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Recommended Citation

Herrick K. Lidstone, *Liberal Construction of Tax Treaties An Analysis of Congressional and Administrative Limitations of an Old Doctrine*, 47 Cornell L. Rev. 529 (1962)
Available at: <http://scholarship.law.cornell.edu/clr/vol47/iss4/2>

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LIBERAL CONSTRUCTION OF TAX TREATIES—AN ANALYSIS OF CONGRESSIONAL AND ADMINI- STRATIVE LIMITATIONS OF AN OLD DOCTRINE

Herrick K. Lidstone†

Automatic data processing, identification numbers for taxpayers, withholding of income tax from dividends and interest, and tax subsidies for investments in new equipment, revolutionary as they are in United States tax philosophy,¹ could normally have been expected to obscure the bitter infighting over those portions of H.R. 10650, the Revenue Bill of 1962, which prescribe new rules for taxation of foreign income.² However, two years of publicizing the flow of gold toward Europe have so dramatized the possibilities for income tax avoidance (and even evasion) in foreign operations and through foreign bank accounts and tax havens that envious taxpayers can almost sympathize with Ingemar Johansson's failure to convince the district court that he was the fighting chattel of a Swiss corporation.³

From 1954 to 1961 the political battle was for freedom from income tax on foreign earnings. Today, the protagonists, who are now concerned with maintaining their present advantages, are faced not only with the impact of H.R. 10650 on international operations but also with the Treasury's pressure for more strenuous measures.

Although almost half of the bulk of H.R. 10650 relates to foreign operations and investments, few taxpayers will be directly affected by the bill's provisions.⁴ Indeed, since the House bill has followed pre-

† See contributors' section, masthead p. 631, for biographical data.

¹ Although the Martinsburg, West Virginia, experiment in automatic data processing will almost certainly attract interest and attention throughout the world, tax administrators from the least developed country are undoubtedly wondering why there is any fuss about taxpayers' numbers or withholding of tax from dividends, interest, etc. Many countries long ago instituted withholding from dividends and interest. Puerto Rico represents the most famous experiment of subsidizing new investment through the tax system.

² H.R. 10650, 87th Cong., 2d Sess. (hereinafter cited as H.R. 10650), originally contained twenty-one sections of which twelve dealt entirely with problems, both substantive and administrative, of foreign income or assets.

³ *United States v. Johansson*, — F. Supp. — (D.C. Fla. 1961). Race horses obviously fare better than fighters. Rev. Rul. 58-63, 1958-1 Cum. Bull. 624; cf. Rev. Rul. 60-249, 1960-2 Cum. Bull. 264.

⁴ H.R. 10650, § 5 (distributions of property by foreign corporations), § 6 (allocation of income), § 7 (foreign personal holding companies), § 15 (foreign investment companies), and § 19 (administrative provisions). Similarly, few taxpayers will be very much concerned with § 11 which requires the inclusion in gross income of foreign income taxes before the foreign tax credit will be allowed or with § 19(c)(1), which, regardless of tax treaty provisions to the contrary, requires withholding of income tax from payments to nonresident aliens and foreign corporations to be at a minimum of 20%. But see 108 Cong. Rec. 4890-91 (daily ed. March 28, 1962) (remarks of Congressman Bow) and 108 Cong. Rec. 7169-70 (daily ed. May 3, 1962) (remarks of Congressman Betts).

dictable routes to reduce the individual advantages for those fortunate taxpayers who have been able to arrange foreign residences and property ownership to achieve substantial tax benefits,⁵ most people must be having real difficulty in understanding the reason for the hue and cry against the House's proposals. On the other hand, some of the bill's provisions,⁶ representing new and rather drastic approaches to old problems, may present difficulties to legitimate business enterprises because past business practices may have created situations which cannot be changed to meet the proposed new criteria in United States tax law. Nevertheless, in spite of the number of pages devoted to "foreign problems" and the complications they will raise not only for the taxpayers but also for the Internal Revenue Service, it is section 21 of H.R. 10650 which, in the last three lines of the House bill, can create the greatest obstacles to international trade and investment: "Section 7852(d) of the Internal Revenue Code of 1954 (relating to treaty obligations) shall not apply in respect of any amendment made by this Act."⁷

It is not difficult to presage that these few words, which in sweeping terms abrogate various provisions in each of our twenty-one tax treaties, will lead to new and not necessarily welcome negotiations at least with the twenty-one tax treaty countries. The mere proposal of the amendment contained in section 21, combined with two recent decisions, one of the Court of Appeals for the Second Circuit⁸ and the other a Revenue Ruling,⁹ both of which are quite correct but unfortunately timed, guarantees an early end to the doldrums which have deterred progress with income tax treaties. The curious coincidence of H.R. 10650, the *Maximov* case and Rev. Rul. 62-31 occurs when there are three income tax treaties signed but pending ratification by the Senate¹⁰ and when the

⁵ H.R. 10650 § 9.

⁶ Particularly H.R. 10650, § 13 (controlled foreign corporations) and § 16 (gain from sales or exchanges of stock in foreign corporations).

⁷ Int. Rev. Code of 1954, § 7852(d) provides as follows: "No provision of this title shall apply in any case where its application would be contrary to any treaty obligation of the United States in effect on the date of enactment of this title."

⁸ *United States v. Maximov*, 299 F.2d 565 (2d Cir. 1962). See discussion *infra*, note 93.

⁹ Rev. Rul. 62-31, 1962 Int. Rev. Bull. No. 11, at 21 which revoked Rev. Rul. 54-588, 1954-2 Cum. Bull. 657. Rev. Rul. 54-588 erroneously had held that a United Kingdom corporation did not have a permanent establishment in the United States within the meaning of the tax treaty with the United Kingdom even though it maintained a showroom and samples in the United States for the solicitation of orders which were subject to acceptance and fulfillment in England.

¹⁰ Income Tax Agreement with India, November 10, 1959; with Israel, September 30, 1960; and with the United Arab Republic, December 21, 1960. It is particularly interesting to note that, while the twenty-one existing treaties and the proposed treaty with India, with minor variations, are entitled conventions for the avoidance of double taxation and the prevention of fiscal evasion, the title to the proposed treaty with Israel refers to "Encouragement of International Trade and Investment" and that with the United Arab Republic to "Elimination of Obstacles to International Trade and Investment" in addition to the traditional "avoidance of double taxation" language.

Treasury has announced¹¹ discussions with The Netherlands on the existing Income Tax Convention with The Netherlands.¹²

When the Senate finally considers the Indian, Israeli and United Arab Republic treaties, after the enactment or rejection of H.R. 10650, it will be forced to reject a number of specific provisions in these tax treaties in order to maintain a consistent treaty pattern. Furthermore, the Senate will probably suggest that the treaties be renegotiated. Long delays arising from rejection of specific provisions and suggestions for renegotiation of signed treaties, however, are not without precedent: The first "pure" income tax treaty, *i.e.*, the 1932 treaty with France¹³ was delayed for three years and the treaty with the Union of South Africa¹⁴ for more than five and one-half years.

The sweeping provisions of section 21 of H.R. 10650 are disturbing not only because they can be interpreted as a proposed legislative reversal of the trend to encourage tax treaties, but also because section 21 can be interpreted by officials of other countries as an unprecedented disavowal of treaty obligations.¹⁵

Within our constitutional system it has long been settled that treaty obligations and federal statutes are of equal rank so that the more recent, whether a treaty or a statute, can abrogate or supersede the older.¹⁶ Having clearly determined the constitutional position of treaties and statutes, the courts have tried to be equally helpful in establishing rules of interpretation and construction:

¹¹ Treasury Department Release, February 27, 1962. Periodic reviews of tax treaties, of course, are perfectly normal (see Treasury Announcement 61-65, 1961 Int. Rev. Bull. No. 32, at 33, regarding proposed discussions on the Japanese treaty).

¹² April 29, 1948, T.D. 5778, 1950-1 Cum. Bull. 92, extended to the Netherlands Antilles by Protocol, June 15, 1955 6 U.S.T. & O.I.A. 3696 (effective November 10, 1955).

¹³ IV Treaties, Conventions, International Acts, Protocols and Agreements between the United States and other Powers (hereinafter referred to as "TCIA") 4184, April 27, 1932 (proclaimed April 16, 1935). World War II explains the extended delay between the signing of the present treaty with France (T.D. 5499, 1946-1 Cum. Bull. 134) on July 25, 1939 and January 5, 1945, the date the treaty was proclaimed by the President.

¹⁴ Signed December 13, 1946; ratifications exchanged July 15, 1952, see S. Ex. 0, S. For. Rel. Comm., 80th Cong., 1st Sess. (1950); S. Ex. Rep. No. 1, S. For. Rel. Comm., 81st Cong., 1st Sess. (1951).

¹⁵ In eight hours of debate on March 28-29, 1962, covering over 100 pages of the Congressional Record, it is surprising that less than 500 words were devoted to the problem of potential disregard of treaty obligations. 108 Cong. Rec. 4902 (daily ed. March 28, 1962) (remarks of Congressman Meader). Cf. 108 Cong. Rec. 7169-70 (daily ed. May 3, 1962) (remarks of Congressman Betts).

¹⁶ Head Money Cases, 112 U.S. 580 (1884); The Cherokee Tobacco, 78 U.S. 616 (1870); The Constitution of the United States of America 420 (Corwin ed. 1952); Potter, Relative Authority of International Law and National Law in the United States, 19 Am. J. Int'l Law 315 (1925). So well settled is this doctrine that political and scholarly debates have been limited to discussion of the merits of Senator Bricker's proposal to reduce the effect of the treaty making power. For example, see Perlman, "On Amending the Treaty Power," 52 Colum. L. Rev. 825 (1952); Preuss, "On Amending the Treaty-Making Power: A Comparative Study of the Problem of Self-Executing Treaties," 51 Mich. L. Rev. 1117 (1953); Sutherland, "The Bricker Amendment, Executive Agreements, and Imported Potatoes," 67 Harv. L. Rev. 281 (1953).

The principles which should control the diplomatic relations of nations, and the good faith of treaties as well, require that their obligations should be liberally construed so as to effect the apparent intention of the parties to secure equality and reciprocity between them. . . . Upon like ground, where a treaty fairly admits of two constructions, one restricting the rights that may be claimed under it and the other enlarging them, the more liberal construction is to be preferred.¹⁷

Continuing efforts on the part of the courts have extended the liberal construction rule to a holding that, in spite of the complementary rule that a later act of Congress supersedes an inconsistent treaty provision, a treaty is not abrogated if the inconsistent later statute is only a re-enactment of the statute which was superseded by the treaty.¹⁸

Although the courts might interpret the amendments made by H.R. 10650 so that they would not supersede treaty obligations, Congress could easily accomplish its purposes either by clear draftsmanship or by specific references in the committee reports of its intention that specified treaty obligations be superseded.¹⁹ Indeed, the amendments to the tax credit rules to require corporations to include as additional gross income the "deemed" foreign tax credit allowed under section 902 of the Internal Revenue Code of 1954 so clearly supersede the present more favorable rule²⁰ which is incorporated in fourteen treaties²¹ that section

¹⁷ *Jordan v. Tashiro*, 278 U.S. 123, 127 (1928). *Geofroy v. Riggs*, 133 U.S. 258 (1890); *Hauenstein v. Lynham*, 100 U.S. 483 (1879).

¹⁸ *Cook v. United States*, 288 U.S. 102 (1933).

¹⁹ *Ibid.* In *Ross v. Pan Am. Airways, Inc.*, 299 N.Y. 88, 85 N.E.2d 880, 77 N.Y.S.2d 257 (1949), the court used for interpretive assistance the letter of transmittal with which the Secretary of State forwarded the Warsaw Convention to the President prior to transmission of the proposed treaty to the Senate for ratification. *Id.* at 97-98, 85 N.E.2d at 885.

²⁰ H.R. 10650 § 11. See the general explanation of the effect of the present rate differential, H.R. Rep. No. 1447, 87th Cong., 2d Sess. 50-52 (1962). See also *American Chicle Co. v. United States*, 316 U.S. 450 (1942). Although the subject has been much discussed, the most thorough examinations of the benefits of deemed tax credit computations are: *United Nations, United States Income Taxation of Private United States Investment in Latin America (ST/ECA/18)* (1953), and *Owens, The Foreign Tax Credit* 113-18, 126, 137-46 (1961). See also the clear and simplified elimination of treaty rate reductions incorporated in H.R. 10650 § 19(c)(1).

²¹ Tax treaties which freeze the foreign tax credit provisions as they existed on the date of signing the treaty: Australia, art. XV(1), May 14, 1953 [1953] 4 U.S.T. & O.I.A. 2264; Honduras, art. XVI(1)(a), June 25, 1956 [1957] 8 U.S.T. & O.I.A. 219; New Zealand, art. XIII, March 16, 1948 [1951] 2 U.S.T. & O.I.A. 2378; Pakistan, art. XV(1), July 1, 1957 [1959] 10 U.S.T. & O.I.A. 984; treaties which freeze the tax credit provisions as they existed on the date of entry into force of the treaty: Austria, art. XV, Oct. 25, 1956 [1957] 8 U.S.T. & O.I.A. 1699; Belgium, art. XII(2), Oct. 28, 1948 [1953] 4 U.S.T. & O.I.A. 1647; Finland, art. XV(1)(a), March 3, 1952 [1952] 3 U.S.T. & O.I.A. 4464; Germany, art. XV(1)(a), July 22, 1954 [1954] 5 U.S.T. & O.I.A. 2768; Ireland, art. XIII(1), Sept. 13, 1949 [1951] 2 U.S.T. & O.I.A. 2294; Norway, art. XIV(1)(a), June 13, 1949 [1951] 2 U.S.T. & O.I.A. 2353; Switzerland, art. XV(1)(a), May 24, 1951 [1951] 2 U.S.T. & O.I.A. 1751; Union of South Africa, art. IV(1), Dec. 13, 1946 [1952] 3 U.S.T. & O.I.A. 3821. Treaties which freeze the tax credit provisions as of a fixed date: Japan, art. XIV(a) as at January 1, 1954, April 16, 1954 [1955] 6 U.S.T. & O.I.A. 149, and United Kingdom, art. XIII(1) (as amended by art. II of the supplementary Protocol, August 19, 1957) as at January 1, 1956, Aug. 19, 1957 [1958] 9 U.S.T. & O.I.A. 1329. Cf. the remarks of Congressman Betts on the effect of the "abrogation" of these treaty provisions, 108 Cong. Rec. 7169-70 (daily ed., May 3, 1962). The Treasury's counter-argument that the "savings

21 is unnecessary. The disallowance²² of the foreign tax credit for failure to file the detailed information about foreign operations²³ clearly modified the same treaty provisions and it was not considered necessary or advisable to specify the superseding nature of 1960 amendments.

Prior to the enactment of section 7852(d) as part of the 1954 Code,²⁴ Congress, being more concerned with the recognition of treaty rights, included treaty responsibility recognition provisions in all bills which might have restricted or amended treaties.²⁵ Certainly, the coincidence of the recent reversal of the highly favorable "permanent establishment" ruling,²⁶ the reversal of the *Maximov* case,²⁷ and the Treasury's acceptance of the foreign income provisions of H.R. 10650 pending further study of its own proposals²⁸ cannot be interpreted as a political climate favorable to treaties or to treaty obligations.

Although a reappraisal of treaty policy is not unexpected in the present circumstances of the flow of gold and monetary resources from the United States, the first significant public attacks arising in the field of taxation have surprised and disturbed many persons.²⁹ Even though

clauses" in the various treaties [Australia, none; Honduras, art. XVI(1)(a), supra; New Zealand, none; Pakistan, none; Austria, art. XV(1), supra; Belgium, art. XII(2), supra; Finland, art. XV(1)(a), supra; Germany, art. XV(1)(a), supra; Ireland, none; Norway, art. XIV(1)(a), supra; Switzerland, art. XV(1)(a), supra; Union of South Africa, art. IV(1), supra; Japan, art. XIV(a), supra; United Kingdom, none], exempts the proposed action from the status of abrogation of the treaties is not convincing: Five treaties have no savings clause; the others incorporate the tax credit provisions in the sentence immediately following the savings clause; and the Treasury previously conceded that similar tax credit provisions acted to freeze credit provisions as they existed on the specified effective dates: "It is believed to be undesirable to stabilize as of a particular date the laws relating to tax credits." Letter, June 29, 1950, with which the June 1950 amendments to the Canadian treaty were transmitted by the Secretary of State to the President. Since most of the tax treaties referred to above were negotiated, signed, or proclaimed effective after June 29, 1950, it is reasonable to assume that stabilization of the tax credit provisions was in fact desired by the treaty negotiators, the Senate and the President.

²² Int. Rev. Code of 1954, § 6038(b).

²³ Int. Rev. Code of 1954, § 6038(a).

²⁴ See Report of the Committee on Finance to Accompany H.R. 8300, S. Rep. No. 1622, 83d Cong., 2d Sess. 627-28 (1954).

²⁵ Revenue Act of 1941, § 108; Revenue Act of 1942, § 109; Revenue Act of 1943, § 136; Revenue Act of 1950, § 214; Revenue Act of 1951, § 615.

²⁶ Rev. Rul. 62-31, 1962 Int. Rev. Bull. No. 11, at 21, revoking Rev. Rul. 54-588, 1954-2 Cum. Bull. 657. See note 9 supra.

²⁷ 299 F.2d 565 (2d Cir. 1962).

²⁸ Treasury Department Release, July 28, 1961; House Ways & Means Committee Release, July 20, 1961; Remarks of Stanley S. Surrey, Assistant Secretary of the Treasury, Before the Annual Meeting of the American Institute of Certified Public Accountants, Chicago, Illinois, November 1, 1961; Testimony of Douglas C. Dillon, Secretary of the Treasury, before the Senate Finance Committee, April 2, 1962 (New York Times, Apr. 13, 1962, 1, 24). See also the President's Recommendations on Tax Revision, 1 H.R. Doc. No. 140; Hearings on the Tax Recommendations of the President, Comm. on Ways and Means, 87th Cong., 1st Sess. 3, 8-10 (1962); Statement of Secretary of the Treasury Dillon, 1 Hearings, op. cit. 253. For comments of various interested taxpayers and experts, see 4 Hearings, op. cit. 2587-3551.

²⁹ For example, on March 29, 1962 while the debate on H.R. 10650 was progressing in the House of Representatives, Senator Morton presented the Senate with "Facts and Fables on American Investment Abroad," 108 Cong. Rec. 5042-46 (daily ed., March 29, 1962). See also note 21, supra.

many sophisticated persons undoubtedly have recognized (and perhaps even have acknowledged) that the present tax laws permit considerable avoidance of United States income taxes, there are justifiable grounds for complaint against the "meat axe" approach initially suggested by the Treasury and partially adopted in H.R. 10650.

Since most of our tax treaties are with European countries the legal systems of which differ both historically and functionally from that of the United States, Congress' willingness to consider the approach proposed in section 21 of H.R. 10650 (whether or not the section is included in the final act) may affect European interpretations not only of income tax treaties with the United States but also of the numerous treaties of friendship, commerce, and navigation.

The philosophy of continental countries is generally that international law should take precedence over municipal law.³⁰ French lawyers are proud of their constitutional provisions³¹ which state, in effect, that, since diplomatic treaties are superior in authority to French internal legislation, treaty provisions "shall not be abrogated, modified or superseded without previous former denunciation through diplomatic channels."³²

During the early 1950's the French courts frequently considered the relationship between treaties and municipal laws, and since they developed interpretative guides which differ from those of the United States, a brief review of their problems and attendant solutions may be helpful.³³

The Franco-Spanish Consular Convention of January 7, 1862, provides that citizens of one contracting state, who are authorized to reside in the territory of the other, may engage in the other state in any kind of industry or commerce and shall pay only the duties and taxes and observe only the laws and regulations enforced for nationals of the state in which the foreigner resides. A French Decree Law of January 12, 1938, required that aliens obtain special identity cards before they would be permitted to engage in a commercial or industrial profession in France.

The issue presented to various French courts was whether the 1938 Decree Law was applicable to aliens entitled to the benefits of the

³⁰ See Erades & Gould, *The Relation Between International Law and Municipal Law in The Netherlands and in the United States*, pt. V (1961); Bial, "Some Recent French Decisions on the Relationship Between Treaties and Municipal Law," 49 *Am. J. Int'l Law* 347 (1955); Preuss, "The Relation of International Law to Internal Law in the French Constitutional System," 44 *Am. J. Int'l Law* 641 (1950).

³¹ Preuss, *supra* note 30.

³² Constitution of the French Republic art. 28 transl., 2 Peaslee, *Constitutions of Nations* 8, 12 (1950). See also Erades & Gould, *supra* note 30, at 466-68, for a discussion of the Dutch constitutional principle that a treaty is superior both to internal legislation and to the Dutch Constitution. Furthermore, later national Dutch legislation is inferior to and does not supersede pre-existing treaties. Erades & Gould, *supra* note 30, at 320-21, 412-13.

³³ See Bial, *supra* note 30, for a more extended discussion of the cases and the issues.

1862 Franco-Spanish Consular Convention or to aliens assimilated to the 1862 Franco-Spanish Convention by most-favored nation clauses such as that in the February 23, 1853 Consular Convention between the United States and France. In the first *Coll* case,³⁴ a Spanish citizen's argument that the 1938 Decree Law was not applicable was rejected by a lower court. In a second case involving the same person,³⁵ it was held that the treaty did not free him from the requirement of obtaining an identity card but the card had to be delivered to him upon his request. In a third case, the Cour de Lyon held that the Spanish citizen did not have to obtain the special identity card.³⁶

As Bial has explained,³⁷ French commentators criticized the two *Coll* decisions and generally approved the *Sanchez* case which was followed by other French courts, not only for Spanish citizens but also for a Swiss citizen through assimilation to the Franco-Spanish Treaty under a most-favored nation clause in a French-Swiss Treaty.³⁸ Thereafter, France's Supreme Court, the Cour de Cassation, adopted a different and curious attitude: Courts should not interpret treaties. Instead, they should stay the proceedings and request the Ministry of Foreign Affairs to advise them "whether the 1862 Convention authorized Spanish citizens to engage in commerce in France without being in possession of a 'carte de commercant,' and whether France would enjoy reciprocal rights in Spain."³⁹

The Minister of Foreign Affairs, responding to the lower court's request for interpretative guidance, stated that Spanish citizens could rely on the Franco-Spanish Convention of 1862 and could claim French national treatment. He also stated, however, that Spanish citizens could not escape the measures of control which France, for reasons of public order, might deem necessary to take with respect to aliens. He then observed that the same principles were generally accepted in Spain where similar controls were in effect. The French courts later came to the conclusion that, since the June 18, 1953 letter of the Minister of Foreign Affairs was not altogether clear and did not expressly state whether Spanish citizens must comply with the 1938 Decree Law, the conflict must be resolved in favor of the treaty which is the higher law.

The conclusion, in France at least, now is that, in the case of public

³⁴ *Coll*, Cour de Paris (13th ch. Corr.), January 29, 1951, [1952] *Juris-classeur periodique* II. 7056. Hereafter the *Juris-classeur periodique* will be referred to as "JCP."

³⁵ *Coll*, Cour de Lyon (16th ch. Corr.), January 24, 1952, [1952] JCP II 7056.

³⁶ *Sanchez*, Cour de Paris (4th ch. Corr.), February 6, 1952, [1952] JCP II 6996.

³⁷ Bial, *supra* note 30.

³⁸ *Sastella*, Cour de Paris (13th ch. Corr., 2d Sec.), April 1, 1954, [1954] *Gaz. Pal.*, May 15-18.

³⁹ Bial, *supra* note 30, at 350-51.

laws, the courts must request ministerial interpretations of treaties unless a treaty is unambiguous and needs no interpretation or unless the government has already published an interpretation.⁴⁰ In the case of private law, of course, the courts will interpret the treaty without requesting an executive branch interpretation.⁴¹

The French emphasis on reciprocity of treatment clearly jeopardizes the United States position vis-à-vis French and other continental administrators who are charged with the primary interpretation of treaties. While foreign courts may understand and sympathize with judicial reversal of previous decisions, foreign administrators cannot be criticized if they take advantage of the new policy attitude expressed by the Congress and the Internal Revenue Service and seek ways to avoid treaty provisions which they may look upon as unwise or expendable.⁴² In this event United States nationals residing and business enterprises operating in treaty countries should be concerned not only with their status under tax treaties but also under treaties of friendship, commerce, and navigation.

The so-called FCN treaties in many ways are more important to the American businesses which operate abroad than tax treaties because FCN treaties have recently been expanded from the traditional recognition and protection of trading rights to bilateral assurances of reciprocal protection and treatment of private investment including reciprocal equality of tax treatment.⁴³

⁴⁰ One might argue that our courts are impressed by administrative interpretations and practices. See *Cook v. United States*, 288 U.S. 102 (1933), where the court said:

The committee reports and the debates upon the [Tariff] Act of 1930, like the re-enacted section itself, make no reference to the Treaty of 1924. Any doubt as to the construction of the section should be deemed resolved by the consistent departmental practice existing before its re-enactment. [Citations omitted.] No change, in this respect, was made either by the Department of the Treasury or the Department of Justice after the Tariff Act of 1930.

Id. at 120.

⁴¹ Bial, *supra* note 30, at 353-55.

⁴² See, for example, the reported European reaction to the President's unilateral decision to raise tariffs on carpets and glass. *New York Times*, March 23, 1962, pp. 1, 10 and June 5, 1962, pp. 1, 12. See also note 15, *supra*.

⁴³ See Walker, "Treaties for the Encouragement and Protection of Foreign Investment: Present United States Practice," 5 *Am. J. Comp. L.* 229 (1956). While European countries began to think about and to arrange treaties to protect and promote international investment and their nationals who resided in other countries to promote and manage the foreign investment, the United States lagged behind. However, after World War I, the United States began to seek equal treatment for its citizens who resided in foreign countries and agreed to afford comparable equality to citizens of the other countries who resided in the United States. (E.g., *Treaties of Friendship, Commerce and Consular Rights*: with Germany (1923) IV TCIA 4191; with Latvia (1928) IV TCIA 4400; with Norway (1928) IV TCIA 4527). After World War II, as United States private foreign investments multiplied, increasing emphasis was placed on expanding the traditional commercial treaty to include bilateral assurances to protect and promote private investment and to assure reciprocal equality of tax treatment. (For example, *Treaties of Friendship, Commerce and Navigation*: with Germany, T.I.A.S. No. 3062, June 3, 1953 [1956] 5 U.S.T. & O.I.A. 1939; with the Netherlands, T.I.A.S. 3942, March 27, 1956, [1957] 8 U.S.T. & O.I.A. 2043. It is interesting

FCN treaties offer comfort and a form of assurance to an American business which has invested time, technology, and money outside the United States. They assure the American enterprise the same treatment as would be accorded to a national enterprise of the country of investment. Furthermore, since most American companies desire to initiate foreign operations with their own personnel in managerial and technical positions, equal treatment is extremely important not only for the business itself but also for the individuals sent to the foreign country. Equal treatment, or assimilation to national status, therefore, is a necessity for American business which operates outside the United States. Achieving this equal treatment has been a principal goal of the FCN treaty.

The "old type" FCN treaty included equal treatment provisions to assure reciprocal protection not only of trading rights but also the personal rights of individual citizens of one country who reside in the other country.⁴⁴ Consequently, the expansion of the FCN treaty to include encouragement and protection of investment brought into force in a new field traditional concepts and clauses of reciprocal protection. Furthermore, equal treatment clauses appear in all but five of the twenty-one tax treaties⁴⁵ and, generally, extend to "taxes of every kind or description, whether national, federal, state, provincial or municipal."⁴⁶

Since most of our tax treaties include national or equal treatment provisions and since the courts liberally construe commercial treaty obligations and privileges, a brief examination of the history of the equal treatment clause may be helpful in understanding the similar clause which is included in tax treaties.

The first American commercial treaty, the 1778 Treaty of Amity and Commerce with France,⁴⁷ states that citizens of France or of the United States residing or doing business in the other state will be subjected to "no other or greater" tax and customs burdens in the other state than that to which the state of residence subjects citizens of the "most-favoured" nation.⁴⁸ Similar clauses, but no longer restricted to the most

to note that tax treaties of Italy, Japan, New Zealand and Norway with other countries include equal protection provisions, e.g., 1956, New Zealand-Sweden Income Tax Convention, art. XVII, 7 U.N. Int'l Tax Agreements 204 .

⁴⁴ For example, see text supra at note 33, for a brief review of recent French cases concerned with the effect of an 1862 "equal treatment" treaty provision on a modern "alien control" provision.

⁴⁵ Equal treatment clauses are not included in American tax treaties with Australia, Italy, Japan (but see note 72, *infra*), New Zealand and Norway.

⁴⁶ See Paragraph XXI, Technical Memorandum of the Treasury Department on the United Kingdom Income Tax Convention, included in Sen. Ex. Rep. No. 6, 79th Cong., 1st Sess. (1945).

⁴⁷ February 6, 1778, I TCIA 468.

⁴⁸ 1778 Treaty, arts. III, IV, at I TCIA 469, 470.

avored nation, appeared in the 1794 Treaty of Amity, Commerce and Navigation with Great Britain,⁴⁹ where it was stated that Americans will pay "no higher or other duties than would be payable by His Majesty's subjects"⁵⁰ and "no higher or other tolls or rates of ferriage than what are or shall be payable by natives."⁵¹

Although American use of the equal treatment clause antedates the Constitution, the history of the clause begins before its use in United States treaties. In the 1642 Treaty between Portugal and Great Britain⁵² it is stated that the subjects of Great Britain "shall, as freely and in the same manner, exercise their trades of merchandizes [in Portugal] as is permitted to the subjects of other Princes and States in league with the King of Portugal, *neither shall they be more burthened with customs, impositions or other taxes than the inhabitants and subjects of the said lands . . .*" (Emphasis added.)⁵³ Twelve years later in a new treaty,⁵⁴ the English, now negotiating on behalf of the "Republic of England," obtained recognition from Portugal far beyond the most favored nation clause included in the earlier Royal Treaty:

"[T]he said people of this Republic shall enjoy the same liberties, privileges and exemptions as the Portugese themselves. . . ."⁵⁵ In Article X of the 1654 Treaty, the English were given the right freely to transport "into any other ports or places whatsoever of His said Majesty, without paying any other or further custom, duty or sum of money besides what the Portugese merchants should pay, if the goods and merchandize belonged to them."⁵⁶

Similar provisions were included in Britain's 1660-61 Treaty of Peace and Commerce with Denmark⁵⁷ and her 1667 Treaty of Peace and Friendship with Spain.⁵⁸ Generally, they have been included in all early British commercial treaties including the 1815 Convention of Commerce with the United States.⁵⁹

⁴⁹ I TCIA 590.

⁵⁰ Art. III, I TCIA at 592.

⁵¹ *Ibid.*

⁵² II Hertslet, *Treaties and Conventions* 1 (1840).

⁵³ *Id.* at 2.

⁵⁴ 1654 Treaty between England and Portugal, Hertslet, *supra* note 52, at 8.

⁵⁵ *Id.* at 10.

⁵⁶ *Id.* at 13. The "secret Article" annexed to the 1654 Treaty provided for arbitration of customs and duties by two English merchants residing in Portugal selected by the English Consul. *Id.* at 19, 20.

⁵⁷ I Hertslet, *supra* note 52, at 179. The Danish treaty is an especially interesting precedent not only because it includes the "more burdensome than" type language but also because the Treaty provides for "administrative equality": "[T]he people . . . shall pay neither more nor greater customs, tributes, tolls and other duties nor in other manner than" Art. XIII, *id.* at 181.

⁵⁸ II Hertslet, *supra* note 52, at 140. As in the case of the 1654 Treaty with Portugal, *supra*, notes 54 and 55 the English negotiators obtained full assimilation of Englishmen to the "tax" rights and privileges of Spanish citizens. Art. V, *id.* at 142.

⁵⁹ *Id.* at 386.

Early treaties between continental European countries also recognized the advantages of reciprocal treatment. For example, the 1648 Treaty of Peace between Spain and the United Provinces of the Low Countries⁶⁰ provided that "the subjects and inhabitants . . . trading to one another's countries, shall not be obliged to pay greater duties and imposts than the respective subjects, natives of the countries" nor more than that which "lay upon them over and above what He does upon His own subjects."⁶¹

The early United States treaties with France and Great Britain apparently interested America's trading circles because, thereafter, the American State Department actively sought to enter into treaties, which assumed a very nautical cast, with other trading nations. For example, the 1827 Treaty with Norway stated that "Norwegian vessels . . . arriving . . . into the ports of the United States of America, from whatever place they may come, shall be treated . . . upon the same footing as national vessels coming from the same place" and vice versa.⁶²

By 1911 the expansion of United States commercial interests had led to a needed treatment beyond shipping and vessels in commercial treaties so that the language of the Japanese treaty was more expertly phrased to accomplish mutual goals of more general reciprocal treatment: "They shall not be compelled, under any pretext whatever, to pay any charges or taxes other or higher than those that are or may be paid by native citizens or subjects."⁶³ In 1923 the language of the German treaty was further refined so that internal revenue taxes were specifically included in the reciprocal provisions: "The nationals . . . of each High Contracting Party within the territories of the other shall receive the same treatment as nationals . . . of the country with regard to internal taxes. . . ."⁶⁴ And in 1928, although the treaty language had become broader, references to income tax had become more specific: "The nationals of either . . . within the territories of the other shall not be subjected to the payment of any internal charges or taxes other or higher than those that are exacted of and paid by its nationals."⁶⁵

Although the principal concern of the United States primarily had been with trade and commerce, it is interesting to compare the sweeping

⁶⁰ *Id.* at 157.

⁶¹ Art. VIII, *id.* at 158-59.

⁶² Art. II, 2 TCIA 1749.

⁶³ Treaty of Commerce and Navigation with Japan, art. I, III TCIA 2712, 2713.

⁶⁴ Treaty of Friendship, Commerce and Consular Rights with Germany art. VIII, IV TCIA 4191, 4194.

⁶⁵ Treaty of Friendship, Commerce and Consular Rights with Latvia, art. I, IV TCIA 4400-01. It is interesting to note that the Latvian Treaty has vitality until the United States announces that it will no longer adhere to the Treaty. *Zalcmanis v. United States*, 173 F. Supp. 355 (Ct. Cl. 1959), cert. den., 362 U.S. 917 (1960).

equal treatment provisions included in the 1845 Treaty of Commerce and Navigation with Belgium⁶⁶ with those of a modern investment treaty. The 1845 Treaty provided that "The said inhabitants, whether established or temporarily residing within any ports, cities or places . . . shall not . . . pay any other or higher duties, taxes, or imposts, than those which shall be levied on citizens or subjects of the country in which they may be. . . ."⁶⁷ The recent Treaty of Friendship, Commerce and Navigation with Japan⁶⁸ provides in general terms that the enterprises controlled by nationals of one country shall "be accorded treatment no less favorable than that accorded like enterprises controlled by nationals" of the other country.⁶⁹ The treaty then provides in Article XI (1):

Nationals of either Party residing within the territories of the other Party . . . shall not be subject to the payment of taxes, fees or charges imposed upon or applied to income, capital, transactions, activities . . . or to requirements with respect to the levy and collection thereof . . . more burdensome than those borne by nationals and companies of such other Party.⁷⁰

Although the tax treaty with Japan is subsequent to the FCN Treaty and although the tax treaty does not contain a more "burdensome" clause,⁷¹ it seems clear, under our usual rules of treaty interpretation, that the provisions of Article XI (1) of the FCN Treaty continue in full force and effect.⁷² There was, therefore, no need to include an equal treatment section in the tax treaty with Japan.

The first interpretations of the equal treatment clauses involved conflicts between treaties and state laws. In such cases the superiority of treaty provisions over inconsistent state laws is well settled. For example, in *Trott v. State*,⁷³ United Kingdom legatees of a North Dakota decedent contested the application of a law which imposed a special twenty-five per cent tax on transfers of property to aliens who did not reside in the United States. The plaintiffs contended that the special tax could not be imposed because it was in conflict with a treaty between the United States and the United Kingdom which permitted the transfer of real and personal property to citizens of the United King-

⁶⁶ I TCIA 64.

⁶⁷ Art. I, I TCIA at 65.

⁶⁸ April 2, 1953 [1953] 4 U.S.T. & O.L.A. 2063.

⁶⁹ Art. VII(1), *id.* at 2069.

⁷⁰ *Id.* at 2071-72. Curiously enough art. XI(3) adds to the treaty a most favored national equal treatment provisions.

⁷¹ See note 45 *supra*.

⁷² *Cook v. United States*, 288 U.S. 102 (1933). On the other hand, since art. XVI of the tax treaty with Japan is inconsistent with art. XXI(5) of the FCN treaty, the tax treaty, being the later act, presumably has superseded art. XXI(5) of the FCN treaty.

⁷³ 41 N.D. 614, 171 N.W. 827 (1919).

dom on the same basis and terms as citizens of the United States.⁷⁴ The court held that the language of the treaty governed and, therefore, that the special tax could not be applied on the transfer of property to British subjects.⁷⁵

It would seem, therefore, in view of the long history of liberal construction of equal treatment clauses, that there should be no question as to the right of citizens of treaty countries to claim the same rights as United States citizens who are residents of the United States. Unfortunately, the United States record of interpretation of the so-called "no more burdensome than" clauses in tax treaties conflicts with the judicial interpretations of the more general commercial treaties. The administrative record is particularly spotty.

In I.T. 3749⁷⁶ the Internal Revenue Service considered the case of a French citizen who was a resident of the United States and who received income from sources in France and other countries. The Internal Revenue Service, citing only articles 14(B)(a) and 14(B)(b) of the French treaty, held that income tax paid to France through withholding could be credited against United States income tax but that the income tax paid to other countries could not be credited against United States tax because there was no specific comparable provision in the French law giving United States citizens residing in France a credit for taxes the United States citizen pays to countries other than the United States.

In reaching this conclusion the Service ignored article V of the Protocol to the French Treaty which states that a citizen of France within the United States shall not be subjected to the payment of higher taxes than are imposed upon citizens of the United States. The reference to article 14(B)(a) in no way changes the result which must be derived from even the most superficial reading of article V of the Protocol. Indeed, as indicated before,⁷⁷ under French law, it is clear that "equal treatment" provisions of treaties assimilate aliens residing in France to French nationals in the fields of civil, commercial, and tax law even though there is no unanimity with respect to the effect of equal treatment provisions on French penal laws in the case of violation of registrations and similar requirements.

After the enactment of the 1954 Code the Service was asked to consider the case⁷⁸ of a Canadian citizen, a bona fide resident of the United

⁷⁴ Convention with Great Britain as to Tenure and Disposition of Real Property March 2, 1899, art. II, I TCIA 774-75.

⁷⁵ Nielsen v. Johnson, 279 U.S. 47 (1929); McKeown v. Brown, 167 Iowa 489, 149 N.W. 593 (1914).

⁷⁶ 1945 Cum. Bull. 202.

⁷⁷ See text supra at note 33.

⁷⁸ This is an unpublished private ruling which was widely discussed.

States, who obtained a temporary foreign service position with an American oil company. Because he was assigned to a difficult area and because he was to be abroad for a relatively short time, he decided not to take his family with him. The Canadian was actually present in the "oil country" for seventeen out of eighteen months. Nevertheless, the Internal Revenue Service held that the \$20,000 exclusion provided for in section 911(a)(2) was not available to a Canadian because the earned income exclusion was specifically limited to individual citizens of the United States who were present in a foreign country or countries for the prescribed period. This result was reached in spite of the equal treatment provision of paragraph 11 of the Protocol to the Canadian Treaty which states that a citizen of Canada residing in the United States shall not be subjected to the payment of more burdensome taxes than a citizen of the United States. The Internal Revenue Service justified its position on the ground that article XVII of the Canadian Treaty specifically states that "the United States in determining the income . . . taxes . . . of its citizens or residents . . . *may include in the basis upon which such taxes are imposed all items of income . . . taxable under the Revenue laws of the United States . . . as though this convention had not come into effect.*" (Emphasis added.)⁷⁹

At the time the Canadian Treaty was amended in 1950, the Secretary of State in a letter to the President,⁸⁰ referred to subparagraph M of the 1950 amendment and stated that the United States reserved the right "to tax its citizens or residents or corporations as though the convention had not come into effect."⁸¹ The report of the Senate Foreign Relations Committee does not comment on the provision. The Treasury Regulations interpreting the Canadian Treaty⁸² provide that "the convention does not . . . affect the liability to United States income tax of Canadian citizens resident in the United States. . . ." On the other hand, article XVII of the Treaty is correctly paraphrased in Regulations section 519.116: "[T]he United States in ascertaining the income . . . tax of its citizens and residents and corporations may take into the basis upon which such taxes are imposed all items of income as though the convention had not come into effect."

The Government's position in the Canadian case can be justified on

⁷⁹ Art. 14A of the French treaty and art. XVII of the Canadian treaty are identical.

⁸⁰ See note 21 *supra*.

⁸¹ "Because the subject matter of tax treaties is less general and the methods of negotiation are less formal than in the case of many other treaties, tax treaties are usually referred to in diplomatic language as tax 'conventions.'" Blough, "Treaties to Eliminate International Double Taxation and Fiscal Evasion," N.Y.U. 5th Inst. on Fed. Tax 208, 209 (1947).

⁸² Treas. Reg. § 519.102(c) T.D. 5206, 1943 Cum. Bull. 526 at 534.

purely technical grounds because the ruling is limited solely to determining that an item of income is to be included in the taxable base, a right which the United States reserved in article XVII of the Canadian Treaty. However technically correct this interpretation may be, it violates the interpretative principle that, where the treaty admits of two constructions, one liberal and the other restrictive, the liberal interpretation is to be preferred.⁸³

The restrictive interpretation, moreover, cannot be justified on the ground that the seventeen out of eighteen months' rule became a part of the tax law after the effective date of the tax treaty unless a court could find a specific intention that Congress intended to abrogate the apparently broad and unqualified equality provisions of article V of the Protocol to the Canadian Treaty.⁸⁴

These excuses, tenuous as they were in the case of the Canadian Treaty, were not available to justify the conclusions reached in I.T. 3749 which interpreted the French Treaty.⁸⁵ Section 131(a)(3) of the Internal Revenue Code of 1939, in effect long before the effective date of the tax treaty with France, contained the limitation on the availability of the tax credit in the case of alien residents of the United States. Similar provisions appeared in all revenue acts since the Revenue Act of 1921. Furthermore, since the application or nonapplication of credit did not involve the inclusion or exclusion of an item of taxable income in the base on which tax was imposed, it seems clear that I.T. 3749 is erroneous and cannot be supported under any interpretation of the treaty. On the other hand, if one ignores the principles of treaty interpretation which the Supreme Court has announced, the interpretation contained in the Canadian private ruling can technically be justified.⁸⁶

In another case akin to I.T. 3749, a Swiss citizen who became a resident of the United States in September, 1957, married another Swiss citizen, who had been a resident of the United States for the entire taxable year. In an unpublished private ruling the Service held that the Swiss couple could not file a joint tax return because section 6013(a)(1) requires that alien residents of the United States may not file joint returns with their spouses unless the alien has been a resident of the United States for the full taxable year.

⁸³ See text *supra* at notes 16 and 17.

⁸⁴ Cf. *Cook v. United States*, 288 U.S. 102 (1933).

⁸⁵ See note 76 *supra*.

⁸⁶ The author has been informally advised that, while the taxpayer referred to in I.T. 3749 was never able to persuade the Internal Revenue Service to allow him credit for the income taxes he had paid to governments other than France, the Canadian citizen ignored the unfavorable ruling and was able to convince the field auditor that he was entitled to the exclusion from income.

The equal treatment provision of the Swiss tax treaty⁸⁷ states, in effect, that citizens of Switzerland shall not, while resident in the United States, be subjected in the United States to other or more burdensome taxes than are citizens of the United States residing in the United States. It was argued that a United States citizen who became a resident of the United States for the first time in September, 1957, would be permitted to file a joint return with his spouse; consequently, the Swiss citizen should likewise be permitted to reduce his income tax by filing a joint return with his spouse, otherwise the Swiss would be subjected to other or more burdensome taxes than the American citizen. In its ruling the Service referred to article XV(1)(a) of the Swiss Treaty as permission for the United States to tax "residents" as if the convention had not come into effect. The Service ignored article XV(1)(a) which limits the United States' right, with respect to its citizens and residents, to include items of income in the taxable base as if the convention had not come into effect.⁸⁸

In 1959 the Service restated treaty interpretation principles in a ruling involving a United States citizen taxpayer who desired to exclude from his taxable income, income he had received from German real estate. Rev. Rul. 59-56⁸⁹ states that:

The meaning of Article XV(1)(a) of the German Convention . . . is that the United States income tax liability of United States citizens, residents, or corporations is determined "as if this Convention had not come into effect." The purpose of this "saving clause" is to make it plain that the United States reserves the right, in the case of its citizens, residents, or corporations, to include in its tax base all items of income taxable under its revenue laws. . . .

This statement is a rather curious interpretative hodgepodge. The direct quotation from the treaty, contained in the first sentence quoted above, is completely out of context and provides the reader with an inaccurate understanding of the treaty.

The courts have also had opportunities to consider the problems of interpretation of tax treaties. The appellate courts, generally, have sustained the liberal interpretation principle, sometimes erroneously. For example, *American Trust Co. v. Smyth*⁹⁰ dealt with an American

⁸⁷ Swiss Treaty art. XVIII(3), May 24, 1951 [1951] 2 U.S.T. & O.I.A. 1751.

⁸⁸ It is interesting to note that the Swiss negotiators were informed of the unfortunate provisions of I.T. 3749 because the final sentence of art. XV(1)(a) states that "Switzerland satisfies the similar credit requirement found in section 131(3), Internal Revenue Code." The author has been informed that, as in the case of the Canadian citizen, the Swiss citizens involved in the unfavorable ruling issued in the spring of 1958, were allowed to file a joint return in spite of the Service's issuance of the unfavorable ruling.

⁸⁹ 1959-1 Cum. Bull. 737 at 738.

⁹⁰ 247 F.2d 149 (9th Cir. 1957).

trust which had United Kingdom income beneficiaries. The trust had sold corpus and had realized a substantial capital gain which was neither distributed nor distributable to the beneficiaries. The government argued, successfully in the lower court, that, since the capital gain was not income for the United Kingdom beneficiaries or remaindermen, but instead was income of the United States trustee, the capital gain was taxable. The taxpayer-trustee argued that the treaty exempted capital gains from tax not only to the extent distributable to the beneficiaries but also to the extent retained by the trustees.

The court, stating that the purpose of the United Kingdom tax treaty was to provide full reciprocity and equality of tax treatment, agreed with the taxpayer's argument. The court then quoted at length from various cases in which the Supreme Court announced the principle of liberal construction of tax treaties. After considering that the treaty announced a broad general purpose of avoiding the economic impact of the tax on the trustee (*i.e.*, if the trustee were required to pay the tax, the corpus of the trust would be reduced and the future income of the beneficiaries, therefore, would be reduced), the court held that the trustee would not be required to pay the capital gains tax. The court also indicated that, since the United Kingdom Treaty does not contain a "savings clause" as do the Swedish, Canadian, and French treaties, the government could not rely on its retained right to include items of income in the taxable base of United States citizens or resident taxpayers.

The Second Circuit recently considered the question raised by the *American Trust Co.* case⁹¹ and correctly came to the opposite conclusion.⁹² After carefully reviewing the British treaty and its background, the court stated that it could find nothing to require the United States to abandon the concept that a trust was a taxable entity separate from the beneficiaries of the trust. Consequently, since the trust was a separate taxable entity under American law, American tax principles would be applied to the trust without resort to the United Kingdom treaty.

In reaching its conclusion in the *Maximov* case⁹³ the court, carefully reviewing the principles of treaty interpretation, stated that the following criteria must necessarily be considered in the interpretation and construction of tax treaties:

The broad aim of the Convention, as with income tax treaties generally, was to facilitate commercial enterprise between the two countries [and]

⁹¹ *Ibid.*

⁹² *Maximov v. United States*, 299 F.2d 565 (2d Cir. 1962).

⁹³ The court's conclusion seems to be inescapably correct.

to avoid double taxation . . . which, because of the high rates of income taxation then and now prevailing in the two nations, constituted what the Secretary of State called "an undesirable impediment to international trade." A primary motivation for inclusion of provisions equalizing tax treatment . . . was reduction of tax barriers to the free movement of individuals for commercial purposes.⁹⁴

To the court's very useful addition to the principles of treaty construction one other must be added: A primary motivation of 320 years of history of the equal treatment clause in treaties has been the encouragement of free movement of individuals for commercial purposes by assuring nationals of country A that they will be subject to no other or more burdensome tax treatment than their native neighbors and associates in country B when and if the nationals of country A reside in country B.

In sixteen tax treaties equal treatment provisions are clear:

- no "other or more burdensome,"⁹⁵
- no "higher taxes,"⁹⁶
- no "more burdensome taxes,"⁹⁷
- no "other, higher or more burdensome,"⁹⁸
- no "other or higher."⁹⁹

In spite of the difference in language there can be no serious doubt as to the meaning and the intention of these equal treatment provisions which was perhaps expressed best in the 1953 FCN Treaty with Japan.¹⁰⁰

The same intention has frequently been expressed in various State Department letters of transmittal of treaties and in Treasury memoranda. The equal treatment clause:

"Has application only to taxation by one of the contracting States of citizens of the other contracting State residing in the former state. Under our existing law residents of the United States are subject to the same taxation as are United States citizens";¹⁰¹

⁹⁴ 299 F.2d at 570. (Footnotes omitted.)

⁹⁵ Austria, art. XVIII(3), Oct. 25, 1956 [1957] 8 U.S.T. & O.I.A. 1699; Denmark, art. XVI(1), May 6, 1948 [1948] 62 Stat. 1730; Finland, art. XVI, March 3, 1952 [1952] 3 U.S.T. & O.I.A. 4464; Germany, art. XVIII(3), July 22, 1954 [1954] 5 U.S.T. & O.I.A. 2768; Greece, art. XVI(3), Feb. 20, 1950 [1953] 5 U.S.T. & O.I.A. 47; Honduras, art. XV(5), June 25, 1956 [1957] 8 U.S.T. & O.I.A. 219; Ireland, art. XVI, Sept. 13, 1949 [1951] 2 U.S.T. & O.I.A. 2294; The Netherlands, art. XXV(3), June 15, 1955 [1955] 6 U.S.T. & O.I.A. 3696; Switzerland, art. XVIII(3), May 24, 1951 [1951] 2 U.S.T. & O.I.A. 1751; United Kingdom, art. XXI(1), Aug. 19, 1957 [1958] 9 U.S.T. & O.I.A. 1329.

⁹⁶ Belgium, art. XX(3), Oct. 29, 1948 [1953] 4 U.S.T. & O.I.A. 1647; France, Protocol V, June 22, 1956 [1957] 8 U.S.T. & O.I.A. 843.

⁹⁷ Canada, Protocol II, Aug. 8, 1956 [1957] 8 U.S.T. & O.I.A. 1619; Union of South Africa, art. III(1), Dec. 13, 1946 [1952] 3 U.S.T. & O.I.A. 3821.

⁹⁸ Pakistan, art. XVII, July 1, 1957 [1959] 10 U.S.T. & O.I.A. 984.

⁹⁹ Sweden, Protocol 7, March 23, 1939 [1939] 54 Stat. 1759.

¹⁰⁰ 1953 Japanese FCN, note 55 *supra*, art. XI(1).

¹⁰¹ Technical Memorandum of the Treasury Department, In Re Proposed Tax Conven-

Expresses "on a reciprocal basis . . . the long recognized principles relating to equality of treatment in respect of the taxation of resident aliens as compared with the taxation of resident nationals";¹⁰²

Assures "equality of tax treatment . . . as between the nationals of the country imposing tax and nationals of the country who reside within its borders. *The article does not change domestic law*"; (Emphasis added.)¹⁰³ and

"Has no practical effect, since our domestic taxation does not discriminate as between United States citizens and British nationals residing in the United States."¹⁰⁴

Even though the premises stated by the Department of State and the Treasury Department were erroneous, the intention of the negotiators and of their respective departments was made clear to the President and the Senate. There can be, therefore, no justification for the contrary interpretations promulgated by the Internal Revenue Service in the Canadian, French and Swiss cases discussed above. The equal treatment provision is unambiguous in its requirements. To permit the so-called "savings clause" to override the equal treatment provision serves only to abrogate the equal treatment clause, a step the courts have indicated they will not permit even though the Tax Court perhaps inadvertently took a step in that direction in *Matthew Klaas*.¹⁰⁵

The President and the Secretary of the Treasury do not deserve the condemnation they are receiving from many sources because of their pursuit of evasive tax dollars which statistics indicate may be hidden in foreign corporations and bank accounts. On the other hand, the

tion between the United States and Sweden. The second quoted sentence of course is and at the time was wrong because foreign corporations engaged in business in the United States were subject to different normal tax under § 14(c) of the Int. Rev. Code of 1939 in effect on the date of signature of the Swedish treaty. See also the tax credit limitation for alien residents, § 131(a)(d) of the 1939 Code, discussed in text following note 85.

¹⁰² April 14, 1950, Letter from the Secretary of State to the President transmitting the Greek treaty; cf. May 18, 1948, Letter of Secretary of State to the President transmitting The Netherlands Treaty.

¹⁰³ May 18, 1956, Treasury Memorandum on the Honduras Treaty. By 1956 the Treasury statement (in the second sentence) was even more erroneous than in 1939. Section 14(c) of the 1939 Code had been repealed, but the tax credit limitation remained as 1954 Code, § 901(b)(3). By 1956 the following other citizen-alien differences had become part of the laws: § 1(b)(4)(A) (head of household rate table); § 911(a)(2) (the exclusion of income under the 17 out of 18 months rule); § 931 (income from possessions of the United States); §§ 6013(a)(1), 6015(b) (requirements for filing joint returns) 6015(a)(1)(A)(ii), 6015(a)(1)(B)(i) (declarations of estimated tax).

¹⁰⁴ July 3, 1945 Treasury Department Technical Memorandum on the Income Tax Convention with the United Kingdom, Sen. Ex. Rep. No. 6, 79th Cong., 1st Sess. — (1945).

¹⁰⁵ 36 T.C. 239 (1961). The equal treatment clause apparently was not raised by taxpayer's counsel and was not considered by the Court. Cf. *Joyce de la Begassière*, 31 T.C. 1031 (1959), *aff'd per curiam*, 272 F.2d 709 (5th Cir. 1959) where a similar argument might have been made and should have been successful. Cf. *Grant v. United States*, 202 F. Supp. 608 (W.D. Va. 1962) where the taxpayer was successful even though the equal treatment clause was not raised.

Congress should resist becoming a participant in the unilateral termination of important treaty provisions. Quite clearly, section 21 of H.R. 10650 deserves an early death and our treaty negotiators should be given the time and the opportunity to meet with their counterparts in treaty countries to negotiate a revision of those portions of treaties which may be affected by H.R. 10650.¹⁰⁶ The administration's failure to protest the inclusion of section 21 in the bill will not soon be forgotten by government officials in foreign countries. Clearly, every effort should be made to avoid giving continental European administrators additional evidence of lack of reciprocity in the United States interpretation of tax treaties. A useful opening gambit would be for the Internal Revenue Service and the courts, particularly the Tax Court, to take the first opportunity to assure everyone that the "equal treatment" clause will be respected and liberally construed in the tradition of the Supreme Court's long-accepted pronouncements. If the Service and the Treasury should fail to take advantage of the first opportunity for clarification of the American administrative position, continental European administrators will almost certainly act in a way which will be unfavorable to American citizens who reside or businesses which operate abroad.

¹⁰⁶ See notes 4 and 21, *supra*.