fraud only requires proof of a scheme to defraud and the use of a wire communication

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87 Boots, supra note 79, at 587.
88 Ibid., at 588.
89 A crate of liquor that cost US$56 on purchase from a discount store in Maryland would sell for US$100 in Ontario.
90 18 USC section 1343, which defines the offence of fraud by wire, radio, or television, and the consequent penalties, as follows: “Whoever, having devised or intending to devise any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretences, representations, or promises, transmits or causes to be transmitted by means of wire, radio, or television communication in interstate or foreign commerce, any writings, signs, signals, pictures, or sounds for the purpose of executing such scheme or artifice, 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 v. United States, 305 F. 3d 291 (4th Cir. 2002).
in furtherance of the scheme. In the language of the legislation, an offence arises where a person has devised or intends to devise any scheme or artifice to defraud; in other words, no evidence is required in respect of the success of the scheme or the damages suffered as a result. The majority of the Fourth Circuit panel found that the revenue rule was applicable because, in order to discern whether there was a scheme to defraud under the legislation, the court had to inquire into the object of the scheme—that being the avoidance of Canadian tax laws—and determine whether the scheme in question avoided those laws by fraudulent means. The court cautioned that

[expansion of the mail and wire fraud statutes to reach violations of foreign tax laws “risks turning federal prosecutors and investigators into de facto criminal law enforcement agents for [certain] foreign tax authorities.”]

Agreeing with the First Circuit in Boots and disagreeing with the Second Circuit in Trapilo, the court stated:

Generally, we would agree that the identity and location of the victim in a wire fraud case are irrelevant. However, when that victim is a foreign government, that identity takes on a new importance. Here, in order to determine whether Canada was deprived of property (tax revenues), a determination must be made into whether Canada’s tax laws were in fact broken, or were intended to be broken. The Second Circuit [in Trapilo] opined that the validity of Canada’s revenue laws is not an issue. Rather, it has found that all that is necessary to prosecute a defendant for wire fraud in the United States is evidence that Canada imposes a duty on imported liquor, i.e., evidence of the existence of a foreign tax or duty. United States v. Pierce, 224 F. 3d 158, 166 (2d Cir. 2000). But recognizing the existence of a law is inherently and inescapably tied to recognizing the validity and scope of that law. Certainly, prosecuting a defendant for violations of a law, or for attempting to violate that law, requires an inquiry into the applicability and validity of the law.

The matter was then referred to the Fourth Circuit court en banc for rehearing. The court upheld the convictions, finding that by the time the wire fraud legislation was passed in 1954, the revenue rule had been narrowed in its application to only “those rare instances in which the court is compelled to actually enforce the judgment of a foreign court.”

Therefore, Congress could not be presumed to have passed the wire fraud legislation in the belief that the revenue rule would be an obvious, implicit exception to its application. The en banc Fourth Circuit court assumed that Congress had intended that evasion of foreign tax laws would be a sufficient


93 Supra note 91, at paragraph 21.

predicate offence upon which to found a domestic RICO conviction for illegal activities. The court went on to reject the argument of the First Circuit in *Boots* that, in upholding the conviction, it was functionally enforcing the tax laws of another sovereign, and instead maintained that it was only enforcing a domestic criminal law.

The defendants then appealed to the US Supreme Court. In a 5-4 decision, the court upheld the convictions, with majority and minority opinions revolving around the same debate about the applicability of the revenue rule that had been a central feature of the rulings in *Boots* and *Trapilo*, and of the lower court decisions in *Pasquantino*. The following summarizes the findings of the majority of the Supreme Court:

1. The US government may punish domestic criminal conduct even when the purpose of that conduct is to defraud a foreign government of tax revenue.
2. Such prosecutions are not invalidated by the revenue rule, or by related legislation such as the Mandatory Victims Restitution Act of 1996, which mandates that a restitution order be made in favour of the victim of wire fraud, and thus appears to require the restitution of lost tax revenue to the defrauded foreign government. While the court acknowledged that, as a result of that legislation, the prosecution of the *Pasquantino* case had the effect of enforcing Canadian revenue law, it did so “in an attenuated sense, but not in a sense that clearly would contravene the revenue rule.” In so ruling, the court did not indicate that it was in any way influenced by the fact that the US attorney general had invoked the revenue rule to prevent Canada from recovering tax revenues pursuant to such legislation, but stated that “the purpose of awarding restitution in this action is not to collect a foreign tax, but to mete out appropriate criminal punishment for [the defendant’s] conduct.”
3. The prosecution of the case by the US attorney general overcame any objection that the court was overreaching by entering the jurisdiction of the executive in foreign policy matters.
4. While it was unusual for the government of the United States to expend its resources in prosecuting a US citizen for smuggling liquor into Canada, there was nothing in law to prevent the executive branch from doing so.
5. The Supreme Court expressed no opinion on civil RICO applications, but remanded an outstanding case on its docket back to the Second Circuit Court of Appeals for reconsideration in light of its decision in *Pasquantino*. Upon

95 Supra note 9.
96 18 USC sections 3663A-3664.
97 *Pasquantino*, supra note 9, at 1778.
98 Ibid., at 1777.
reconsideration, the Second Circuit court reconfirmed that the absence of the US attorney general’s support was fatal to any foreign government’s application under RICO because of the revenue rule.  

The *Pasquantino* decision has important policy implications, which we will examine later. It also has important procedural implications with respect to the application of foreign tax laws in a US criminal prosecution. The sole evidence on Canadian tax law and its application came from a CRA intelligence officer, who appeared to have no legal training beyond her 17 years working for the CRA. No statute, regulation, or Canadian jurisprudence was put before the court. Therefore, the view of the foreign law applied by the court was that of a foreign enforcement official.  

This is not an anomaly: under US court procedure, determinations of foreign law are a question of law to be established by any relevant source, whether or not submitted by a party or otherwise admissible under federal rules of evidence. Thus, US courts have allowed not only expert evidence supplied by attorneys and judges, but also student law review notes and a variety of other non-expert sources as a means of ascertaining the application of foreign law. The reliability of such evidence was called into question, without success, in the other “David” case at the centre of this article, that of David McNab, discussed below.

**McNab**

*McNab* was decided by the Eleventh Circuit appeal court in 2003, the year after David Pasquantino won his first appeal at the Fourth Circuit court—only to have that decision overturned on rehearing. While *McNab* did not involve a violation of foreign tax law, there are some similarities between the two cases. Like Pasquantino, *McNab* was decided by the Eleventh Circuit appeal court in 2003, the year after David Pasquantino won his first appeal at the Fourth Circuit court—only to have that decision overturned on rehearing. While *McNab* did not involve a violation of foreign tax law, there are some similarities between the two cases.

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100 *European Community v. RJR Nabisco Inc.*, 150 F. Supp. 2d 456 (Dist. Ct. EDNY 2001); rev’d. 355 F. 3d 123 (2d Cir. 2004); remanded 125 S. Ct. 1968 (2005); aff’d. 424 F. 3d 175 (2d Cir. 2005). The Second Circuit court (2005, at paragraph 10) set out the following reasons for its decision:

[T]he revenue rule is designed to address two concerns: first, that policy complications and embarrassment may follow when one nation’s courts analyze the validity of another nation’s tax laws; and second, that the executive branch, not the judicial branch, should decide when our nation will aid others in enforcing their tax laws. . . .

[In *Pasquantino* the Supreme Court] found that concerns about sovereignty and separation of powers were not implicated where the United States government brings a criminal prosecution. . . .

The present civil lawsuit, on the other hand, is brought by foreign governments, not by the United States. Moreover, the executive branch has given us no signal that it consents to this litigation. . . . In short, the factors that led the *Pasquantino* Court to hold the revenue rule inapplicable to § 1343 smuggling prosecutions are missing here.


103 Supra note 8.
McNab was prosecuted successfully under US criminal legislation (on charges of conspiracy, money laundering, and smuggling) on the basis of an alleged violation of the law of a foreign jurisdiction; and, in upholding the defendant's conviction, the appeal court relied on the evidence of foreign enforcement officials in determining the application of the foreign law.

David McNab was a Honduran businessman with a commercial fishing operation, which included the transport of lobsters to the United States. McNab and three associates were charged in respect of a shipment of lobsters to Alabama, allegedly in breach of Honduran lobster fishing laws and in violation of the US Lacey Act. The section of the Lacey Act relied on by the prosecution prohibits the importation of “any fish or wildlife taken, possessed, transported, or sold in violation of . . . any foreign law.”104 The foreign laws in question were two Honduran resolutions and a regulation.105 For evidence on the application of the Honduran law, the prosecution relied on individuals employed by the Honduran regulatory agency that enforced the country’s fishing laws. The court accepted the testimony of those officials over the legal opinions of several experts in Honduran law—including the attorney general of Honduras, a regional prosecutor, and two law professors—all of whom maintained that these resolutions and regulation were not a valid source of Honduran law.106 McNab and his co-defendants were convicted; McNab was sentenced to over eight years in a US jail.

After filing an application to appeal, McNab obtained a declaration from a Honduran court that one of the resolutions relied upon by the US court was null and void. On this basis, the Honduran embassy, the attorney general of Honduras, and other senior Honduran officials filed positions with the US appeal court maintaining that the conviction of McNab should be invalidated.107 Nevertheless, the US court of appeal was not prepared to interfere with the lower court’s finding on Honduran law, and the conviction was upheld.

McNab’s petition for rehearing was refused, despite further formal objections from senior Honduran government officials. Notably, the attorney general of Honduras asked the US attorney general to intervene personally, citing the prosecution’s reliance on individuals who lacked the legal capacity and authority to interpret Honduran law, and its disregard for both the views advanced by qualified Honduran government spokesmen and the ruling of a Honduran court on the validity and interpretation of Honduran law. Moreover, in an amicus brief filed in support of McNab’s petition, the Honduran embassy stated that if the appeal court’s decision

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104 16 USC section 3372(a)(2)(A).
105 McNab, supra note 8, at 1231. The resolutions and regulation pertained to size limits, inspection and processing requirements, and the protection of lobster eggs: ibid., at 1239.
106 Ibid., at 1234.
107 Ibid., at 1248-49. The Honduran court ruled that resolution 030-95 (establishing size limits) was ultra vires because it had not been approved by the president of Honduras and authorized by the secretary of state of Honduras as required by Honduran law.
were allowed to stand, it “would damage international rules of comity and deference due a sovereign Government’s declaration of the meaning of its own law.” As we shall see, these objections go to the heart of the issues surrounding recent departures from the revenue rule in US and Canadian courts.

**Canadian Case Law**

One should not suppose that “the two Davids” are an anomaly peculiar to American law: the result in *McNab* is quite possible in Canada. Canadian law recognizes that violations of foreign law can be proven in domestic courts solely on the testimony of foreign enforcement officials, by reason of their experience in office (*peritus virtute officii*). Moreover, Canadian courts are not free to construe foreign legislation independent of expert testimony. Thus, Canadian judges are unable, as a matter of law, to apply their own construction of foreign tax statutes and regulations in the face of the uncontradicted testimony of foreign tax officials.

The prosecution of offences under domestic criminal legislation in respect of extraterritorial conduct is already firmly established in Canadian case law. For example, in *VitaPharm Canada Ltd. v. F. Hoffman-LaRoche Ltd.*, a number of foreign companies conspired to fix prices of vitamin products in Canada. The defendants did not sell these products in Canada—in fact, some did not sell them at all. Nevertheless, the Ontario courts assumed jurisdiction on the basis that damage was suffered in Canada. The same logic applies under our laws of criminal conspiracy. (This doctrine, known as “impact territoriality,” is discussed in the next section of the article.)

The result in *Pasquantino* is also not inconsistent with the *Morguard* line of cases in Canada. In *Morguard*, decided in 1990, the Supreme Court of Canada endorsed the application of comity by Canadian courts in enforcing judgments under foreign laws. Although *Morguard* dealt with interprovincial enforcement of judgments, the court made the following comments, in obiter, to emphasize the need for Canadian courts to recognize notions of international comity in deference to the requirements of modern international commerce:

> The business community operates in a world economy and we correctly speak of a world community even in the face of decentralized political and legal power. Accommodating the flow of wealth, skills and people across state lines has now become imperative. Under these circumstances, our approach to the recognition and enforcement of foreign

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109 For example, *Guerin v. Proulx* (1982), 37 OR (2d) 558 (Co. Ct.).
111 (2002), 20 CPC (5th) 351 (Ont. SCJ).
112 *British Columbia v. Imperial Tobacco Canada Ltd.*, 2006 BCCA 398, at paragraphs 41-44.
113 *Morguard Investments Ltd. v. De Savoye* (1990), 76 DLR (4th) 256 (SCC).
judgments would appear ripe for reappraisal. Certainly, other countries, notably the United States and members of the European Economic Community, have adopted more generous rules for the recognition and enforcement of foreign judgments to the general advantage of litigants.114

Morguard thus confirmed that in Canada the rules of private international law would henceforth be governed by the concept of comity, defined as the systematic accommodation of foreign laws within Canada, in the interests of providing an orderly, fair, and secure system for international commerce.

The comity principle was applied in United States of America v. Ivey,115 an Ontario decision in which a US statute (the Comprehensive Environmental Response, Compensation and Liability Act, 1980—the so-called superfund legislation) effectively stripped the protection of the corporate veil from Canadian directors and shareholders of a Michigan corporation in regard to certain environmental offences. The Canadian court permitted an American court to enforce a Michigan judgment granted against the corporation and the Canadian residents who were its controlling owners. The lower Ontario court rejected the defendants’ argument that the US government was enforcing a “revenue law,” directly or indirectly, despite expert evidence, as well as textbook authority, supporting their position. The court stated that, in any event, the public law exception was based on the principle that a foreign sovereign was trying to overreach and impinge on Canadian sovereignty, whereas in this case

[the defendants chose to engage in the waste disposal business in the United States and the judgements at issue go no further than holding them to account. . . .

There is clearly a public purpose at stake, but in my view, the presence of the public purpose does not defeat the plaintiff’s case. . . . In an area of law dealing with such obvious and significant transborder issues, it is particularly appropriate for the forum court to give full faith and credit to the laws and judgments of neighbouring states.116

Judgment in Ontario was therefore granted summarily in favour of the US government in the amount of approximately $4.5 million. The Ontario Court of Appeal agreed with the reasoning of the lower court, stating, “The public law exception to the enforceability of foreign judgments rests, as Sharpe J. pointed out in rejecting it, on a shaky doctrinal foundation.”117 Therefore, it appears that, with the cooperation of Crown prosecutors, a criminal prosecution brought in Canada by the US government, coupled with the restitution and forfeiture remedies under Canada's

114 Ibid., at 270.
116 Supra note 115 (Gen. Div.), at 548-49.
117 Supra note 115 (CA), at 374.
Criminal Code,\textsuperscript{118} the Competition Act,\textsuperscript{119} or provincial legislation,\textsuperscript{120} could replicate the result of the \textit{Pasquantino} decision in Canada.

Indeed, Canadian law may go even further than \textit{Pasquantino} in allowing US tax authorities to collect their revenues in Canada, notwithstanding that the Supreme Court in \textit{Harden} recognized the revenue rule as the law of this country.\textsuperscript{121} In \textit{Harden}, the Supreme Court supported the revenue rule in its strongest form, upholding the prohibition of any attempt to enforce a foreign power’s revenue laws, whether through direct or indirect means. However, in subsequent decisions, Canadian courts appear to have accepted the idea that comity has overtaken the traditional rationale for the revenue rule set out in \textit{Harden}, and have therefore favoured a narrow interpretation of the ratio decidendi of that case. Indeed, some rulings appear to have gone beyond \textit{Pasquantino} in viewing foreign taxes as being enforceable “in an attenuated sense” when the domestic criminal law is used to assist foreign revenue officials.

In \textit{United States of America v. Levy},\textsuperscript{122} for example, Canadian telemarketers were sued for wire fraud in connection with the sale of Lotto 6/49 tickets to American consumers. The US government alleged that the scheme was illegal under section 206 of Canada’s Criminal Code, as well as provincial lottery legislation.\textsuperscript{123} In lieu of seeking the participation of the attorney general of Canada in prosecuting this case, which was framed as a civil restitution action, the US government relied on documents exchanged by the governments of both countries pledging “United States-Canada cooperation against cross-border telemarketing fraud.”\textsuperscript{124} The Ontario Superior Court allowed the US government to pursue the action and, in effect, enforce Canada’s domestic law where its own government had not done so, in order to secure restitution for fraud and to trace assets in Canada.

With respect to tax evasion, which may be considered a form of criminal fraud,\textsuperscript{125} Canadian case law may go further than \textit{Pasquantino} in allowing the US government to seek restitution of unpaid tax revenue from Canadians without even the need for a criminal prosecution. Indeed, our courts have been quite receptive to the idea that one ought not to apply the penal or revenue rule exceptions where doing so

\begin{footnotesize}
\begin{itemize}
\item 118 RSC 1985, c. C-46, as amended, sections 462.37, 490.1, and 491.1.
\item 119 RSC 1985, c. C-34, as amended, section 36.
\item 120 See David Debenham, \textit{The Law of Fraud and the Forensic Investigator} (Toronto: Thomson Carswell, 2006), 64; and \textit{British Columbia v. Imperial Tobacco Canada Ltd.} (2005), 44 BCLR (4th) 125 (SC).
\item 121 See supra note 53 and the accompanying text.
\item 122 (1999), 45 OR (3d) 129 (SCJ).
\item 123 Ontario Lottery Corporation Act, RSO 1990, c. O.25, as amended, prohibiting the sale of lottery tickets above their face value, and the Gaming Control Act, 1992, SO 1992, c. 24, as amended, requiring all vendors of lottery tickets to be licensed.
\item 124 Levy, supra note 122, at 138.
\item 125 In \textit{Dwyer v. The Queen}, [2001] 3 CTC 2755 (TCC), the judge uses the terms interchangeably.
\end{itemize}
\end{footnotesize}
“would . . . condone or even encourage commercial activity which is legally or morally reprehensible.” 126 British Columbia’s Supreme Court has held that the fact that a claim for recovery by a foreign state is made in tandem with contemporaneous criminal or other prosecutions, and may result in the payment of some taxes, “does not convert [an] action [for the disgorgement of ill-gotten gains] into a proceeding for the enforcement of a taxing statute.” 127 In so ruling, our courts have taken the same view as the US Supreme Court in Pasquantino (that “the purpose of awarding restitution in this action is not to collect a foreign tax, but to mete out appropriate criminal punishment for [the defendant’s] conduct”). 128 As noted above, the US court found it entirely appropriate to order the restitution of ill-gotten gains to a foreign government, since such foreign tax collection “in an attenuated sense” was, in the court’s view, essentially a means of enforcing domestic criminal sanctions.

The Supreme Court of Canada has also sent signals that the revenue rule no longer has the support it enjoyed at the time of the Harden decision. Indeed, in Libman v. The Queen, the court anticipated the result in Pasquantino when it rejected the argument that a Canadian court had no jurisdiction to convict Canadian telemarketers of fraud in respect of certain misrepresentations made to US citizens. 129 Justice La Forest applied a broad notion of impact territoriality to convict those who plan their frauds in Canada, stating that the “preparation and evolution [of such schemes], even in the case of failure, is reprehensible” 130—a view that is echoed in the ratio of Pasquantino. Justice La Forest went on to conclude:

[Means of communication have proliferated at an accelerating pace and the common interests of states have grown proportionately. Under these circumstances, the notion of comity, which means not more nor less than “kindly and considerate behaviour towards others” has also evolved. How considerate is it of the interests of the United States in this case to permit criminals based in this country to prey on its citizens? How does it conform to its interests or to ours for us to permit such activities when law enforcement agencies in both countries have developed cooperative schemes to prevent and prosecute those engaged in such activities? To ask these questions is to answer them. No issue of comity is involved here. . . . I also agree with the sentiments expressed by Lord Salmon in Director of Public Prosecutions v. Doot, supra, that we should not be indifferent to the protection of the public in other countries. In a shrinking world, we are all our brother’s keepers. 131

127 Ibid., at paragraph 21, quoting United States of America (Securities and Exchange Commission) v. Shull (sub. nom. Pfunder v. Shull, 1999 CanLII 6625, at paragraph 29 (BCSC).
128 Pasquantino, supra note 9, at 1777.
129 [1985] 2 SCR 178. The court found that the telemarketing scheme not only misrepresented the investments to the foreign buyers but also required them to send payments to an address in a third country (Costa Rica).
130 Ibid., at paragraph 49.
131 Ibid., at paragraph 77.
Canadian courts are therefore increasingly likely to ignore the strict interpretation of the revenue rule, which requires its application even where there is a suggestion that a foreign sovereign is seeking to give extraterritorial effect to its penal or revenue laws. With the US Treasury department making collection of taxes abroad a priority (because, in its view, less than 10 percent of non-residents who should be paying US taxes are in fact doing so), one can foresee that the US government will increasingly seek the application of Pasquantino principles in Canada as a matter of comity or reciprocity.

**IMPLICATIONS OF BROAD JUDICIAL DISCRETION TO ENFORCE FOREIGN REVENUE LAWS**

Between independent States, respect for territorial sovereignty is an essential foundation of international relations.

*United Kingdom v. Albania*, [1949] ICJ 4, at 35

**Significance of the Decisions in McNab and Pasquantino**

Several common elements formed the basis for the prosecution and ultimate conviction of David McNab and David Pasquantino for offences under US criminal law:

1. A social harm was alleged to have occurred, with a foreign government as the victim.
2. The laws of the foreign jurisdiction had allegedly been broken.
3. Evidence with respect to both the laws alleged to have been broken and the harm alleged to have been done came from foreign enforcement officials.
4. The breach of foreign law was essential to a conviction under the domestic criminal law.
5. The approval of the executive branch of government, in the form of prosecution by the US attorney general, superseded any foreign relations implications that might arise as a result of interpreting and indirectly enforcing a foreign law on the basis of the views of foreign enforcement officials (in McNab, regardless of the foreign embassy’s position on the matter).

If Canada and the United States wish to expand the scope of current reciprocal enforcement provisions, the accepted procedure is to amend the existing tax treaty. However, apart from the usual delay that treaty amendments entail, the political environment is not currently conducive to swift approval by the respective legislatures. Canada’s minority Conservative government faces an uncooperative Parliament, and

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132 “[I]f it were otherwise, litigants could freely avoid the impact of the revenue rule by bringing tax claims under the guise of non-tax related causes of action”: *Republic of Honduras v. Philip Morris Companies*, supra note 19, at 1258.

133 See *Chua*, supra note 21, at paragraph 15.
the Bush administration faces a hostile, Democratic-controlled Congress. McNab and Pasquantino appear to offer enforcement officials in both countries a way around this difficulty.

The CRA, for example, could pursue tax claims in cross-border tax-avoidance cases by simply issuing notices of reassessment in Canada; identifying American participants who used the telephone, fax, or e-mail to plan, promote, or implement the scheme; and teaming up with American enforcement officials to enforce their view of Canadian tax laws by way of prosecution on criminal conspiracy charges in the American courts. A subsequent contrary ruling on the same point of law in a Canadian court by a judiciary less inclined to take the legal opinions of the CRA at face value would not overturn the conviction (as McNab demonstrates).134

Moreover, the Pasquantino case gives the CRA an easy way to get around article XXVI A of the Canada-US tax treaty, which (as discussed below) allows for enforcement of Canadian tax judgments in American courts only in limited circumstances and under certain conditions. As a US citizen, David Pasquantino was not subject to the assistance-in-collection article of the treaty.135 His case demonstrates how the domestic criminal law can be used by enforcement officials to circumvent negotiated treaty protections and the common values they are intended to uphold. As a result of Pasquantino, merely by securing the approval of the US attorney general, the CRA can evidently use American criminal legislation to charge those it believes are tax evaders, and (assuming that the prosecution is successful) can likely also use American criminal restitution or forfeiture legislation (such as the civil RICO provisions) to collect Canadian taxes at American taxpayers’ expense via the American courts.136 Thus, Canadian tax officials may not only get an interpretation of the law they like, and the money they want, but get it at a fraction of the cost of domestic enforcement. This, of course, raises the question of what American enforcement officials would want in return.137

“The two Davids” turn the revenue rule on its head, by allowing American courts to interpret Canada’s tax laws in a manner favourable to Canadian enforcement officials. It can be assumed that most American criminal defence attorneys are not well versed in Canadian law of any kind, let alone the complexities of Canadian tax law. Even if they are, McNab shows that their submissions may not be readily accepted.

134 The reversal of David Pasquantino’s conviction in his first appeal did not change the outcome for David McNab.

135 See the appendix to this article, paragraph 8 of article XXVI A.

136 It should be noted, however, that there is as yet no reported civil case in which the US attorney general has sanctioned such restitution.

137 Many American jurisdictions provide that forfeited property may be kept and utilized by the law enforcement agency responsible for the investigation leading to the conviction: Alan B. Morrison, Fundamentals of American Law (New York: Oxford University Press, 1996), 324. In such cases, the CRA may end up, in effect, using Canadian tax revenues to fund the collection of domestic taxes by American enforcement agencies. Is this what Parliament intended?
Pasquantino and McNab may give Canadian tax officials a unique opportunity to have their interpretation bulletins, information circulars, and other guidelines and interpretations of Canadian tax law given the force of law by American courts, which can then use American criminal law as a means of deterring tax evasion, if not outright collection of Canadian tax, without recourse to extradition, tax, or other treaties. While the American courts have not yet conflated civil and criminal prosecutions under RICO and other statutes, time will tell whether the judicial appointment of the US attorney general as the gatekeeper on the recovery of Canadian tax through American taxes will prove an effective safeguard. In any event, it appears that the use of American criminal law to punish tax evaders constitutes a sufficient abrogation of the revenue rule to implicate much broader policy concerns.

There is no obvious policy reason to support the abrogation of the revenue rule at this time, or in this fashion. Canada and the United States already have enforcement mechanisms in place to assist the collection of taxes owing in respect of cross-border transactions.

- First, while multinationals give rise to greater opportunities for tax arbitrage that may be perceived as tax avoidance or evasion, the domestic taxing authority can take steps to secure the payment of taxes owing through due process, by attaching assets of the corporate group held in the domestic jurisdiction.
- Second, when the income is passive and the only assets are readily transferable, Canada and the United States (like most other countries) use withholding taxes to secure their tax base.
- Third, to the extent that the above measures are insufficient, both countries can rely on tax and extradition treaties, freely negotiated and sanctioned by their legislatures, rather than make requests of enforcement officials.

Those who advocate the abrogation of the revenue rule have not advanced any argument suggesting that the treaty mechanism is not sufficient to fill any gaps in domestic tax enforcement. Indeed, the treaty process has proved to be quite flexible and robust in dealing with the challenges posed by the international tax-planning industry. As evidence of this, one can point to the long history of cooperation among OECD countries in developing and refining treaty mechanisms for tax law enforcement.138

138 See supra note 58 and the accompanying text. Amendments to Canada’s tax treaties often have their origins in prior discussions among OECD members and consequent amendments to the OECD model treaty. For example, in February 2007, OECD countries agreed to broaden the treaty mechanisms available to companies and individuals involved in cross-border disputes over taxation by introducing the possibility of arbitration if other attempts to resolve disagreements fail. The OECD model treaty is to be modified to provide for arbitration in cross-border disputes if they remain unresolved for more than two years. This change is reflected in the substantially expanded paragraph 6 added to article XXVI by the Fifth Protocol to the Canada-US treaty, infra note 141, article 21.
It is hardly comity for the American courts to encourage a confederacy of tax enforcement officials and federal prosecutors who seek to circumvent due process and treaty obligations in the name of US criminal law enforcement. The policy implications of such judicial accommodation are examined in the discussion that follows.

Circumvention of Treaty Protections

The Canada-US tax treaty reinforces the common-law principles underlying the revenue rule while recognizing the need for comity and cooperation to facilitate enforcement of domestic tax laws in an international context. Three articles specifically provide for cooperation between domestic authorities in securing the payment of taxes owing across jurisdictional boundaries: article XXVI, Mutual Agreement Procedure; article XXVI A, Assistance in Collection; and article XXVII, Exchange of Information.

Article XXVI provides a mechanism for the resolution of disputes where conflicts arise over taxing jurisdiction. It also contains a reciprocal collection provision in respect of treaty benefits (relief from taxation granted by a state) that may enure to persons who are not entitled to them; however, the obligation to pursue the collection of taxes on behalf of the other state is limited to measures that are consistent with domestic administrative practices and public policy.\(^\text{139}\)

Article XXVI A extends the scope of assistance in collection to “revenue claims”—that is, tax judgments awarded by domestic courts in the jurisdiction requesting collection assistance\(^\text{140}\)—and it applies to “all categories of taxes collected by the taxing jurisdiction.”\(^\text{141}\) However, the right to extraterritorial enforcement of domestic tax laws is subject to certain limitations, including the following:

\(^{139}\) Paragraph 4 of article XXVI states, “[N]othing in this paragraph shall be construed as imposing on either of the Contracting States the obligation to carry out administrative measures of a different nature from those used in the collection of its own tax or which would be contrary to its public policy (ordre public).”

\(^{140}\) The use of the term “revenue claim” may be confusing, since article XXVI A does not apply to any tax claim, but only to a claim that has been “finally determined” in accordance with all applicable administrative and legal processes: see the appendix to this article, paragraph 2 of article XXVI A.

\(^{141}\) Paragraph 9 of article XXVI A. The fifth protocol to the treaty (ratified by Canada on December 14, 2007 but not yet ratified by the United States) will extend the application of article XXVI A to “contributions to social security and employment insurance premiums” levied by the taxing jurisdiction, thus blocking another potential source of tax leakage through cross-border structures: Protocol Amending the Convention Between Canada and the United States of America with Respect to Taxes on Income and on Capital Done at Washington on 26 September 1980, as Amended by the Protocols Done on 14 June 1983, 28 March 1984, 17 March 1995 and 29 July 1997. See the appendix to this article for amendments to article XXVI A introduced by the fifth protocol.
The taxing jurisdiction (“the applicant state”) must make formal application for assistance in collection of a revenue claim, which must include certification that the claim has been “finally determined” in a domestic court (paragraph 2).

The state whose assistance is sought (“the requested state”) is not obliged to agree to the request. The decision to accept (or refuse) the application lies within the discretion of that state’s competent authority\(^\text{142}\) (paragraph 3), subject to any terms agreed to by the two states to ensure reciprocity in the level of assistance provided (paragraph 11).

The requested state has no right to subject the revenue claim to further administrative or judicial review; the adjudication of the claim in the applicant state must be accepted as final (paragraph 5).

No collection assistance is granted in respect of a taxpayer who is resident in, and a citizen of, the requested state (paragraph 8).

As in the case of article XXVI, the effort to collect the claim on behalf of the applicant state is limited to measures that are consistent with the usual administrative practices and public policy of the requested state. In addition, the provisions of article XXVI A in no way limit the assistance available under paragraph 4 of article XXVI (paragraph 10).

The taxing jurisdiction therefore retains sovereign control over the use of its tax laws in terms of the final determination by its own constitutional decision makers regarding both the interpretation of those laws and their enforcement in the foreign state. At the same time, the foreign state is protected from overreaching by the taxing jurisdiction, should it attempt to impose extraterritorial taxation on citizens of the foreign state, and it retains the right to determine whether enforcement of the revenue claim is consistent with its own administrative practices and public policy. Significantly, that determination rests with the executive branch of the foreign government and not with its judiciary. Any gap in the tax collection process in cases involving tax evasion is bridged by extradition rights under a separate treaty.\(^\text{143}\)

\(^{142}\) The “competent authority” referred to in the treaty means Canada’s minister of national revenue or his authorized representative, or the US secretary of the treasury or his delegate (article III(1)(g)).

\(^{143}\) Protocol Amending the Treaty on Extradition Between the Government of Canada and the Government of the United States of America, signed at Washington on December 3, 1971, as Amended by an Exchange of Notes on June 28 and July 9, 1974. Article 2 of the protocol provides:

1. Extradition shall be granted for conduct which constitutes an offense punishable by the laws of both Contracting Parties by imprisonment or other form of detention for a term exceeding one year or any greater punishment.

2. An offense is extraditable notwithstanding

   (i) that conduct such as interstate transportation or use of the mails or of other facilities affecting interstate or foreign commerce, required for the purpose of establishing jurisdiction, forms part of the offense in the United States, or

   (ii) that it relates to taxation or revenue or is one of a purely fiscal character.
Thus, the assistance-in-collection article creates a limited inroad on the revenue rule, but preserves the “common values of the two countries and their similar approach to tax administration and the protection of taxpayer rights.” Pasquantino is significant because the constitutionally appointed enforcement officials in both countries failed to give due consideration to these principles and the enforcement mechanism available under the treaty. They had the opportunity to pursue prosecution of the tax claim in the Canadian courts, and they chose not to do so.

The third treaty article that facilitates cross-border enforcement of tax laws is article XXVII, which provides for the exchange of tax-related information between the competent authorities of the two countries—again, subject to certain conditions. Paragraph 1 of the article protects taxpayers’ rights by imposing the following restrictions on the type of information that may be exchanged and on its handling and use:

- The information must be relevant to the application of the treaty or of domestic tax laws relating to taxes covered by the treaty.
- The state that receives the information must treat it according to the same standard of secrecy that it applies to information obtained under its domestic tax laws.
- The information may be disclosed only to persons or authorities (including courts and administrative bodies) involved in the assessment or collection of, or administration and enforcement in respect of, taxes covered by the treaty.
- Such persons or authorities may use the information only for the above purposes (but the information may be disclosed in public court proceedings or judicial decisions).

There are also limitations on the nature and scope of the information that a state may be required to provide, including the following:

- The form of the information (such as depositions, records, and accounts) provided by a state in response to a request is governed by the laws and administrative practices relating to information obtained for domestic purposes in that state (paragraph 2).

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145 Mallinak, supra note 7, at 97.
146 The fifth protocol to the treaty, supra note 141, article 23, amends the language to refer to “such information as may be relevant” (emphasis added), and adds a new paragraph allowing a state to request (and requiring the other state to provide) information that it may not need for its own tax purposes. These amendments permit access to information relating, for example, to transactions or business arrangements in other jurisdictions.
147 The fifth protocol, ibid., adds further amendments broadening the scope of the information that may be requested, removing some limitations on the obligation to respond, and allowing representatives of a state to conduct interviews and examinations of books and records in the other state (subject to the consent of the persons concerned).
A state is not obliged to provide information that would disclose certain trade or business secrets or processes, or information the disclosure of which would be contrary to public policy (paragraph 3b).

Article XXVII of the treaty thus regulates the types of information that can be exchanged, and the manner of complying with information requests, in relation to tax law enforcement. It preserves sovereign control of taxpayers’ private information and prevents fishing expeditions by either government.

This is an important consideration where Canadian and American domestic laws have very different regimes to protect privacy and taxpayer rights. Compared with Canadian authorities, criminal law enforcement officials in the United States have historically had a broader range of information-gathering and -sharing powers. For example, the Patriot Act\textsuperscript{148} allows the Federal Bureau of Investigation to issue administrative subpoenas, known as national security letters, without any judicial oversight. While we may not subscribe to the rather extreme view that “[o]ur democratic societies are at risk of being turned into surveillance societies over time,”\textsuperscript{149} we should at least be sufficiently concerned to question whether criminal enforcement of tax laws is good tax policy, and whether US criminal statutes should be used to circumvent protections built into the Canada-US tax treaty and other conventions.\textsuperscript{150}

Tax evasion and criminal law enforcement have been directly linked by those who draw an analogy between catching Al Capone for tax evasion and catching drug traffickers, arms dealers, and terrorists who use tax evasion hand in glove with money laundering to protect their ill-gotten gains. However, others argue that there is a fundamental difference: “Money laundering is taking money from the underground economy and bringing it above ground. Tax avoidance is taking legally made money and hiding it from the government.”\textsuperscript{151} It has been difficult to reach an international consensus on measures to combat money laundering, because such legislation has often been challenged on privacy grounds. For example, in 1999, the US Congress refused to pass the International Counter-Money Laundering Act, which would have given officials the authority to ask banks to release customer information (provided that the request was based on “reasonable grounds”), because granting such powers would compromise privacy rights. However, that was before 9/11. Since then, we have seen a radical policy shift on the question of the balance between the national


\textsuperscript{151} Eileen M. Cieslä, “Are Efforts to End ‘Tax Competition’ the First Steps of Global Tax Cartel?” Investor’s Business Daily, October 26, 2000 (online: http://www.freedomandprosperity.org/Articles/ibd10-26-00/ibd10-26-00.shtml).
interest and individual privacy rights. In the present climate, the conflation of tax collection with money laundering and other criminal enterprises raises a real concern that the protection of individual privacy rights in tax matters¹⁵² (hitherto guaranteed by domestic legislation and confirmed by our treaties) may be implicated by the enforcement of post-9/11 criminal law in US courts.¹⁵³

Impact Territoriality and Arbitrage Concerns

US case law, including (but not limited to) the McNab and Pasquantino decisions, provides a basis for the “overreaching” of US courts into foreign jurisdictions by way of the doctrine of impact territoriality (also known as “objective territoriality”). This doctrine, as originally formulated, allows for the prosecution in US courts of conduct taking place in another jurisdiction because it is alleged to have a detrimental effect in the United States.¹⁵⁴ Thus, American courts have applied this doctrine in the prosecution of extraterritorial price-fixing activity that occurred entirely outside the country, because of its effect on American markets. The judiciary may thus assume jurisdiction to rule against any foreign transaction that is perceived to have harmful consequences for the interests of the United States. In a world that is increasingly dominated by e-commerce and complex cross-border structures, the limits on the jurisdiction of American courts are hard to discern. As Podgor has noted, “[t]he ‘objective territorial’ principle provides an almost limitless breadth, as it is relatively easy to demonstrate that [extraterritorial] criminal conduct had an effect on the United States.”¹⁵⁵

Podgor also points out that McNab and Pasquantino “present a new dimension to the extraterritoriality discussion” in that the presumed harm (on which the prosecution of each case depended) was inflicted on a foreign sovereign state.¹⁵⁶ For example, in Pasquantino, the defendants’ conduct allegedly resulted in a loss of tax revenues to the Canadian government. The prosecution proceeded on the basis of the inferred harm to the United States from the use of the domestic wire system in the furtherance of an extraterritorial criminal enterprise. Moreover, the court inferred its jurisdiction to apply Canadian revenue law in establishing the ground for criminal prosecution under the wire fraud statute (which does not specifically provide for

¹⁵² Discussed in Chua, supra note 21.

¹⁵³ For an example of the abuse of criminal-law warrants and money-laundering allegations to acquire information, see Budd v. Canada, 2004 CanLII 21325 (Ont. SCJ). It should be noted that the Fifth Protocol to the Canada-US tax treaty, supra note 141, article 23, introduces a new provision in article XXVII that opens the door to the exchange of information held by a bank or other financial institution (new paragraph 5).

¹⁵⁴ Strassheim v. Daily, 221 US 280, at 285 (1911). This case addressed the question of jurisdiction in applying state laws. The principle articulated by the court was subsequently extended to activities occurring in another country.

¹⁵⁵ Podgor, supra note 16, at 98.

¹⁵⁶ Ibid. Podgor discusses the question of extraterritoriality in some detail.
extraterritorial application of its provisions). The Pasquantino case suggests that the United States could claim an interest in challenging virtually any international transaction if a connection with US wire services—however tenuous—can be alleged,\(^{157}\)

When considering the implications of Pasquantino in this respect, we should look to past experience with the US Foreign Corrupt Practices Act (FCPA).\(^{158}\) The anti-bribery provisions of the FCPA make it unlawful to make a payment to a foreign official for the purpose of obtaining or retaining business or with, or directing business to, any person. This prohibition applies to any American, certain foreign issuers of securities, and foreign firms and persons who undertake any act in furtherance of such a corrupt payment while in the United States. The meaning of “foreign official” is broad. For example, an owner of a foreign bank who was the brother of the foreign minister of finance would count as a foreign official, according to the US government.\(^{159}\) There is no statutory restriction in respect of either the amount or the form of the payment. Thus, what constitutes a bribe is open to interpretation. It could be illegal, for example, to pay a foreign official as little as $1, or to make a gift of hockey tickets, or pick up the tab at a restaurant. The US government focuses on the intent of the bribe more than the monetary value.

The anti-bribery provisions provide for penalties that include a fine of up to $2 million for a firm, and a fine of up to $100,000 and imprisonment for up to five years for an officer, director, or stockholder of the firm. There can be civil penalties as well. The US attorney general or the Securities and Exchange Commission (SEC), as appropriate, may bring a civil action for a fine of up to $10,000 against any firm as well as any officer, director, employee, or agent of a firm, or stockholder acting on behalf of the firm, who violates the anti-bribery provisions. In an SEC enforcement action, the court may also impose an additional fine not to exceed the greater of (1) the gross amount of the pecuniary gain to the defendant as a result of the violation and (2) a specified dollar limitation. The FCPA’s penalty provisions do not override the provisions in other federal criminal statutes providing for alternative fines. For example, under RICO, individuals may be fined up to $250,000 or up to twice the amount of the gross gain or gross loss if the defendant derives pecuniary gain from the offence or causes a pecuniary loss to another person.

The international reach of the FCPA has meant that doing business with, or for, an American multinational corporation in any part of the world has become fraught with risk. According to one observer,

U.S. companies . . . face an ever-expanding interpretation of the FCPA by the enforcement agencies—the Justice Department on the criminal side and the Securities and Exchange Commission at the civil end.

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158 15 USC section 78.
159 See United States, Department of Justice, “Foreign Corrupt Practices Act (FCPA)” (online: http://www.usdoj.gov/criminal/fraud/fcpa/).
The agencies operate largely unrestrained by judicial precedent: Staying in business is more important than setting precedent for most companies, so they typically plead guilty or settle with the government rather than risk the potentially ruinous consequences of going to trial. . . .

[Moreover, the business reflex is to overcompensate and not exercise a right where] things can go wrong, especially in an enforcement atmosphere where the prosecutors, not the courts, assume the leading role in determining what violates the FCPA and what doesn’t. With that kind of commercial uncertainty, compliance planners constantly have to ask themselves when prevention becomes overkill.160

The RICO, mail fraud, and criminal conspiracy161 charges have been called “hydrogen bombs on stealth aircraft”162 because of their expansive extent despite their relatively innocuous language. American prosecutors use them to prosecute persons who have engaged in perceived improprieties that are not the subject of any particular statute. In the commercial context, these laws have been used to squeeze corporate managers for testimony about the criminal activities of third parties . . . [while courts [have] acceded to the desire of prosecutors for the creation of amorphous crimes that would allow prosecutors to pursue hard-to-define improprieties—or conduct that was improper only in the eyes of the particular prosecutor—or to pressure individuals thought to possess knowledge of other criminal activities.163

Thus, an alleged RICO violation allows US investigators the leverage to conduct inquiries and collect information beyond the boundaries established under tax statutes and treaties. For example, allegations of criminal misconduct based on transfer prices would allow criminal investigators to get third-party information not otherwise available under tax law.164 Pasquantino allows tax enforcement agencies to engage in two forms of legal arbitrage: jurisdictional arbitrage (or “forum-shopping”) with respect to the country of choice in which to seek enforcement of domestic revenue laws, and procedural arbitrage in the use of criminal or tax record subpoena powers most conducive to the agency’s purposes.

Even under the Canada-US tax treaty, the CRA can obtain information from the US authority that it cannot obtain under domestic law, and a breach of Charter rights by a foreign government may not prevent the use of that information in a Canadian or foreign court.165 Violating domestic protections through a treaty process

161 18 USC section 371.
163 Ibid., at 956-57.
165 See McCracken, supra note 150, at 1897-98.
is troubling enough without the added burden of criminal prosecutions based on \textit{Pasquantino}, which will only compound the consequences of circumventing domestic constitutional rights. Is the desire to combat cross-border tax avoidance sufficient reason to allow Canadian and US enforcement officials to devise tax jurisdiction arbitrage schemes that use the criminal law to enforce revenue laws, particularly in a world where tax authorities have expanded access to taxpayer information from other sovereign states?

The opportunities for tax jurisdiction arbitrage also exist domestically. \textit{Pasquantino} conflates the distinctive functions of the US Department of Justice and the State Department when it adopts the view that the executive sanctions criminal prosecutions based on foreign tax laws. Within the executive branch, foreign relations is the domain of the State Department, while the Department of Justice enforces the criminal law. (The interpretation of the law is the responsibility of the judiciary.) There was no evidence that the State Department was consulted in the prosecution of \textit{Pasquantino}, and the two departments regularly clash where their respective areas intersect.\textsuperscript{166} In these circumstances, tax enforcement officials can play off the various departments (including the Treasury) and the SEC to obtain the maximum prosecutorial advantage.\textsuperscript{167}

As the matter now stands, US tax professionals who advise Canadians, and the Canadian professionals they advise, are subject to charges of conspiring to evade taxes when they use American wire services to plan or effect aggressive tax-avoidance schemes over the objections of governments increasingly concerned about the erosion of their tax base.\textsuperscript{168} It is a commonly held view that multinational corporations often engage in aggressive tax minimization that borders on, if not actually constitutes, evasion of taxes due in the country of origin. As one author has noted, “much of the income earned by multinationals from cross-border transactions is likely to escape the income tax altogether.”\textsuperscript{169} For those who might believe that tax evasion is only tangentially related to other forms of white-collar criminal prosecutions, one should note that those engaged in surveillance of organized crime and money laundering consider tax evasion as part and parcel of their job description, with the common elements being cross-border transactions and jurisdictions with bank secrecy laws. “Consequently, both in the domestic context and in cooperative international initiatives, national authorities have often taken an integrated approach to tax and non-tax law enforcement.”\textsuperscript{170}

\textsuperscript{166} One widely publicized example was the conflict between former Secretary of State Colin Powell and former Attorney General Alberto Gonzales over the application of the Geneva Conventions to the war on terror.


\textsuperscript{168} Rearden, supra note 66, at 234, note 289.


\textsuperscript{170} McCracken, supra note 150, at 1893.
Use of American criminal law to enforce Canadian tax laws is almost by definition contrary to the public policy of Canada as expressed in its tax laws. Consider a hypothetical case on facts similar to *McNab*, where a special “sin” tax law was passed to impose a cost on polluters in order to assuage environmentalists, on the tacit understanding that domestic law enforcement officials would not be given the resources to enforce the tax in order to balance the interests of declining industries that could not bear additional costs.171 Alternatively, suppose the tax legislation contains relatively nominal fines for a breach of the law such that the costs of compliance outweigh the fines, and the fines are therefore treated as a licensing fee to pollute. On the basis of *McNab* and *Pasquantino*, American prosecutors could use such legislation as leverage and, if pressed, could seek to secure a conviction far in excess of what the domestic law makers envisioned. It is hard to argue with the following comment on the implications of imposing an American criminal sentence instead of imposing a penalty based on the non-payment of Canadian taxes:

> At a time when international scorn arising from the widespread sense of American arrogance in world affairs is at a high level, it is injudicious to ignore the revenue rule and use American courts to interpret foreign law as a subversive means of asserting American policies that are potentially unwelcome in foreign legal systems.172

It is possible that American overreaching will reach a point where Canadian companies are caught between the domestic law and fear of American criminal prosecution—the Canadian law in question being the Foreign Extraterritorial Measures Act173 (FEMA). One can foresee the imposition of FEMA penalties where Canadian taxpayers yield to a foreign government’s attempts to overreach into Canada’s tax jurisdiction, by paying taxes to that government which are owed to Canada. The penalty for a firm is a fine of up to $1.5 million, and for an individual a fine of up to $150,000 or imprisonment for a term not exceeding five years, or both. In any battle between Canada and the United States over where tax should be paid because the Canada-US treaty is vague, the Helms-Burton Act174—like American tax legislation and Canadian retaliation under FEMA—would place Canadian corporations, their managers, and their advisers in an extremely difficult position that a more robust application of the revenue rule avoids.

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171 I express no view on the Canadian government’s endorsement of the Kyoto Protocol without any legislative implementation mechanism.


173 RSC 1985, c. F-29, as amended.

174 The Cuban Liberty and Democratic Solidarity (Libertad) Act of 1996 (Helms-Burton Act, 22 USC sections 6021-6091) is a US federal law that continues and strengthens the US embargo against Cuba. The Act extends the territorial application of the initial embargo to apply to foreign companies trading with Cuba, and penalizes foreign companies allegedly “trafficking” in property formerly owned by US citizens but expropriated by Cuba after the Cuban revolution.
The potential for forum-shopping by Canadian enforcement officials does not end with the American federal jurisdiction. For example, the CRA could rely on a criminal conviction under the laws of one of several states, and the “full faith and credit” provision of the US constitution to obtain a civil RICO-like restitution order from a friendly state, allowing it to forum-shop between state and federal courts, the US attorney general’s office, and the state district attorney's office. As the petitioners noted in *Pasquantino,*

> [t]he fact that the unintentional violation of an obscure foreign tax law could result in criminal penalties under the wire fraud statute could have chilling implications for all U.S. businesses that are involved in international transactions. . . .

> [E]ven if the Executive branch were able to limit offense to foreign governments by controlling federal wire fraud prosecutions based on foreign tax evasion, it could do little to exercise the same kind of control over prosecutions brought by state and local prosecuting authorities under state analogues to RICO. Some twenty-nine of these statutes use federal mail and wire fraud as a predicate offense. *Accordingly, if this Court determines that schemes to evade foreign taxes are actionable federal mail and wire fraud, it will effectively give rise to twenty-nine different crimes under state law.*

American state sales taxes are premised on a physical presence in a jurisdiction—a concept so incoherent in a world of over $150 billion Internet sales per year that each state government loses 3 percent of its sales tax revenue annually because of the inability to obtain information about Internet sales in the state, and then collect tax on those sales. *Pasquantino* provides a remedy to this problem. As a result, every multinational enterprise that has avoided state taxes by way of Internet transactions may be implicated in a tax-evasion criminal conspiracy.

It is worth recalling that the Canada-US tax treaty provides that each country will assist in the collection of certain tax debts of its residents owed to the other state: the United States will assist Canadian tax authorities in collecting adjudicated revenue claims against US residents, and vice versa; but neither country can pursue residents of the other state for unpaid domestic taxes. As noted earlier, David Pasquantino (as a US citizen) was not subject to the treaty. The ruling in *Pasquantino,* via the impact territoriality argument, allows the United States to use its domestic criminal law to

175 Article IV, section 1 of the Constitution of the United States of America states, in part, “Full Faith and Credit shall be given in each State to the public Acts, Records, and judicial Proceedings of every other State.”

176 *Pasquantino,* petitioner's brief, supra note 101, at 22 and 27 (emphasis added).


pursue Canadian residents for unpaid American taxes as part of a cross-border criminal wire fraud scheme or other form of criminal conspiracy. Thus, evasion of American tax laws thought to be “fair practice” by Canadians is now criminalized, as is evasion (or perceived evasion) of Canadian tax laws by US residents. The result is revolutionary. As one American commentator has noted,

[i]mpact territoriality allows application of United States law . . . where an individual outside the United States has caused consequences within. Impact territoriality is the theory that provokes the most friction with foreign governments as activities considered entirely innocent abroad [such as evasion of another country’s taxes], and undertaken primarily with an eye to their foreign consequences, might nevertheless be punished in American courts.179

The Pasquantino decision will likely throw transborder tax planning into chaos. By way of example, consider that, had David Pasquantino sought a tax opinion, based on the law as it stood before his trial, he might have been advised that a foreign tax assessment would not be enforceable against him in the United States; and a criminal lawyer might have assured him that the federal anti-smuggling statute only prohibits smuggling into countries with reciprocal legislation criminalizing smuggling into the United States.180 Pasquantino might then have had good reason to believe that he could not be prosecuted in the United States for a violation of Canadian tax law. Now, international tax advisers will find it more difficult to give opinions. For example, a multinational may be a US parent with a subsidiary, call centre, distributor, or computer server in another jurisdiction, where the government is eager to tax non-residents rather than its own citizens by way of discriminatory taxes imposed on those with only a tenuous connection to the foreign jurisdiction.181 Moreover, thanks to McNab, cross-border tax advisers cannot even rely on the domestic courts’ interpretation of their own country’s revenue laws in giving an opinion. The resulting uncertainty has far-reaching implications.

179 Morrison, supra note 137, at 192-93.
Consider a fact situation along the lines of *Canada Trustco*. The form of cross-border leasing involved in that case is only one example of “textbook” tax arbitrage that has traditionally allowed taxpayers to take advantage of inconsistencies in the tax laws of different jurisdictions. In essence, a cross-border capital lease permits both the lessor in Canada and the lessee in the United States to claim depreciation for the same investment: in Canada, we look at the legal form of ownership and conclude that the asset is owned by the lessor, who may therefore claim capital cost allowance annually as a depreciation expense; in the United States, the courts look to the economic substance of the transaction (as is the case under Canada’s provincial personal property security legislation, but not under the federal Income Tax Act) and conclude that the true owner is the lessee, who is therefore entitled to claim the depreciation.

As a result of “the two Davids,” international tax arbitragers now face tax jurisdiction arbitration by domestic enforcement officials. The CRA, for example, may now attempt to collect tax revenue, or deter aggressive tax planning “in an attenuated sense,” by pursuing a tax claim in a foreign jurisdiction, where enforcement officials and the courts hold views of tax law or doctrine (such as the “economic reality” test) that are more in keeping with its own interpretation of Canadian tax legislation. In this way, the CRA may succeed in imposing, in the foreign jurisdiction, an interpretation of the law that may be rejected in the Canadian courts (as occurred, for instance, in *Canada Trustco*).

The decision in *Pasquantino* also demonstrates that when the revenue rule is abandoned, the application of comity—a principle designed to create the certainty and predictability necessary for stable cross-border commercial relationships—can have the opposite effect. As one commentator has noted,

> [f]or U.S.-based corporate tax managers who break foreign laws, sometimes in the name of “aggressive tax planning,” *Pasquantino* could lead to federal investigations—possibly even convictions. And for managers who exploit legal loopholes but still adhere to the letter of the law regarding tax shelters, transfer pricing, or the characterization of foreign revenue, the ruling might bring uncertainty to areas once considered settled.

182 *Canada Trustco*, supra note 28.
183 See Doernberg, supra note 22, at 464-65.
184 *Re Speedrack Ltd.* (1980), 11 BLR 220 (Ont. SC).
186 See Interpretation Bulletin IT-233R, “Lease Option Agreements; Sale Leaseback Agreements,” February 11, 1983, a pre-GAAR interpretation of sale-leasebacks that emphasized the economic reality test then favoured by the CRA.
Let us use transfer pricing as an example. The OECD transfer-pricing guidelines\(^\text{188}\) establish a “hierarchy of methods” of fixing transfer prices—specifically, the comparable uncontrolled price, resale price, cost-plus, profit-split, and transactional net margin methods. Although there is a hierarchy, the taxpayer is supposed to use the method most appropriate in the circumstances, with the hierarchy forming, in effect, a tie-breaking mechanism where methodologies appear equally applicable but produce differing results. The CRA has its own view of how to apply these guidelines.\(^\text{189}\) That view may, of course, differ from the taxpayer’s or tax professional’s view. In addition, “[t]ax authorities may ignore countless pages of documentation only to rely on one or two statements they believe gives their country the right to tax a significant portion of the profits of the global enterprise.”\(^\text{190}\) The taxpayer may have already paid taxes based on its understanding of its tax liability in another jurisdiction, and may then face the prospect of double taxation. Should the CRA be able to employ American criminal charges to intimidate the taxpayer, in order to avoid having its view, as set out in the information circular, tested by the competent authority appointed under the relevant tax treaty, or by a domestic court?\(^\text{191}\)

For Canadian tax advisers and preparers, there is the additional concern that the IRS, which has aggressively pursued US tax advisers and preparers who participate in offensive tax-avoidance schemes,\(^\text{191}\) might use Canadian legislation to try to reach into Canada to attack them.\(^\text{192}\) Canada would then have to make a value judgment as to whether the goal of effectively combatting the Goliath tax-planning industry justified the circumvention of the constitutionally sanctioned means, provided by treaty and by domestic legislation, to investigate, assess, prosecute, and collect unpaid taxes and, where applicable, administer penalties designed to address cross-border tax malfeasance.

Canadian clients have to be concerned because under US tax law, a non-resident alien may be subject to tax on income connected in some manner to the United States. The United States exerts extraterritorial jurisdiction over persons not otherwise subject to US taxes in quite unusual ways; for example, a 30 percent withholding tax is imposed on dividends paid to a non-resident shareholder by a non-resident corporation that derives 25 percent or more of its income from the United States over a two-year period, and a foreign entity that earns “effectively connected business income” (but has no permanent residence) in the United States is subject to US tax on its worldwide business income.\(^\text{193}\) Consider also the IRS’s ability to reassess

\(^{188}\) OECD, *Transfer Pricing for Multinational Enterprises*, supra note 58.


\(^{192}\) Section 163.2 of the Income Tax Act provides for penalties in respect of misrepresentations of tax matters by third parties (such as professional tax advisers and tax preparers).

\(^{193}\) Morrison, supra note 137, at 642-43.
cross-border non-arm’s-length transactions to assign a “reasonable profit,” with only a vague standard of what a reasonable profit is, and whether this may invite a charge of criminal conspiracy to evade American taxes if a Canadian subsidiary resists an IRS investigation.194

Limitations of Domestic Courts in Interpreting Foreign Laws

The use of criminal conspiracy statutes to address alleged violations of foreign tax laws subverts the justice system in several ways:195

- It effectively turns criminal prosecutors and investigators into de facto enforcement agents for foreign tax authorities.
- It engages domestic criminal courts in interpreting and applying foreign tax laws without the benefit of familiarity with the foreign milieu, save for the evidence of foreign tax collection officials.
- Criminal defence counsel are also at a disadvantage, since they are unlikely to be well versed in the tax law of any jurisdiction.

Consider the following characterization of tax law offered by a noted American judge:

In my own case, the words of such an act as the Income Tax, for example, merely dance before my eyes in a meaningless procession; cross-reference to cross-reference, exception upon exception—couched in abstract terms that offer no handle to seize hold of—leave in my mind only a confused sense of some vitally important, but successfully concealed, purport, which it is my duty to extract, but which is within my power, if at all, only after the most inordinate expenditure of time.196

It is easier for such an “overtaxed” judge to rely on Canadian tax officials for an interpretation of Canada’s tax laws than to engage in the arduous task of interpreting the statute without knowledge of the policy context. Moreover, as noted above, defence attorneys in white-collar criminal cases may be equally at sea when it comes to foreign revenue laws; indeed, the National Association of Criminal Defense Lawyers admitted as much in its amicus curiae brief to the US Supreme Court in Pasquantino.197 It appears that putting domestic tax law in the hands of foreign courts not only has negative implications for domestic sovereignty; it does not even provide the corresponding benefit for international commerce that comity usually promises, as the interpretation of laws becomes increasingly uncertain.

194 Ibid., at 640.
195 See Keneally, supra note 92, for a discussion of the issues.
An American judge may maintain that domestic sovereignty concerns are not directly implicated when a foreign sovereign asks for a US interpretation of its law in the course of a criminal prosecution, but consider whom the courts accepted as speaking for Canada in *Pasquantino*. Is it fair to say that the CRA speaks for Canada in foreign affairs? When the CRA seeks foreign assistance in enforcing its tax assessments without the necessity of obtaining a tax judgment, as required by the Canada-US treaty, or is the driving force in prosecuting David Pasquantino without relying on an extradition treaty to bring him to trial in Canada for tax evasion, does it not defy the Canadian sovereign in the form of Parliament, by circumventing treaties ratified by our democratically elected government and avoiding the interpretation of Canada’s tax laws in our courts?

**Use of Foreign Laws To Advance National Policy Objectives**

To some American commentators, the erosion of the revenue rule in *Pasquantino* is justified, as a matter of principle, because the preservation of a foreign country’s tax base supports the programs necessary to maintain domestic peace and public order. *Pasquantino* is therefore seen as an effective tool in the war on terror.\(^{198}\) If this is true, the American executive should be able to obtain the Senate’s consent to a treaty with a foreign power providing for mutual recognition of domestic revenue laws. Otherwise, doesn’t unilateral recognition threaten sovereignty, rather than preserve it?

Adding other elements of the American judicial process to the extraterritorial application of foreign tax laws—specifically, the deference of the judiciary to the executive on the effect of domestic prosecutions based on foreign law,\(^{199}\) the broad investigative powers of American prosecutors (even without a complaint being filed), and the right of prosecutors to take the initiative in commencing any prosecution—we find that we have all the ingredients for the use of tax law as a lever for American prosecutors to investigate international commerce conducted anywhere in the world, supporting the United States’ self-appointed role “as a sort of world economic policeman.”\(^{200}\) In other words, foreign tax laws can be used to extend American criminal laws throughout the world through the conduit of e-commerce and multinational

\(^{198}\) Rearden, supra note 66, at 234-35.

\(^{199}\) Commenting on the decisions in *McNab* and *Pasquantino*, Podgor states, “In both cases the courts found that the United States had jurisdiction to prosecute the conduct because it violated a federal statute in the United States. Both cases gave deference to the executive to proceed with these types of prosecutions, and the majority opinions in both cases were less concerned with the international implications of the decisions.” Podgor, supra note 16, at 94; see also ibid., at 92 and note 76 regarding the US Supreme Court’s specific statement on this point in *Pasquantino*. In Podgor’s view, “the possible impediment to foreign policy” is “[a]t the forefront” of the concerns raised by the US courts’ assumption of jurisdiction to prosecute extraterritorial social harms: ibid., at 101.

\(^{200}\) Gibeaut, supra note 160, at 48. For this view in the context of *Pasquantino*, see Guttman, supra note 67.
transactions. Those who criticize the revenue rule as a relic of a bygone era, which has no place in a world inundated with cross-border transactions, should be careful what they wish for. If comity means that the executive branch is free to carry out its foreign policy through the US attorney general’s office, as the decision in Pasquantino seems to imply, the potential exists for American legal hegemony to supplant both domestic sovereignty and negotiated tax treaties.

Those who regard sovereignty as a “hurdle to international tax reform” should understand that this position strengthens the American view that, as the world’s leading democracy, their country has an obligation to intervene with other nations, and it does not advance the cause of multilateral treaties and international organizations (which many Americans regard as undemocratic and ineffective). According to this view of America’s international role (which has come to be called “the Roosevelt doctrine”), “chronic wrongdoing, or an impotence which results in a general loosening of the ties of civilized society, may . . . force the United States, however reluctantly, in flagrant cases of such wrongdoing or impotence, to the exercise of an international police power.” Attacking the revenue rule as a tool to slay the Goliath of the tax-avoidance industry does not just undermine the sovereignty of other nations; it also supports the Bush administration’s efforts to use domestic and foreign law enforcement to protect and encourage international commerce, and thus to further American economic interests. As one proponent of this view put it,

[...]

While the academic debate presents the issue in terms of the revenue rule versus comity, what is really in dispute is two competing views of the rule of law.

One view supports American enforcement of other countries’ laws in order to thwart criminal conduct that undermines the stability of America and its allies. Under
this view, Canada is a “free rider” that benefits from having its revenue laws vindicated in American courts by American prosecutors. Judicial expression of this view justifies the abrogation of the revenue rule because it “advances . . . [American] interests, and any collateral effect furthering the governmental interests of a foreign sovereign is, therefore, necessarily incidental.”

The competing view defines the rule of law in terms of democratically elected governments making their laws and controlling their own enforcement of those laws, rather than succumbing to foreign powers or the administrative discretion of domestic bureaucrats. “In a tax context, it means that taxes will be imposed through a proper parliamentary process rather than through administrative discretion . . . [granted to tax enforcement officials] empowered effectively to decide what the law is.” Under this paradigm, the taxing power is fundamental to the sovereignty of the state and the democratic control of sovereign power. American overreaching challenges the rule of law in two ways: by displacing a sovereign nation’s control of its laws, and by superseding treaties, which provide protection against foreign intervention and ensure reciprocal treatment of a nation’s citizens in other jurisdictions.

The marriage of convenience between the Bush administration’s post-9/11 laws passed for the purpose of addressing the ongoing war on criminals-without-borders and the CRA’s enforcement officials, tacitly sanctioned by Pasquantino, allows the executive branch to contradict foreign policies sanctioned by the democratically elected Parliament and US Senate under treaty regarding the enforcement of tax judgments (which have gone through due process in Canadian courts) and the extradition of criminals. We are therefore potentially facing a situation where the American executive branch, in the name of international crime fighting, may decide to enforce Canadian tax laws in the United States in order to preserve the effective tax-rate disparity between the two countries and maintain America’s position as a relative “tax haven,” while the CRA in turn gets what it wants—deterrence, and possible collection of taxes for what it considers to be tax evasion, without the burden of getting a tax judgment in Canada. If the CRA also gets restitution in addition to an American criminal conviction with the approval of the US attorney general, that is only a bonus. Even without a restitutionary remedy, the threat of criminal prosecution in the United States is enough to deter most taxpayers from engaging in activities

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206 R.J. Reynolds, supra note 74, at 136.


208 Shore, supra note 172, at 218-19.

209 Lithwick, supra note 157.


211 Ciesla, supra note 151.
that the CRA considers unlawful tax avoidance. Pasquantino and McNab provide the key to foreign tax collectors to use the United States as a sanctuary to collect any kind of tax, or at least deter aggressive cross-border tax planning by professional tax advisers.\footnote{212}

By using American criminal law to implement foreign tax policy, the American judiciary is circumventing treaty restrictions on the recognition of foreign tax laws put in place, or sanctioned, by the legislatures of treaty nations in the name of protecting the integrity of the tax system at the request of the tax collectors. Pasquantino thus invites a larger debate: “Will the citizens of liberal democracies retain the right to determine their own laws and public policies or will they yield these rights to transnational entities in the quest for universal order and justice?”\footnote{213}

**WHAT IS TO BE DONE?**

*The role of taxation and the ways in which tax policy enters into and shapes the political agenda of the contemporary state raises two sets of issues or questions. One involves the matter of who determines policy and how this is done. The other relates to the terms under which political claims, policy analysis, public debate and state commitments are carried out. Put otherwise the first set of concerns raises the question of democracy. . . . Asking who determines policy raises the matter of access to the institutions of political decisionmaking. Democracy is concerned with both the extent and kind of such access. . . . The second set of concerns raises the matter of public discourse or (using the term loosely and generally) ideology.*


Has the time come for us to abandon the revenue rule? If so, we should do so openly and on clearly articulated policy grounds, not surreptitiously, by handing over the decision to enforcement agencies acting outside their authority as established by the constitution and confirmed by statute law.

If the principle of comity is to replace the revenue rule, so be it. Let revenue laws be treated like any other foreign laws that are interpreted and enforced in domestic courts. Acknowledge openly that revenue laws are not analogous to penal laws, and that domestic public policy implications rarely arise because sovereign states that impose revenue laws have developed customs and conventions that ensure a certain uniformity or harmony in the way this is done, based on source of income and territory of origin.\footnote{214} Further, accept explicitly that the domestic tax jurisdiction bears the cost of foreign tax law interpretation and enforcement, as well as the associated risk of misinterpreting foreign laws and the cultural milieu in which they originated.\footnote{215} Finally, be prepared to find that comity may not be applied in all cases—that

\footnotetext{212}{2nd Circuit Holds Foreign Governments Cannot Use RICO,” supra note 181.}

\footnotetext{213}{Judd, supra note 18 (front cover).}

\footnotetext{214}{Silver, supra note 59, at 612 and 617-18; and Kovatch, supra note 63, at 277-83.}

\footnotetext{215}{Compare Burgess, supra note 64, and Briggs, supra note 71.}
the domestic court may refuse to enforce a foreign revenue law where doing so would offend the rules of due process or conflict with domestic commercial interests, or because the law is otherwise considered discriminatory to the domestic jurisdiction.\textsuperscript{216} Do not, however, transform tax law into in terrorem penal law by using statutes such as RICO, the Patriot Act, and wire fraud legislation to enforce domestic revenue laws in foreign criminal courts that are ill equipped to deal with them.

In light of the concerns raised throughout this article, perhaps we should not be too eager to embrace comity as a substitute for the revenue rule. It is worth noting that in civil code countries, the revenue rule overwhelmingly predominates, with some exceptions that allow for reciprocal recognition of tax judgments, and a few anomalies.\textsuperscript{217} It seems that it is only in certain common-law jurisdictions, where the revenue rule is not legislated but is subject to judicial discretion, that its application is in a state of turmoil. Given that academic opinion, though sparse, almost universally supports the growing preference for comity, no one has proposed how this trend might be halted. One possible approach is for tax advisers in Canada to band together with defence counsel in tax litigation in an unprecedented and heretofore unlikely alliance to address the threat to the revenue rule.

Since Canadian law still recognizes the revenue rule as the law of the land, and \textit{Harden} is still the leading precedent, it is not too late to preserve the rule in the face of discouraging recent Canadian precedents, which tend to adopt the \textit{Pasquantino} approach of narrowing the rule by interpreting the “pith and substance” of the matter under adjudication as enforcing domestic criminal law rather than foreign tax claims. What we need is strong advocacy to assert the continuing policy considerations that should discourage our courts from taking anything other than the robust view of the revenue rule that until recently was the norm. Unfortunately, courts have tacitly accepted the prevailing tide of academic opinion that the needs of international comity outweigh the “outdated” policy reasons underlying the rule itself. The recent challenges to the rule have taken place in the context of a milieu where fostering good Canadian-American relations has become increasingly important, and hard cases have indeed resulted in bad law. However, advocates have to invite our courts to consider other types of hard cases.

While \textit{Pasquantino} opens up the possibility of Canadian nationals being prosecuted in the United States under mail or wire fraud legislation, RICO, or some other criminal statute, with an unproven allegation of Canadian tax evasion serving as the predicate offence, we should recognize that a Canadian court could face a similar situation.\textsuperscript{218}


\textsuperscript{218} McCracken observes, supra note 150, at 1891, “Tax evasion is increasingly viewed as the type of financial crime that constitutes a predicate offence to money laundering.”
Consider, for example, the case of the arrest and prosecution of three leading Yukos executives in Russia for tax evasion and fraud. Also consider that one or more of the defendants might have assets hidden in Canada, or seek refugee status here. Let us presume that the following allegations surrounding the prosecution of the three executives are true:

- There was search and seizure of documents in the defence lawyers’ offices, lawyers were summoned for questioning on their clients’ cases, and prosecutors engaged in eavesdropping on defence lawyers.
- The prosecution circumvented the lawyer-client privilege by a simple play on case file numbers: seizing documents from one defendant’s lawyer to allegedly prosecute a co-defendant who was not a client in obviously closely related prosecutions of tax evasion cases against Yukos and its subsidiaries.
- The circumstances surrounding the arrest and prosecution of the leading Yukos executives strongly suggest that this is a clear case of non-conformity with the rule of law, in that these executives were arbitrarily singled out by the authorities because of their religious background and their support of a political rival of the Russian president. In particular, the allegedly abusive practices used by Yukos to minimize taxes were also used by other oil and resource companies operating in the Russian Federation that have not been subjected to a similar tax reassessment, or its forced pre-judgment execution, and whose leading executives have not been criminally prosecuted.
- While the tax laws in question were changed in 2004 and the alleged “loop-hole” thus closed, the incriminated acts dated back to 2000 and a retrospective prosecution started in 2003 before the legislation had even been amended. The criminal charges laid against persons who made use of the possibilities offered by the law as it stood at the time of the incriminated acts, following a retroactive change of the tax law, offend the principles of *nullum crimen, nulla poena sine lege* laid down in article 7 of the European Charter of Human Rights (ECHR), and also the right to the protection of property laid down in article 1 of the first protocol to the ECHR.

Now consider what a Canadian court would do if the Russian tax enforcement officials tried to use arguments such as those in *Pasquantino* to vindicate their charges of tax evasion. A robust view of the revenue rule simply takes the position that this is

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an indirect application or enforcement of foreign tax laws, and refuses jurisdiction. Since the criminal fraud charges in Russia were based on defrauding the Russian government of tax revenue, any similar charges here must be also based on revenue laws, fatally implicating the revenue rule. The court does not have to play diplomat—a problem that does arise when the revenue rule is narrowed at the request of “friendly” foreign states and then the precedents are taken up by those who seek to apply them in less felicitous circumstances.

Under a narrow view of the revenue rule, a Canadian court would have to delve into whether the Russian state’s action was motivated by reasons beyond the mere pursuit of criminal justice, to include such elements as to weaken an outspoken political opponent, to intimidate other wealthy individuals, and to regain control of strategic economic assets. Given that the fact that all of the prosecuted oligarchs are Jewish, would our court be prepared to make a finding that the prosecution was really an attempt to panderm to anti-Semitic sentiment among the Russian electorate for purely political reasons? What if Canada were engaged in an economic development project abroad that depended on assistance from Russia? Could we risk penalizing a country in need, or alienating a fellow-member of the G8? Does our answer change if Canadian tax advisers are alleged to have aided and abetted the tax fraud? Should our courts be engaged in such a foreign relations controversy? If they sided with Russian tax officials, would they be supporting the rule of law by stamping out tax evasion and preserving the Russian tax base, or would they be undermining it by tacitly supporting what some would see as practices that attack the very fabric of the rule of law?

Aside from the concern that small national tax administrations might become the instruments of larger tax administrations as the imperial view of tax enforcement gains momentum, there is the larger concern that tax enforcement officials, quite properly guided by the sole objective of collecting taxes, are not equipped by mandate, temperament, or training, and likely will lack the political acuity, to judge whether the foreign tax enforcement officials with whom they “team” to collect taxes in the domestic jurisdiction are acting on behalf of an inequitable tax regime. These concerns, coupled with the fact that our courts should not have to pass judgment on foreign tax laws, must be asserted as the strongest reasons why our courts should not travel any farther down the road that narrows the revenue rule into oblivion in the name of “comity” between nations.

The alternative approach is to pass domestic legislation, or negotiate treaty amendments, that explicitly recognize the revenue rule. The problem with this approach is that it ignores the fact that the courts do not acknowledge that they are offending the revenue rule; in their view, they are only vindicating the domestic law. Once the courts are convinced that the revenue rule is bad policy, the erosion of the rule is an inevitability. No amount of rewriting of Canada’s general anti-avoidance rule can force a court that views it as bad policy to give it a liberal interpretation. So too is the case with the revenue rule: it must be vindicated as a matter of sound policy in the 21st century, or be reinterpreted into oblivion. While even the harshest critics of the revenue rule recognize that “perhaps its abolition would require safeguards
against capricious, corrupt, or ‘unfair’ fiscal regimes,” they do not explain what those safeguards would be, who determines the “unfairness” of a particular fiscal regime, or why a court is the most appropriate forum for these determinations.

Perhaps the best policy argument against erosion of the revenue rule is the courts’ unfamiliarity with these types of foreign relations issues, and the best policy argument in favour of the revenue rule is found in the following comments of McLachlin J in an unrelated Supreme Court of Canada case:

Generally speaking, the judiciary is bound to apply the rules of law found in the legislation and in the precedents. . . .

There are sound reasons supporting this judicial reluctance to dramatically recast established rules of law. The court may not be in the best position to assess the deficiencies of the existing law, much less problems which may be associated with the changes it might make. The court has before it a single case; major changes in the law should be predicated on a wider view of how the rule will operate in the broad generality of cases. Moreover, the court may not be in a position to appreciate fully the economic and policy issues underlying the choice it is asked to make. Major changes to the law often involve devising subsidiary rules and procedures relevant to their implementation, a task which is better accomplished through consultation between courts and practitioners than by judicial decree. Finally, and perhaps most importantly, there is the long-established principle that in a constitutional democracy it is the legislature, as the elected branch of government, which should assume the major responsibility for law reform.

Considerations such as these suggest that major revisions of the law are best left to the legislature. 221

The courts are not the place to make the profound policy shift that abrogation of the revenue rule portends. The normal basis for taxation is predicated on the existence of this rule. Most states tax their residents on worldwide income and non-residents only on income earned within the state’s jurisdiction. The reason for this determination of tax liability is that it has traditionally been considered impractical to enforce revenue claims outside the state—in no small part because of the revenue rule. While income earned by non-residents outside the state might have some link to the state that might justify a tax claim, the practical limits of enforceability encouraged independent countries, from the time of the League of Nations onward, to agree to grant prior claims based on domestic residence and domestic source.

In a world where the revenue rule seems to have no application, nations ravaged by harmful tax competition can seek to expand their tax base beyond the traditional

220 Robert Couzin, “Imposing and Collecting Tax,” in Brian J. Arnold, Jacques Sasseville, and Eric M. Zolt, eds., The Taxation of Business Profits Under Tax Treaties (Toronto: Canadian Tax Foundation, 2003), 171-200, at 191. Couzin seems to cautiously suggest that these difficult questions might be addressed by a whitelist/blacklist approach or perhaps by treaties or conventions.

boundaries based on consensus, by pursuing extraterritorial claims subject only to the approval of the executive of the foreign jurisdiction. If abrogation of the revenue rule is mutually beneficial because it overcomes the inequitable effects of flat-rate withholding taxes and other exigencies caused by the inability to enforce tax claims against non-residents, we must ask why countries do not address these concerns by employing the usual democratic processes to negotiate a more equitable and rational division of the international tax base. Historically, both in the more distant past and since the events of 9/11, those processes have proved expeditious and effective in addressing international tax issues and other threats to the national interest. In short, there is no valid reason to bypass the authority of the legislature to deal with the growing problem of international tax avoidance.222

CONCLUSION

According to the counsel for the defendants in *Pasquantino*, the decision in that case “should send a chill through every company in America that does business abroad.”223 Tax professionals have expressed their own fears that their aggressive multijurisdictional tax-minimization strategies might result in criminal prosecutions under American criminal law where a similar wire transfer of funds in the execution of such a strategy might constitute a predicate offence. Foreign laws and customs of interpretation and enforcement, and the combination of foreign tax laws and domestic criminal laws, create a great deal of uncertainty for tax professionals worldwide, increasing the cost of international commerce. We can only agree with the advice that “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.”224

Revenue authorities, and others who view the tax-planning industry as a Goliath to be slain, may be unsympathetic to these implications of *Pasquantino*. They may argue that in a globalized marketplace, where national borders are becoming otiose, and illegal or improper commercial conduct in one market has an impact on others, there is a need for international law enforcement, including the enforcement of tax laws. Domestic tax enforcement should not be thwarted by cross-border schemes that threaten the tax base, and ultimately the sovereign power of democratically elected governments that rely on tax revenues to serve their constituents. Some critics maintain that without international cooperation, the “strong fortress” of the


revenue rule only protects the Goliath tax-planning industry. I suggest, however, that this is an incomplete view of the problem of protecting the national tax base.

When national governments have common problems and mutual concerns, they enter into treaties, which are subject to various constitutional constraints that address the norms of the societies from which these governments gain their sovereign legitimacy.

Moreover, there are strong policy reasons to justify retention of the revenue rule in the 21st century, as common-law courts outside the United States continue to affirm.\(^\text{225}\) Significantly, the Canada-US tax treaty refuses to recognize unadjudicated tax claims and recognizes tax judgments only where the competent authority is satisfied that due process of the foreign court meets domestic standards.\(^\text{226}\) When foreign and domestic “revenuers” are allowed to circumvent tax and extradition treaties in their pursuit of tax evaders, prosecutorial discretion by bureaucrats supplants the rule of law. Those who seek to attack the Goliath tax-planning industry in this fashion threaten to bring down the Goliath of democratic institutions instead.

The threat is only compounded when the views of foreign revenue officials on the interpretation of the law are allowed to displace those of the foreign attorney general and the foreign court system, as McNab establishes and Pasquantino reinforces. Although in Pasquantino the Supreme Court stated that the concern about a US court’s ability to interpret foreign law was overblown, it is more than a little disconcerting that the prosecution failed to establish the exact Canadian tax rate or cite any applicable Canadian law or regulation, but instead relied on the general experience of a CRA official (who was not qualified as an expert) to support the “reasonable inference” that a Canadian tax law had been broken, and used that official’s “estimate” of the tax loss to determine the amount of jail time that should be imposed on conviction.\(^\text{227}\) In McNab, in relying on the US attorney general to present the foreign law, the court ignored the opinion of a Honduran court that the American courts had misinterpreted the Honduran law, and in doing so, it offended the Honduran government. The vested interest (or bias) of foreign enforcement officials, coupled with the fact that domestic courts have neither the necessary understanding of the cultural milieu, nor the legal expertise, to interpret the laws of another jurisdiction, supports the view that domestic courts should be reluctant to rely on the executive as a sufficient excuse for them to venture into the deep waters of foreign policy.\(^\text{228}\) Surely international tax avoidance has not advanced so far as to warrant overriding


\(^{226}\) Mallinak, supra note 7.

\(^{227}\) See Terwillinger, supra note 180; and Pasquantino, supra notes 9 (SC), at 1768, and 94 (4th Circuit), at 323.

\(^{228}\) Mallinak, supra note 7, at 79.
all democratic values and constitutional protections. Does taxpayer avoidance of domestic tax laws justify the revenuers’ avoidance of domestic courts and legislated treaty requirements? Although tax avoidance may sap sovereignty by draining states’ coffers of the tax revenue that they need to sustain them, does not circumventing treaties and domestic tribunals pose at least as ominous a threat? These are the important questions that “the two Davids” pose.

In this article, I have argued that the traditional reasons for preserving the revenue rule remain intact. The domestic judiciary should be the interpreter of complicated domestic revenue laws. The executive and legislative branches of government are the best judges of domestic public policy in the recognition of foreign tax laws, not revenue officials or the courts. Domestic courts are poor interpreters of foreign tax laws. The expense of interpreting and enforcing tax laws should be borne by their country of origin. Domestic tax systems can protect themselves through tax and extradition treaties, withholding taxes, and domestic enforcement against local branches of multinational enterprises, without abrogating the common-law revenue rule. Application of foreign revenue laws in the name of domestic crime fighting only encourages the type of international overreaching that brings to the forefront sovereignty issues that the revenue rule is designed to avoid.229

The US Supreme Court’s view in Pasquantino that the secretary of state can theoretically intervene to control prosecutorial discretion and impose executive control does not address the circumvention of Congress’s treaty ratification powers.230 Nor does it address the lack of federal oversight with respect to overzealous prosecutors who (following the example of Rudy Giuliani and Eliot Spitzer) seek to build their public reputation and advance their political career by taking on multinational corporations in malum in se criminal prosecutions with serious penal consequences, in order to enforce malum prohibitum foreign tax revenue violations with less drastic consequences.231 Ignoring the revenue rule in favour of comity in the application of foreign revenue laws decreases certainty and therefore hinders international trade. In present circumstances, it is almost impossible for a tax adviser to render an international tax opinion, particularly where a client engages in cross-border commerce in multiple jurisdictions.232 “The two Davids” have given tax enforcement officials

229 See, for example, Fountain v. US, 357 F. 3d 250, at 252 (2d Cir. 2004), a precursor to the ultimate decision in Pasquantino, which used breach of Canadian cigarette tax-evasion laws as the predicate offence for wire fraud.

230 In United States v. Alvarez-Machain, 504 US 655, at 669 (1992), the court deferred to the executive in sanctioning the abduction of a doctor from Mexico to stand trial in the United States. This shocking violation of general international law principles, as well as any recognized concept of comity, exposed as a fiction any claim that a conservative government was capable of protecting international relations. Compare C & S Air Lines v. Waterman Corp., 333 US 103, at 111 (1948), declaring that foreign policy is delegated jointly to the executive and legislative branches of government.

231 Podger, supra note 16, at 98.

232 See supra note 181.
a new weapon in their attack on the Goliath tax-avoidance industry, raising the
danger that the revenue rule may be supplanted by “the rule of the revenuers,” with
fatal consequences for democratic sovereignty. We should heed the warning of Sir
Thomas More in *A Man for All Seasons*:

Roper: So now you’d give the Devil benefit of law!

More: Yes. What would you do? Cut a great road through the law to get after the
Devil?

Roper: I’d cut down every law in England to do that!

More: Oh? And when the last law was down, and the Devil turned round on you,
where would you hide, Roper, the laws all being flat? This country’s planted
thick with laws from coast to coast—man’s laws, not God’s—and if you cut
them down—and you’re just the man to do it—do you really think you
could stand upright in the winds that would blow then? Yes, I’d give the
Devil benefit of law, for my own safety’s sake.\(^{233}\)

APPENDIX  ARTICLE XXVI A OF THE CANADA-US TAX TREATY

The full text of article XXVI A, as it currently reads, is reproduced below.

Article XXVI A
Assistance in Collection

1. The Contracting States undertake to lend assistance to each other in the collection of taxes referred to in paragraph 9, together with interest, costs, additions to such taxes and civil penalties, referred to in this Article as a “revenue claim.”

2. An application for assistance in the collection of a revenue claim shall include a certification by the competent authority of the applicant State that, under the laws of that State, the revenue claim has been finally determined. For the purposes of this Article, a revenue 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.

3. A revenue claim of the applicant State that has been finally determined may be accepted for collection by the competent authority of the requested State and, subject to the provisions of paragraph 7, if accepted shall be collected by the requested State as though such revenue claim were the requested State’s own revenue claim finally determined in accordance with the laws applicable to the collection of the requested State’s own taxes.

4. Where an application for collection of a revenue claim in respect of a taxpayer is accepted
   (a) by the United States, the revenue claim shall be treated by the United States as an assessment under United States laws against the taxpayer as of the time the application is received; and
   (b) by Canada, the revenue claim shall be treated by Canada as an amount payable under the Income Tax Act, the collection of which is not subject to any restriction.

5. Nothing in this Article shall be construed as creating or providing any rights of administrative or judicial review of the applicant State’s finally determined revenue claim by the requested State, based on any such rights that may be available under the laws of either Contracting State. If, at any time pending execution of a request for assistance under this Article, the applicant State loses the right under its internal law to collect the revenue claim, the competent authority of the applicant State shall promptly withdraw the request for assistance in collection.

6. Subject to this paragraph, amounts collected by the requested State pursuant to this Article shall be forwarded to the competent authority of the applicant State. Unless the competent authorities of the Contracting States otherwise agree, the ordinary

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234 See the Canada-US tax treaty, supra note 10. For forthcoming amendments, see the fifth protocol, supra note 141.
costs incurred in providing collection assistance shall be borne by the requested State and any extraordinary costs so incurred shall be borne by the applicant State.

7. A revenue claim of an applicant State accepted for collection shall not have in the requested State any priority accorded to the revenue claims of the requested State.

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
   (a) where the taxpayer is an individual, the revenue claim relates to a taxable period in which the taxpayer was a citizen of the requested State, and
   (b) where the taxpayer is an entity that is a company, estate or trust, the revenue claim relates to a taxable period in which the taxpayer derived its status as such an entity from the laws in force in the requested State.

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 of a Contracting State.

10. Nothing in this Article shall be construed as:
   (a) limiting the assistance provided for in paragraph 4 of Article XXVI (Mutual Agreement Procedure); or
   (b) imposing on either Contracting State the obligation to carry out administrative measures of a different nature from those used in the collection of its own taxes or that would be contrary to its public policy (ordre public).

11. The competent authorities of the Contracting States shall agree upon the mode of application of this Article, including agreement to ensure comparable levels of assistance to each of the Contracting States.

The fifth protocol to the treaty235 will make the following amendments to article XXVI A:

Article 22

1. Subparagraph 8(a) of Article XXVI A (Assistance in Collection) of the Convention shall be deleted and replaced by the following:

   (a) Where the taxpayer is an individual, the revenue claim relates either to a taxable period in which the taxpayer was a citizen of the requested State or, if the taxpayer became a citizen of the requested State at any time before November 9, 1995 and is such a citizen at the time the applicant State applies for collection of the claim, to a taxable period that ended before November 9, 1995; and

2. Paragraph 9 of Article XXVI A (Assistance in Collection) of the Convention shall be deleted and replaced by the following:

   9. Notwithstanding the provisions of Article II (Taxes Covered), the provisions of this Article shall apply to all categories of taxes collected, and to contributions to social security and employment insurance premiums levied, by or on behalf of the Government of a Contracting State.

235 Supra note 141.