SOME AMERICAN DISCRIMINATIONS AGAINST FOREIGN ENTERPRISES

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A. INTRODUCTION

In an article published in the financial section of the *New York Times* in January of this year¹ attention was called to the desire of business interested in foreign trade for modernization of over 30 treaties or trade agreements existing between the United States and foreign nations. One of the problems declared to be of great concern is the prevention of discrimination against American trade. And there will be no dearth of evidence for presenting a strong case for protection against a multitude of barriers, other than tariffs, restricting American business abroad. The fight against discrimination, however, is a two-way affair. In the United States, as elsewhere, there exists a body of law discriminating against aliens, some directed against professional activities,² some against the right to work,³ some against certain types of business,⁴ some against the ownership of land⁵ and there are others. All these discriminations have seemingly little connection with foreign trade, if such trade is conceived as an interchange of goods or services between nations. But they may easily gain significance when their aggregate effect is considered. Measuring and evaluating such effects in terms of money and relating it to foreign trade in the accepted common meaning of the term is rather the task of an economic analyst than the job of a lawyer and not within the scope of the present paper which intends to discuss some discriminatory provisions of American law, particularly of the law of federal income taxation more clearly connected with international business. No exhaustive survey will be attempted.

Discrimination implies comparison and for our topic comparison of the treatment of citizens or corporations of a foreign nation with the treatment accorded to citizens or domestic corporations. The term "citizen" is ambiguous in any country in which under a federal system an individual has a dual citizenship; and so is the term "domestic" corporation. For the present the distinction between national and state citizenship will be disregarded; furthermore the term "domestic" corporation

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¹ *N. Y. Times*, January 6, 1946, section 3/5, p. 1, col. 1.

² See Cutler, *The Treatment of Foreigners* (1933) 27 *AM. J. INT. L.* 225, 228.

³ See Fellman, *The Alien's Right to Work* (1938) 22 *MINN. L. REV.* 137; Note, *Constitutionality of Legislative Discrimination Against the Alien in His Right to Work* (1934) 83 *U. OF PA. L. REV.* 74.

⁴ 3 HACKWORTH, *DIGEST OF INTERNATIONAL LAW* (1942) 614 *et seq.*

⁵ *Id.* at 671; Miller, *Alien Land Laws* (1939) 8 *GEO. WASH. L. REV.* 1; Powell, *Alien Land Cases in the United States Supreme Court* (1924) 12 *CALIF. L. REV.* 259.

will be used to include corporations (and any other entity treated like a corporation⁶) organized under the laws of the United States, any state or territory.

The problem of discrimination arises any time that foreign business is not accorded in the United States equality with its American competitor. It is complicated by the different scope of the protection accorded under the Federal system to individuals and corporations against discriminatory state action. Particularly when the question of discrimination arises under state law the inquiry might be difficult whether the corporation incorporated under the law of a foreign country can claim discrimination when receiving equal treatment with a corporation incorporated in another state, but not with a domestic corporation incorporated in the same state. Such inquiry requires examination of the increasing recession of the Fourteenth Amendment⁷ as a protection against economic legislation, the expanding doctrine of reasonable classification⁸ and the casuistry under the commerce clause of the Constitution.⁹

B. FEDERAL LAW

Taxation. The heaviest burden on international trade in the field of taxation results from double taxation¹⁰ and extraterritorial taxation.¹¹ Each of these concepts differs in principle from discrimination. They arise from a conflict of jurisdiction to tax or from the exercise of such jurisdiction whereas discriminatory taxation presupposes jurisdiction to tax. Occasionally the same set of facts may raise a problem of double taxation and discrimination.¹²

The treaties intended to minimize double taxation of income are few.¹³ Treaties pretending to grant equal treatment to foreign nationals, specifically including matters of taxation,¹⁴ were already numerous before the more liberal trade policy inaugurated by the Trade Agreements Act of 1934.¹⁵

The latest Income Tax Convention negotiated by the United States, the Tax Convention with Great Britain of April 16, 1945, has in its Art. XXI the most comprehensive and technically best formulated provision against discriminatory tax-

⁶ Cf. INT. REV. CODE §3797(a)(3)(4).

⁷ See *infra* note 85.

⁸ See *Madden v. Kentucky*, 309 U. S. 83, 88 (1940).

⁹ See in general Dowling, *Interstate Commerce and State Power* (1940) 27 VA. L. REV. 1.

¹⁰ See Carroll, *Development of International Tax Law in the Americas* (1941) 8 LAW & CONTEMP. PROB. 793, 795, notes 4 and 5; Henry H. Kimball, 6 T. C. No. 68 (1946); Ke Chin Wang, *International Double Taxation of Income* (1945) 59 HARV. L. REV. 73.

¹¹ See Wurzel, *Foreign Investment and Extraterritorial Taxation* (1938) 38 COL. L. REV. 809.

¹² See the provisions of the Internal Revenue Code granting credit for foreign taxes. Wurzel, *Tax Agreements and Trade Privileges* (1940) 18 TAXES 484, 487.

¹³ See Carroll, *Tax Inducements to Foreign Trade*, this symposium, *supra* p. 760.

¹⁴ Fourteen such treaties guaranteeing equality of treatment in matters of taxation with American nationals are listed by HERNDON, *RELIEF FROM INTERNATIONAL INCOME TAXATION* (1932) 18; five more treaties do not use the word "taxes" though "succession duties" and similar phrases are used. *Ibid.* However, as the author remarks, all those treaties, but one, were concluded at a time when there was no Federal income tax.

¹⁵ 48 STAT. 943 (1934), 19 U. S. C. §1351 (SUPP. 1945); for the reciprocal agreements in force on July 31, 1945, see 19 U. S. C. A. §1351 note (SUPP. 1945).

ation.¹⁶ In the report submitting the Convention to the Senate, the Secretary of State referred to that article in the following terms:¹⁷

"Article XXI gives expression to principles, long recognized in practice in the United States and found in many commercial or general-relations treaties of the United States, relating to equality of taxation in the United States as between United States citizens residing in the United States and aliens resident in the United States. Article XXI effects no change in existing United States revenue laws."

Accepting for the time being this statement at its face value as a broad statement of policy, it seems satisfactory, provided that the term "equality" means what it says without any mental reservations restricting it to "equality as appropriate" or a similar rubber clause which covers any transgression. The optimism displayed by the Secretary is shared by other semi-official publications of the Department of State¹⁸ but the Treasury apparently does not have the same candid understanding of treaty provisions.¹⁹ Since Article XXI in using the term "nationals" includes therein corporations and other "legal persons" it is only fair to assume that the Secretary did not mean to restrict his views on Article XXI to individuals and that he intended to state that resident aliens (individuals or corporations, British or not)²⁰ are treated alike even in absence of any specific provisions in treaties. However, the Internal Revenue Code, although applying the principle in general²¹ to resident alien individuals within the meaning of the Code, falls short of it once foreign corporations or non-resident aliens are involved.

Definitions. Under the terminology of the Code "a domestic corporation is one organized or created in the United States . . . or under the Laws of the United States or of any State or Territory and a foreign corporation is one which is not domestic." It is usually said that consequently the place of incorporation determines whether a corporation is domestic or foreign.²² Such view is in accord with

¹⁶ (1946) C. C. H. FED. TAX REP. ¶6052. Art. XXI provides:

"1. The nationals of one of the Contracting Parties shall not while resident in the territory of the other Contracting Party, be subjected therein to other or more burdensome taxes than are the nationals of such other Contracting Party resident in its Territory.

"2. The term 'nationals' as used in this Article means

a. In relation to the United Kingdom, all British subjects and British protected persons, from the United Kingdom or any territory to which the present Convention is applicable by reason of extension made by the United Kingdom under Article XXII; and

b. In relation to the United States, United States citizens, and all persons under the protection of the United States, from the United States or any territory to which the present Convention is made applicable by reason of extension . . . ;

and includes all legal persons, partnerships and associations deriving their status as such from, or created or organized under, the laws in force in any territory of the Contracting Parties to which the present Convention applies.

"3. In this Article the word 'taxes' means taxes of every kind or description, whether national, Federal, state, provincial or municipal."

¹⁷ 1946 C. C. H. FED. TAX REP. ¶6052.

¹⁸ See 3 HACKWORTH, DIGEST OF INTERNATIONAL LAW (1942) 577.

¹⁹ See 8 MERTENS, LAW OF FEDERAL INCOME TAXATION (1942) 245, note 19.

²⁰ The term resident used in treaties is difficult to define, its meaning uncertain. See *infra* p. 789.

²¹ TREAS. REG. III, §29.211-1.

²² 8 MERTENS, *op. cit. supra* note 19, at 276.

the American position generally taken with respect to the nationality of corporations.²³ But if it is considered that under the lenient laws of some countries a corporation may be organized abroad provided the necessary papers are filed with some official of the incorporating state,²⁴ it might very well be that the Code departs from the formal test and enlarges the concept of domestic corporation. Even if such view be correct, the domestication of foreign corporation has no importance, since no case or ruling has been found in the Reports raising the problem. However, it is submitted that the provisions of the Code are in conflict with the purely legal test using the state of incorporation as criterion, like the Draft Convention with Great Britain.²⁵

Non-resident Aliens and Foreign Corporations. In general—there are exceptions²⁶—a resident alien individual is treated like a citizen. The taxation of non-resident alien and of foreign corporations follows a more involved pattern: they are taxed on income from domestic sources only; if they are engaged in trade or business, on all such income,²⁷ otherwise only on periodical items of income like salaries, dividends.²⁸ When the Revenue Act of 1936 reshaped the scheme of taxation of aliens and foreign corporations, apprehension existed that the flat rate favored non-residents, since citizens were subject to progressive surtax rate. The dissimilarity of this situation and of the position of citizens abroad (generally fully taxed) makes of questionable value any comparison between the taxation of resident and of non-resident aliens and foreign corporations not engaged in trade or business in the United States.

Sections 211(a) and 231(a) of the Internal Revenue Code raise another problem: the rate of 30 percent can be reduced by treaty to not less than 5 percent in favor of residents of Western Hemisphere countries. Under the Treaty with Canada the rate is reduced to 15 percent, or complete exemption granted;²⁹ under the French and Swedish treaties many items of periodical income are likewise exempt or subject to a lower federal tax.³⁰ Since a treaty overrides earlier statutes, the restriction provided for in Sections 211(a) and 231(a) is meaningless unless its function is to serve notice that a reduction in rate cannot be obtained by operation of general clauses, like the most favored nation clause, but by specific provision only.

Resident foreign corporation (that is those engaged in trade or business in the

²³ Hanna, *Nationality and War Claims* (1945) 45 COL. L. REV. 301, 325.

²⁴ E.g., Panama, Lichtenstein. See *Hearings before the Joint Committee on Tax Evasion and Avoidance*, 75th Cong., 1st Sess. (1937) 258.

²⁵ *Supra* note 16.

²⁶ The most important is the denial of the credit for foreign taxes if there is no reciprocity; see Wurzel, *supra* note 12.

²⁷ INT. REV. CODE §§211(b), 212(a), 231(b), (c). See in general 8 MERTENS, *op. cit. supra* note 19, ch. 45.

²⁸ INT. REV. CODE §§211(a)(c), 231(a).

²⁹ Tax Convention with Canada, 57 STAT. 1399 (1942) Art. XI; see Carroll, *The New Tax Convention Between the United States and Canada* (1942) 20 TAXES 459, 461.

³⁰ See Castimore, *Income Tax Treaties*, PROCEEDINGS OF NEW YORK UNIVERSITY, 4TH ANNUAL INSTITUTE ON FEDERAL TAXATION (1946) 537.

United States) are in principle taxed like domestic corporations. The computation of their taxable net income, starts with their gross income from domestic sources, the permissible deductions correspond to those allowed domestic corporations. The foreign income is disregarded except as used for apportioning general expenses. The provisions are basically fair; however, some flaws exist. Domestic corporations having a normal tax net income of less than \$50,000, are taxed at a lower rate than the normal rate of 24 percent. Foreign corporations are denied the reduction.³¹ The discrimination is patent, but insignificant in amount. Foreign insurance companies, however, are taxed at the same rates as domestic insurance companies.³²

Dividends-paid Credit. A very heavy tax,³³ according to one view without possibility of escape, may result from the interplay of several very technical provisions of the Internal Revenue Code. By three devices the Code attempts to force distribution of the income of corporations to the stockholders, thus subjecting them to progressive surtax rates. One device, through the concept of foreign personal holding company, is aimed at citizens and resident aliens and, its misleading name notwithstanding, affects neither a foreign corporation nor non-residents. The two other devices are the surtax on corporations improperly accumulating surplus and the surtax on personal holding companies, each applicable to foreign corporations with a narrow exception.³⁴

Each tax can be avoided by distributing in dividends an amount sufficient for constituting the basic surtax credit. That credit is the most important element in eliminating the income potentially subject to the surtax. To enter into the computation of the basic surtax credit, the distribution must be taxable. According to one view the dividend must be actually taxed to each stockholder, and it is not sufficient if it conforms to the definition of a dividend given by the Code and is as such potentially taxable.³⁵ The test for taxing dividends distributed by a foreign corporation is based on the average earnings over a three-year period,³⁶ the qualification for the surtax is based on the income in the taxable year. The income upon which the surtax is based is the domestic income, and doing business in the United States is not a condition for the application of either tax.³⁷ Aside from the details and the variations that may result from the different nature of the surtax on improper accumulation and of the surtax on personal holding companies, a foreign corporation making the same distributions as a similar domestic corporation may discover that average earnings in the preceding three years were not derived from United States sources to the extent of at least 50 percent, and are not taxed to non-resident stockholders though taxed to residents. If it be true that in such

³¹ INT. REV. CODE §14(c)(1).

³² INT. REV. CODE §§201(a)(2), 204(a)(2).

³³ Rudick, *Personal Holding Companies Owned by Non-resident Aliens* (1946) 1 TAX L. REV. 218.

³⁴ TREAS. REG. III, §§29.102-1, 29.500-1.

³⁵ Rudick, *supra* note 33.

³⁶ INT. REV. CODE §119(a)(2)(B).

³⁷ *Porto Rico Coal Co. v. Comm'r*, 126 F. (2d) 212 (C. C. A. 2d, 1942); *G. C. M.* 18,077, 1937—C. B. 123.

case no basic surtax credit can be obtained by the corporation³⁸ a surtax ranging from 27½ percentum to 85 percentum will be imposed upon the foreign corporation but not on the domestic.³⁹ Since the cases in which a foreign corporation may suddenly discover that it qualifies as personal holding company are more frequent than it would seem at first thought,⁴⁰ the provision carries a real danger, particularly in connection with the sanctions for failure to file returns hereinafter discussed.

Capital Losses. In general capital losses are deductible only to the extent of capital gains. Stock and stock rights are considered capital assets subject to the general rule. A loss realized by a domestic corporation, but not by a foreign corporation, on stock of an affiliated corporation is not considered as a loss on capital assets, but as an ordinary loss and can, consequently, be deducted in full from ordinary income, not only from capital gains.⁴¹ Furthermore it becomes a part of the net operating loss deduction and can be taken as deduction in the year when incurred, and, when not then exhausted in the two preceding and following years without limitation to capital gains.⁴² A similar rule applies to securities becoming worthless.⁴³ That the foreign interests can incorporate in the United States so as to avoid the discrimination, is an answer that may or may not be practicable according to the circumstances, but at this point irrelevant, since we are not concerned with the avoidance of discriminatory provisions.

Credit for Foreign Taxes. The credit for foreign taxes allowed by the Internal Revenue Code benefits citizens, domestic corporations, and, under condition of reciprocity, resident aliens.⁴⁴ Here the problems of double taxation and discriminatory taxation intersect.⁴⁵ Since the double taxation element prevails two observations only will be made here. The question whether general clauses in treaties providing for equal treatment in taxation, eliminate the requirements of reciprocity, is an open one.⁴⁶ A certain mitigation for aliens not covered by the reciprocity and for foreign corporations, altogether excluded, is effected by the permissibility of taking taxes paid to a foreign country as a deduction.⁴⁷

Withholding of Tax. The provisions of the Code providing for withholding of the tax at the source when periodical items of income (interests, dividends, etc.) are

³⁸ Rudick, *supra* note 33.

³⁹ INT. REV. CODE §§102(a), 500. The writer does not share the view presented in the text. See comment by the present writer in (1946) 1 TAX L. REV. 440. But such view has been so forcefully urged as to warrant consideration.

⁴⁰ Silverson, *Corporations in Foreign Trade and Income Taxes*, PROCEEDINGS OF NEW YORK UNIVERSITY, 4TH ANNUAL INSTITUTE ON FEDERAL TAXATION (1946) 647, 670.

⁴¹ INT. REV. CODE §23(g)(4); TREAS. REG. III, §29.23(g)-2; 3 MERTENS, *op. cit. supra* note 19 (Suppl. 1945) §22.15.

⁴² INT. REV. CODE §122.

⁴³ *Id.* §23(k).

⁴⁴ *Id.* §131(a); see 5 MERTENS, *op. cit. supra* note 19, at 545; Carroll, *Developments in International Tax Law* (1938) 16 TAXES 75, 76; Carroll, *Tax Inducements to Foreign Trade*, this symposium, *supra* p. 760.

⁴⁵ Wurzel, *supra* note 12, at 487.

⁴⁶ *Id.* at 488.

⁴⁷ INT. REV. CODE §23(c)(1)(C). Reciprocity is not a condition. 5 MERTENS, *op. cit. supra* note 19, at 547 note 23.

payable to non-resident aliens and corporations cannot be considered as discriminatory, since they do not "in any wise increase the burden of the tax upon non-residents."⁴⁸ That may be taken as the expression of a principle that differences in the method of collection do not constitute a discrimination.

Failure to File Returns. The preparation of income tax returns has been a fertile source of inspiration for cartoonists. They have, of course, passed up the finer points: whether a piece of paper having all the appearances of a return because the official form has been used, is a "return" depends on legal niceties which at times may prove very costly.⁴⁹ When non-resident aliens and resident foreign corporations are under duty to file returns, the failure to do so brings them within the purview of Sections 215(a) and 233 of the Internal Revenue Code. These sections provide that a non-resident alien or a foreign corporation

"shall receive the benefit of the deductions and credits allowed to it in this chapter only by filing or causing to be filed . . . a true and accurate return of [the] total income received from all sources in the United States."

On its face the quoted provision is innocuous and aimed at tax evaders who do not deserve leniency. But it may catch also the well-intentioned and the unwary. It will be remembered that resident foreign corporations are those engaged in trade or business in this country. "Engaged in trade or business" is an elusive concept. The cases dealing with it are literally legion.⁵⁰ Though the Code attempts to narrow the area of doubt, it is still considerable.⁵¹ The Treasury has been active in trying to extend the scope of the statute by claiming that the sanction applies also if a return, otherwise complete, has been filed at a later date than provided by law. At times it has failed to persuade the courts to accept such view.⁵² In other cases which can be distinguished on various, very technical grounds from the preceding group, the Treasury has found the courts more cooperative.⁵³

The disallowance of deductions and credits applies to the normal tax, the surtax, the surtax on corporations improperly accumulating surplus and to the surtax on personal holding companies. Domestic corporations, citizens or resident aliens

⁴⁸ *Travis v. Yale & Towne Mfg. Co.*, 252 U. S. 60, 76 (1920) decided under N. Y. TAX LAW §366 (McKinney 1943); 3 HACKWORTH, *op. cit. supra* note 4, at 578.

⁴⁹ E.g., see *Lucas v. Pilliod Lumber Co.*, 281 U. S. 245 (1930) [lack of verification]; *Burford Oil Co.*, 4 T. C. 613 (1945).

⁵⁰ See 8 MERTENS, *op. cit. supra* note 19, at 271; *Stikeman, Carrying on Business in Canada* (1942) 22 CAN. BAR. REV. 77.

⁵¹ E.g., see *Helvering v. Scottish American Investment Co.*, 323 U. S. 119 (1944); *Linen Thread Co. v. Comm'r*, 128 F. (2d) 166 (C. C. A. 2d, 1942), *cert. denied*, 317 U. S. 673 (1942); *Berliner Handels Gesellschaft v. United States*, 30 F. Supp. 490 (Ct. Cl. 1939), *cert. denied*, 309 U. S. 670 (1940); *Cantrell & Cochrane, Ltd.*, 19 B. T. A. 16 (1930); more cases are collected in 8 MERTENS, *op. cit. supra* note 19, at §45.20.

⁵² *Ardbern Co. v. Comm'r*, 120 F. (2d) 424 (C. C. A. 4th, 1941); *American Direct Tea Trading Co., Ltd.*, 38 B. T. A. 711 (1938).

⁵³ E.g., *Georday Enterprises v. Comm'r*, 126 F. (2d) 384 (C. C. A. 4th, 1942); *Taylor Securities, Inc.*, 40 B. T. A. 697 (1939); see 8 MERTENS, *op. cit. supra* note 19, at 349 *et seq.*

similarly delinquent are not subject to such disallowance.⁵⁴ The sanctions for late filing imposed upon them may be a penalty which cannot exceed 25 percent of the tax,⁵⁵ in some cases the forfeiture of the right to make an advantageous election,⁵⁶ interest,⁵⁷ all sanctions also applicable to a foreign corporation or non-resident alien equally remiss in their duties. The leniency accorded domestic taxpayer is particularly apparent in the case of corporations. If foreign they are denied the benefit of the 85 percent credit on the income received in form of dividends,⁵⁸ which domestic corporation may nevertheless claim.⁵⁹

Income tax statutes of several states subject non-resident (here non-resident citizens are included) to penalty similar to the one above discussed: the failure to file a return results in the disallowance of deductions.⁶⁰

Regulated Investment Companies. Somewhat on the fringe of our topic are the provisions of the Code dealing with Regulated Investment Companies.⁶¹ The so-called double taxation of corporate income, first to the corporation, then to the shareholders when distributed in the form of dividends, is avoided by making the companies a mere conduit: their income is taxed to the corporation if not distributed, to the shareholders if distributed. This advantage is available to domestic corporations registered under the Investment Company Act of 1940, or to certain common trust funds. Foreign corporations are excluded though they may be registered under the Act.⁶²

Miscellaneous. Other instances, commonly known, of discriminatory legislation by Congress are the prohibition of alien individuals or foreign corporations to operate radio stations, against the awarding of government contract for aircraft, and against the sale of helium gas.⁶³ The foreign fund control legislation temporary in its nature and mainly a war-time measure may have its problems, but they do not belong to the class of exchange-control practiced by other countries which were a deliberate attempt to erect permanent trade barriers.

Discrimination in the treatment of creditors are discussed elsewhere in this issue.⁶⁴ The discrimination that may result from unequal treatment of aliens in imposing estate taxes have great importance for individuals desiring to do business

⁵⁴ Domestic corporations and citizens taxed like non-resident aliens are subject to a similar disallowance for failure to file a return. INT. REV. CODE §251(g); 8 MERTENS, *op. cit. supra* note 19, at 368, 379. But such corporations and citizens are not competing on the domestic market, and, therefore, not a proper gauge for our purposes.

⁵⁵ INT. REV. CODE §291.

⁵⁶ *Burford Oil Co.*, 4 T. C. 613 (1945) and cases there cited; *Second Carey Trust*, 2 T. C. 629 (1943); *Lee H. Marshall Heir's*, 45 B. T. A. 632 (1941); *Joe Goldberg*, 14 B. T. A. 465 (1928).

⁵⁷ INT. REV. CODE §§292, 294.

⁵⁸ *Id.* §26(b).

⁵⁹ If a return has been prepared in behalf of a domestic taxpayer by the commissioner, deductions and credits may be claimed by claim for refund. See 8 MERTENS, *op. cit. supra* note 19, at 607.

⁶⁰ E.g., ALA. CODE, tit. 51 §§398, 406 (Michie 1941); ARK. STAT. §14038 (Pope's Digest 1937); N. Y. TAX LAW §367 (McKinney 1943).

⁶¹ INT. REV. CODE §§361, 362.

⁶² 54 STAT. 803 (1940), 15 U. S. C. §80a-7(d) (1940).

⁶³ See 3 HACKWORTH, *op. cit. supra* note 4, at 624; 1 HYDE, INTERNATIONAL LAW (2d ed. 1945) 654.

⁶⁴ Nadelmann, *Legal Treatment of Foreign and Domestic Creditors*, this symposium, *supra* p. 696.

here, but the problems are rather questions of double taxation, or of discrimination against the individual, not against trade as such.⁶⁵

C. STATE LAW

The numerous limitations put by State law on the alien's right to work or to engage in certain trades or businesses have been examined elsewhere.⁶⁶ They affect international trade, in its usual connotation, indirectly, if at all. So do the limitations on the right to take by descent or discriminatory succession duties. The typical treaty establishes equality and the courts have enforced such provisions vigorously.⁶⁷

The protection afforded to interstate commerce by the Commerce clause equally applies to foreign commerce. Consequently all the learning where the line between *interstate* and *intrastate* commerce shall be drawn becomes applicable to alien individuals and to corporations incorporated under the laws of another country. If a corporation does intrastate business, it becomes subject to the State Laws setting requirements for its admission.⁶⁸

Many states exact an entrance fee from foreign corporations (incorporated in another state or in a foreign country) which has no counterpart in the levies upon domestic corporations. Usually such fee is not high and, therefore, of no particular importance. So are provisions requiring that some incorporators in forming a corporation be citizens, since the practice of dummy incorporators is so well established that it is difficult to understand why such statutes are still on the books.

Of a more serious nature are the land laws preventing aliens, alien corporations (hereafter the term will be used to indicate a corporation incorporated in another country) or domestic corporations owned or controlled by aliens to acquire land. Such restrictions are not imposed in sixteen states;⁶⁹ in thirty-one states, and in the District of Columbia, Hawaii and Alaska, exclusions exist in varying degree.⁷⁰ Some statutes exclude individuals only and are silent as to corporations,⁷¹ others include individuals and alien corporations,⁷² others aliens ineligible to citizenship,

⁶⁵ See *Burnet v. Brooks*, 288 U. S. 378 (1933); *City Bank Farmers' Trust Co. v. Bowers*, 68 F. (2d) 909 (C. C. A. 2d, 1934); *Watson v. Hoey*, 59 F. Supp. 197 (S. D. N. Y. 1943).

⁶⁶ See *supra* notes 2 and 3.

⁶⁷ *Nielsen v. Johnson*, 279 U. S. 47 (1929); Vallance, *Exemptions of Aliens from Taxation* (1929) 23 AM. J. INT. L. 394.

⁶⁸ I HYDE, *INTERNATIONAL LAW* (2d ed. 1945) 662; Feilchenfeld, *Foreign Corporations in International Law* (1926) 8 J. COMP. LEG. & INT. L. 81, 101, 261.

⁶⁹ Alabama, Colorado, Delaware, Georgia, Maryland, Massachusetts, Michigan, New Jersey, New York, North Carolina, North Dakota, Ohio, Rhode Island, Tennessee, Virginia, West Virginia. The law of Maine is not settled.

⁷⁰ Arizona, Arkansas (Japanese only), California, Connecticut (non-resident aliens), Florida (ineligible aliens), Idaho (ineligible aliens), Illinois (6 year limitation), Indiana, Iowa, Kansas (no statutory provision, but common law probably applicable), Kentucky, Louisiana (ineligible aliens only), Minnesota, Mississippi, Missouri, Montana, Nebraska, Nevada (Chinese only), New Hampshire, New Mexico, Oklahoma, Oregon, Pennsylvania, South Carolina, South Dakota (non-residents only), Texas, Utah, Vermont, Washington, Wisconsin, Wyoming (ineligible aliens only).

⁷¹ CAL. GEN. LAWS (Deering 1944) Act 261, §§1-3; ILL. REV. STAT. (1945) c. 16, §2; KY. REV. STAT. (2d ed. 1944) §§381.290, 381.320.

⁷² ARIZ. CODE (1939) §§53.804, 71.201, 71.202; IOWA CODE (1939) §§10214, 10216.

alien corporations, and all other corporations if the majority of the stock is owned by ineligible aliens.⁷³

The doubt created by the decision of the Supreme Court in the *South-Eastern Underwriters* case⁷⁴ how far the states may tax and regulate the insurance business, may affect foreign insurance desiring to engage in business in the United States. If the insurance business, or at least some of its aspects, is interstate commerce, it is *a fortiori* foreign commerce. Upon the authority of *Paul v. Virginia*⁷⁵ restrictions upon alien insurance companies have been held unaffected by treaties providing that nationals of either country are free to engage in commerce. Insurance has been said not to be "commerce" and therefore not within the protection accorded to commerce by the Jay treaty with Great Britain.⁷⁶ If the rule of *Paul v. Virginia* has been qualified by the *Underwriters* case,⁷⁷ the authority of such cases is equally weakened. Is it re-established by the Ferguson-McCarran Act consenting to regulation and taxation by the states?⁷⁸

D. JUDICIAL PROTECTION AGAINST DISCRIMINATION

The lines of defense against discriminatory provisions are multiple: diplomatic, legislative, administrative and judicial. The diplomatic protection against discrimination, if not expressed in international agreements, is of no concern here. The legislature, except in the rare case of removing disabilities inherited from the Common Law, creates discriminations. The task of protecting against discrimination thus rests with administrative bodies and, in particular, with the courts, which have been considered in Anglo-American legal thinking and popular feeling as the traditional protector of the individual. Though the following discussion will be centered upon the judicial approach, it is believed that the principles apply to any law-enforcing agency.

The validity of the discriminatory provisions of the Internal Revenue Code will be considered first, since they have been treated previously at some length and since the conclusions reached there, it is submitted, are of general application.

Relief against discrimination can be expected from two sources of law: from the Constitution and from the treaties entered into with foreign countries. The term "treaty" is not contrasted with "executive agreement," but includes any international agreement without regard to its technical designation from a constitutional

⁷³ MINN. STAT. (1941) §500.22 as amended by ch. 280, laws of 1945; MONT. CIVIL CODE §§6802.1, 6802.2; NEW MEXICO CONST. Art. II §22; ORE. COMP. LAWS ANN. (1940) §§61-101, 61-103.

⁷⁴ *United States v. South-Eastern Underwriters Ass'n*, 322 U. S. 533 (1944).

⁷⁵ 8 Wall. 168 (U. S. 1868).

⁷⁶ Compare *Liverpool Ins. Co. v. Massachusetts*, 10 Wall. 566 (U. S. 1870) with *Pearl Assurance Co. v. Harrington*, 38 F. Supp. 411 (D. C. Mass. 1941).

⁷⁷ *Bobe v. Lloyds*, 10 F. (2d) 730, 734 (C. C. A. 2d, 1926), *cert. denied*, 270 U. S. 663 (1926), but see dissent at 735.

⁷⁸ Tye, *Premium Tax Cases* (1946) 1 TAX L. REV. 259; Note, *Congressional Consent to Discriminatory State Legislation* (1945) 45 COL. L. REV. 937. Since these lines were written, the constitutionality of the Ferguson-McCarran Act has been upheld by the Supreme Court. *Prudential Insurance Co. v. Benjamin*, — U. S. —, 66 S. Ct. 1142 (June 3, 1946); see also *Robertson v. California*, — U. S. —, 66 S. Ct. 1160 (June 3, 1946).

viewpoint—always assuming its validity. Though the courts will not decide a constitutional question if the decision can be based on a non-constitutional ground, it seems convenient to reverse the order followed by the judiciary.

The Sixteenth Amendment having removed the barrier established by the Constitution upon the taxing power of the Federal Government that direct taxes must be apportioned, the protection of the individual against oppressive taxation can be sought in the Fifth Amendment only. The Fifth Amendment, in theory,⁷⁹ and at times in practice limits the taxing power of the Federal Government.⁸⁰ However, the protection is very slight. Said Mr. Justice Stone, in the *Donnan* case⁸¹ quoting from *La Belle Iron Works v. United States*:

"The Fifth Amendment has no equal protection clause; and the only rule of uniformity with respect to duties, imports, and excises laid by Congress is the territorial uniformity. . . . The difficulty of adjusting any system of taxation so as to render it precisely equal in its bearing is proverbial, and such nicety is not even required of the states under the equal protection clause, much less of Congress under the more general requirement of due process of law in taxation."

He then pointed out that no tax has been held invalid under the Fifth Amendment because based upon improper classification. The court has not receded from this stand. Thus, tax inequality as compared with citizens, which could strike down a discrimination under the equal protection clause of the Fourteenth Amendment provided that the complainant is present within the jurisdiction, is unavailable against the Federal Government.

When the discriminatory taxation "is equivalent to confiscation"⁸² or "is so arbitrary and injurious . . . as to violate the due process clause of the Fifth Amendment"⁸³ then the Fifth Amendment may afford protection. However, the quotations are *dicta*, they indicate the potentiality of protection against unreasonable classification, not its actuality. The applicability of the Fifth Amendment in its thus restricted scope, to aliens and foreign corporations is well recognized.⁸⁴ Since practically unlimited discretion is accorded to Congress in the economic field,⁸⁵ the burden is upon the contestant to show that there is an abuse of discretion by Congress,⁸⁶ that his

⁷⁹ E.g., see *Detroit Bank v. United States*, 317 U. S. 329, 338 (1943); *Foley Securities Corp. v. Comm's*, 106 F. (2d) 731, 735 (C. C. A. 8th, 1942).

⁸⁰ *Heiner v. Donnan*, 285 U. S. 312 (1932).

⁸¹ *Id.* at 338.

⁸² See *Stewart Machine Corp. v. Davis*, 301 U. S. 548, 585 (1937).

⁸³ See *Detroit Bank v. United States*, *supra* note 79, at 338.

⁸⁴ See *Bridges v. Wixon*, 326 U. S. 135, 161 (1945) [individual]; *United States v. Pink*, 315 U. S. 203, 228 (1942), dissent at 246 [same]; *Russian Volunteer Fleet v. United States*, 282 U. S. 479 (1931) [corporation]; *City Bank Farmers Trust Co. v. Bowers*, 68 F. (2d) 909 (C. C. A. 2d, 1934), *cert. denied*, 292 U. S. 644 (1934) [estate tax]; *Lord Forbes*, 25 B. T. A. 154 (1932) [income tax] noted 32 Col. L. Rev. 549; 1 MERTENS, *op. cit. supra* note 19, at §4.05.

⁸⁵ See *Polish Nat. Alliance of the United States v. N. L. R. B.*, 322 U. S. 643, 650 (1944); *Dowling, The Methods of Mr. Justice Stone in Constitutional Cases* (1941) 41 Col. L. Rev. 1160, 1168; Note (1943) 43 Col. L. Rev. 836, 937.

⁸⁶ See *United States v. Carolene Products Co.*, 304 U. S. 144, 153 (1938); *Nippert v. City of Richmond*, — U. S. —, 66 S. Ct. 586, 596 (1946) dissent; Note (1936) 36 Col. L. Rev. 283.

"demand for symmetry does not ignore the specific difference that experience is supposed to have shown to mark the class."⁸⁷ This burden, in words of another judge:⁸⁸ "does not imply one measure of equity for citizens and another for aliens; it recognizes that the interests at stake are different."

Sometimes it can even be shown that a provision discriminatory on its face against the alien in the opinion of the Legislature was intended to eliminate a discrimination against citizen and to re-establish parity between the two classes. Provisions like the flat rate imposed upon recurring items of income paid to non-residents and taxable at the source have been defended on the grounds that they prevent discrimination against citizens subject to higher surtax and in reality establish equality of taxation, that they are easy to administer and have provided substantial revenue.⁸⁹ No attempt has been made to attack the validity in court—and justly so, since the over-all fairness of the tax scheme is hardly doubtful.⁹⁰

The disallowance of deductions and credits because the return had been filed too late has been litigated in several cases, but in none was the validity attacked on constitutional or other grounds; only the applicability to the facts was in dispute.⁹¹ But the reasoning of the court in one of the best considered cases shows clearly the importance of the question of judgment—in which Congress is supreme. After referring to the legislative history of the provision—first promulgated under the rule-making power of the Commissioner of Internal Revenue, then taken over into the statute, the court proceeded to say:⁹²

"In the absence of demonstrable fraud, [foreign corporations] will, by self-serving uncooperative conduct, suffer no loss other than the general late filing penalty which is applicable to domestic as well as foreign corporations. Such a construction of the statute would put a premium on tax evasion."

When the corporation is engaged in trade or business in the United States, it is subject to investigation by revenue agents in the same manner as domestic corporations. There is nothing, except speculation, which proves that the determination of the true tax liability is more difficult than in the case of a domestic corporation, but such considerations bear upon the wisdom of the legislation and not upon its validity.

The result under the Fourteenth Amendment might be different. In holding the Illinois Income Tax Act unconstitutional the Illinois Court in *Bachrach v. Nelson*⁹³ thought that the denial of all deductions to non-residents for the failure to file a return invalidated the whole statute as violating the equal protection and privileges

⁸⁷ Holmes, J., in *Patson v. Pennsylvania*, 232 U. S. 138, 144 (1914) [due process under the XIVth Amend.].

⁸⁸ *L. Hand in City Bank Farmers Trust Co. v. Bowers*, *supra* note 84, at 912.

⁸⁹ INT. REV. CODE §§211(a), 231(a); discussion between the Assistant General Counsel of the Treasury, Mr. Kent and Mr. Vinson, *Hearings* cited *supra* note 24, at 317 *et seq.*

⁹⁰ Germany complained on the ground that the provision violated the equal treatment clause of Art. I of the treaty of December 8, 1923. 3 HACKWORTH, *op. cit.* *supra* note 4, at 577.

⁹¹ See cases cited *supra* note 53.

⁹² *Blenheim Co. v. Comm's*, 125 F. (2d) 906, 909 (C. C. A. 4th, 1942), noted 28 VA. L. REV. 657.

⁹³ 349 Ill. 579, 182 N. E. 909 (1932) (alternative holding).

and immunities clause of the Fourteenth Amendment. Without examining the general soundness of the position, it must be noted that the holding does not advance the present problem arising under the Fifth Amendment which in terms has no equal protection clause. Whether other state courts would follow when the validity of similar statutory provisions were to be decided, is highly doubtful.⁹⁴

Once it is recognized that different classification is the basis of discrimination and that in all cases discrimination in matters of taxation can be formulated in terms of the grant or denial of a subsidy, there is no basis left for application of the Fifth Amendment. It will, indeed, be a hard task to demonstrate that a subsidy denied aliens is not based upon some rational basis—or at least that there might be such basis so as to leave the determination to Congress.

Consequently, the only relief to be expected, can be found in the international agreements which on their face manifest the desire to establish equality. Such agreements are of several types: conventions to avoid double taxation, general commercial treaties and trade agreements. The cases interpreting the latter class of treaties in matters of taxation have not been numerous, since the problems raised by the combination of international law (interpretation of the most-favored nation clause) and tax law are frequently out of proportion of the amounts involved and apt to deter from litigation.⁹⁵ The cases arising from the treaties intending in terms to prevent double taxation are similarly few, so that the question resolves itself in problems of statutory construction.

In general discriminatory treatment of commerce is out of step with current trends in American legislation.⁹⁶ So is discriminatory taxation unless retaliatory.⁹⁷ The section of the Internal Revenue Code giving the President the power to increase the tax rates against nationals of a country imposing a discriminatory tax on American nationals was enacted for the very purpose of compelling France to come to an agreement putting an end to discrimination against American interests. But this background is rather a declaration of policy than a tool for deciding cases. It emphasizes the legislative discretion, here delegated by Congress to the President, but does not assist in answering the question whether discrimination exists that can receive judicial recognition.

The provisions in tax conventions aimed at equality of income taxation are similarly phrased in general terms without reference to any particular provisions in the revenue laws of the contracting states. So the treaty with Canada⁹⁸ provides:

"Citizens of one of the contracting States residing within the other contracting State shall not be subjected to the payment of more burdensome taxes than the citizens of such other State."

⁹⁴ Denial of family exemption to non-residents for failure to file a return has been upheld in *Stouffer v. Crawford*, 248 S. W. 581 (Sup. Ct. Mo., 1923, not officially reported); see also *Standard Lumber Co. v. Pierce*, 112 Ore. 314, 228 Pac. 812 (1924).

⁹⁵ Wurzel, *supra* note 12, at 487.

⁹⁶ See TRADE AGREEMENTS ACT of 1934, 48 STAT. 943 (1934), 19 U. S. C. A. §1351 (Suppl. 1945).

⁹⁷ INT. REV. CODE §103.

⁹⁸ Protocol par. 12, 57 STAT. 1399 (1942).

The treaty with Sweden in otherwise substantially equivalent terms refers to "other or higher taxes than are imposed upon the citizens" of the other state.⁹⁹

The treaty with France is still more specific as it includes "citizens and corporations or other entities" which shall not be subjected to "the payment of higher taxes" than those imposed upon nationals.¹⁰⁰ The Convention with Great Britain combines the language of the Canadian treaty, inasmuch as it is designed to prevent "other or more burdensome taxes," is not restricted to citizens but applies to nationals, a term including "legal persons, partnerships and associations."¹⁰¹ It is therefore arguable that the treaties with Canada and Sweden do not extend beyond their literal reading. However, such interpretation would appear unduly restrictive in times when corporations are playing an increasingly important part in commercial intercourse.¹⁰² Admittedly each treaty has to be interpreted in the light of its own history and background,¹⁰³ but these treaties are in *pari materia* and the variations in language hardly justify a different construction. The more reasonable interpretation is not to restrict the term "citizen" to individuals but to give it a broad meaning, the meaning of "national" as used by the Draft Convention with Great Britain.

It is next to be noted that the national treatment accorded by the conventions applies in the Canadian, Swedish and British treaties only to persons *residing* in the other country; the French convention avoids the problems by using a phrase "within the jurisdiction." The construction of the term "residing" in the technical meaning of the Internal Revenue Code leads to absurd results. Indeed, an alien individual engaged in trade or business in the United States is called a "non-resident alien," whereas a corporation similarly engaged is called "a resident foreign corporation."¹⁰⁴ Literally the former is not protected, the latter is protected.

The term resident as used in the income tax statute of Anglo-Saxon countries with reference to individuals has a widely different meaning. So it has been held in England, that an American citizen who used to hunt in Scotland two months every year and had rented a shooting lodge there, was a resident of the United Kingdom and taxable as such.¹⁰⁵ The Exchequer Court of Canada accepted that view, but the Supreme Court of Canada rejected it.¹⁰⁶ There is not the slightest doubt that such person is a non-resident alien in the meaning of the Internal Revenue Code. On the other hand, a person present in Canada during 183 days within the taxable year, is taxed like a resident. Under the Code such person—without

⁹⁹ Protocol par. 7, 54 STAT. 1759 (1939).

¹⁰⁰ Protocol par. V, 59 STAT. — (1945).

¹⁰¹ Art. XXI, *supra* note 16.

¹⁰² See *Jordan v. Tashiro*, 278 U. S. 123, 129 (1928).

¹⁰³ See *Choctaw Nation v. United States*, 318 U. S. 423, 432 (1943); *Arizona v. California*, 292 U. S. 341, 360 (1934); *Cook v. United States*, 288 U. S. 102, 116 (1933).

¹⁰⁴ Compare INT. REV. CODE §211(b) with §231(b).

¹⁰⁵ *C. I. R. v. Cadwalader*, 12 Scots. L. T. R. 449, 5 Tax Cas. 1904 (1904); *Loewenstein v. De Salis*, 10 Tax Cas. 424 (1926).

¹⁰⁶ *Thomson v. Minister of Nat. Revenue*, [1946] 7 D. L. R. 689, 691, 693 (Sup. Ct. of Can.) *aff'g* [1945] 1 D. L. R. 45 [Exch. Ct. of Can.].

more—would be a non-resident. To except such persons from the protection of the treaties is obviously an unreasonable result. Consequently the term "resident" or its equivalent cannot be given the meaning it has in the laws of each of the contracting states, but a different meaning, adapted to the laws of the states involved. The conclusion is submitted that aliens in some, not nearer defined, territorial relation to the United States shall enjoy the equal treatment. The kind of relation satisfying the treaty will depend upon an analysis of each situation taking due care of the fact that every term is supposed to fit the concepts of two legal systems.

A further difficulty arises when an attempt is made to understand what is meant by not "higher taxes," or by not "more burdensome taxes." All the discriminations that have been discussed ultimately result in higher taxes than those imposed upon American nationals similarly situated. It seems clear that a poll tax of \$10 applicable to aliens but not to citizens violates a treaty prohibiting the imposition of "not other," or "not higher" or "not more burdensome" taxes.¹⁰⁷ If the meaning is restricted to such very crude discrimination, the tax conventions have accomplished very little real progress.¹⁰⁸ But any departure from such simple test will be faced with doubts as to whether form will not prevail over substance by mechanically equalizing situations actually dissimilar. The tax advantage accorded to small domestic corporations, if covered by the phrase "not higher taxes" could benefit foreign corporations of considerable financial power provided that their domestic income (which is the income taken into account for that purpose) comes within the lower income bracket.¹⁰⁹ Reconciling such result with the purpose of the statute is an arduous task and only with hesitation would one conclude that the clause covers the case. Whether the same consideration apply to the treatment of capital losses is doubtful.¹¹⁰ The advantage is given without regard to size of the beneficiary and therefore the technical provision of the Code which may reduce a foreign giant corporation for federal income tax purposes to a dwarf, do not apply. Nevertheless some doubts will still linger and the outcome of litigation is hard to predict.

A less difficult problem is presented by the disallowance of deductions for failure to file a return.¹¹¹ In an unpublished letter the Treasury Department has taken the position that the disallowance of deductions for failure to file a timely or accurate return did not violate the Draft Convention with Great Britain. The reason assigned for such position is somewhat surprising. There is no discrimination since the disallowance is not the result of statutory provisions but of the taxpayers delinquency. As ingenious as the argument may sound, it is submitted that it proves too much. The very characteristic of a norm in general and of a penalty—and the

¹⁰⁷ *Ex parte Kotta*, 187 Cal. 20, 200 Pac. 954 (1927) invalidating the California Alien Poll Tax Act as contrary to the treaty with Japan of April 5, 1911, 32 STAT. 1504 (1911).

¹⁰⁸ See Cutler, *Treatment of Foreigners* (1937) 27 AM. J. INT. L. 225, 236.

¹⁰⁹ See discussion, *supra* p. 780.

¹¹⁰ *Id.* at 781.

¹¹¹ *Id.* at 782.

disallowance of deductions is in the nature of a penalty—requires first a statute imposing the sanction, and second, acts being the individual instance to which the statute shall be applied. Though the classification may be constitutionally immune, it will not require much effort to hold it not applicable under a treaty granting equality.

A much more difficult problem is presented by the Regulated Investment Companies.¹¹² The exemption from the corporate normal and surtax is based upon the theory to treat them as mere conduit so as to tax income either to the company or to the stockholder. The taxation of non-resident stockholders on the dividends received from foreign corporations is subject to intricate rules,¹¹³ so is the taxation of foreign corporations which may have domestic and foreign stockholders. The complexity of the administrative problems raised by an attempt to equalize domestic and foreign companies, to prevent escape of income from taxation by operation of the basic surtax credit provisions and to tax nevertheless every item of income once, either to the stockholders or to the company, are apt to exclude the provision from the scope of the national parity clause. No instance is known to the writer where inclusion has been claimed.

The provisions in the Tax Conventions have their counterpart in similar provisions in general commercial, or consular treaties entered into by the United States. The language of the clause has varied over the years,¹¹⁴ but has not substantially changed. The clause has proved effective in cases in which states attempted to collect discriminatory inheritance taxes,¹¹⁵ but there is again no direct precedent for the more subtle type of discrimination.

If recourse is had to the principles underlying the interpretation of treaties there is a wide choice of judicial pronouncements which may justify a restrictive or a liberal interpretation. The several principles are equally well established. First: treaties will be liberally construed.¹¹⁶ Second: international agreements will be scrupulously observed.¹¹⁷ Third: if possible a statute and a treaty will be construed together so as to avoid a contradiction.¹¹⁸ Fourth: if there is contradiction the later in date prevails.¹¹⁹ Fifth: specific provisions in a treaty are not superseded by later general statutes.¹²⁰

¹¹² *Id.* at 783.

¹¹³ *Id.* at 780.

¹¹⁴ 3 HACKWORTH, *op. cit. supra* note 4, at 577.

¹¹⁵ *Nielsen v. Johnson*, 279 U. S. 47 (1929); *Vallance, Exemption of Aliens from Taxation* (1929) 23 AM. J. INT. L. 395 and cases discussed there.

¹¹⁶ See *Factor v. Laubenheimer*, 290 U. S. 276 (1933); *Hauenstein v. Lynham*, 100 U. S. 483, 487 (1879); 2 HYDE, INTERNATIONAL LAW (2d ed. 1945) 1478.

¹¹⁷ See *Bacardi Corp. of America v. Domenech*, 311 U. S. 150, 163 (1940).

¹¹⁸ *United States v. Domestic Fuel Corp.*, 71 F. (2d) 424 (C. C. P. A., 1934); 2 HYDE, INTERNATIONAL LAW (2d ed. 1945) 1464.

¹¹⁹ *Pigeon River Co. v. Cox Co.*, 291 U. S. 138, 160 (1934); *Watson v. Hoey*, 59 F. Supp. 197, 200 (S. D. N. Y. 1943).

¹²⁰ *Cook v. United States*, 288 U. S. 102 (1933); *John I. Bill v. United States*, 104 F. (2d) 67 (C. C. P. A., 1939), noted Catudal, *The Most Favored Nation Clause and the Courts* (1941) 35 AM. J. INT. L. 41; *The Taigen Maru*, 73 F. (2d) 922 (C. C. A. 9th, 1934); see *MacEvoy Co. v. United States*, 322 U. S. 102, 107 (1944).

Principles one, two and five seem to support any treaty provision except against an unequivocal repudiation by the statute. Such was the position of the court in the *Domestic Fuel Corporation* case, one of the few cases dealing with discriminatory taxation.¹²¹ In that case the court held that the application of a higher excise tax on coal imposed by Section 601 of the Revenue Act of 1932 was a violation of the most-favored nation clause accorded to Great Britain and Germany because a similar tax was not imposed upon coal imported from Canada and Mexico. The Act had a saving clause which the court applied literally and rejected a narrow construction urged by the Government.

Whether the court's decision was influenced by the fact that the tax was in effect a higher customs duty does not appear from the opinion. It is therefore difficult to say how valid the precedent set by the case is in cases like those under discussion. It should further be remembered that the court was dealing with an excise tax, akin to a higher customs duty, the statutory mandate notwithstanding,¹²² and within the traditional scope of the most-favored nation clause—that is, to equalize the competitive position of foreign nationals by eliminating discriminatory barriers for the import of goods. Whether a court would be willing to extend the national parity by operation of a most-favored nation clause beyond the clear import of the language is doubtful. The Department of State has taken the position that special privileges granted by treaty, e.g., those pertaining to air navigation or Workmen's Compensation Acts are not covered by the clause.¹²³ Since there is no rule of international law that forbids discrimination in general and in particular heavier taxation on the ground of alienage,¹²⁴ a restrictive interpretation can be expected. Moreover, in the field of taxation, the Internal Revenue Code specifically mentions the exclusion of income to the extent *required* by treaty.¹²⁵ This, with the State Department's position and with the trend of construing exemptions from taxation narrowly, gives little prospect for superseding special provisions disfavoring aliens by general treaty clauses promising equal treatment with nationals. The Fiscal Committee of the League of Nations has adopted the same narrow construction of the most-favored nation clause and rejected its application to matters of taxation.¹²⁶ The background is the same; since every right granted to an alien is a privilege, there is little prospect that discrimination would fare differently.

In discussion of the discriminatory effect of double taxation the question has been raised whether national parity granted to some nation is extended to others by the standard most-favored nation clause used in the Reciprocal Trade Agreements.¹²⁷ Some of these agreements have broad language to the effect that charges

¹²¹ *Supra* note 118.

¹²² No tax shall be construed as a custom duty unless the Act so provides. TARIFF ACT OF 1930, §528 as amended, 52 STAT. 1087 (1938), 19 U. S. C. §1528 (1940); see INT. REV. CODE §3430.

¹²³ See 2 HYDE, INTERNATIONAL LAW (2d ed. 1945) 1514.

¹²⁴ 1 *id.* at 664.

¹²⁵ INT. REV. CODE §22(b)-7.

¹²⁶ LEAGUE OF NATIONS, FISCAL COMM. REPORT, II ECON. AND FIN. 1930, II 23, p. 7 (C. 340. M. 140. 1930. II).

¹²⁷ Wurzel, *supra* note 12, at 488.

of every kind on imported goods and all laws and regulations affecting the sale or use of imported goods shall be included in the most-favored nation treatment.¹²⁸ The rationale of *Peck v. Lowe*¹²⁹ that income taxes are only remotely connected with the sale of goods, cuts short any argument for such extension. The scope of the clause when applied to regulatory measures is less clear. It applies to the imports of goods and to regulations by which they are affected, but probably does not give any protection to commercial activities indirectly connected with import of goods: e.g., brokerage, insurance, investments.

As summary five points are submitted: 1. The Fifth Amendment does not afford protection against discriminatory taxation. 2. Effective equality of treatment can be granted by legislation or, its equivalent, international agreements. 3. Such agreements are effective for preventing crude discriminations but they have not been tested as far as the more subtle type is concerned. 4. It is desirable to give the broadest effect to such clauses, but no judicial pronouncements give any reliable guide. 5. The most-favored nation clause will not extend advantages granted in matters of income taxes, but will do so in the case of excise taxes.

With a slight variation these points are applicable to discriminatory state laws, if they do not fall under the prohibition of the commerce clause.¹³⁰ The equal protection clause of the Fourteenth Amendment cuts probably deeper than the due process clause,¹³¹ but here, as elsewhere, there has been a gradual recession of judicial intervention.¹³² The acquisition of land by aliens and the admission of corporations in particular, are subject to state law,¹³³ in absence of treaty provision. The supremacy of the Federal Government in foreign affairs is so well established today that no state barrier against international trade could be validly established or maintained against an express provision in an international agreement.¹³⁴ However, general clauses will not fare as well; as against such clauses, juridical notions

¹²⁸ E.g., Art. II of the Trade Agreement with Great Britain of Nov. 17, 1938, 52 STAT. 1897, 1899 (1938):

"Articles . . . of either Contracting Party shall not be subjected . . . , to other or higher duties or charges of any kind or to any rule or formalities other or more burdensome than those to which articles . . . of any other country are subject . . ."

"Any advantage, favor, privilege or immunity which has been or may hereafter be granted in the territories of either High Contracting Party in respect of any article originating in or destined for any other foreign country in regard to custom duties and other charges of any kind imposed on or in connection with importation or exportation, to the method of levying such duties or charges . . . , and to all Laws and or regulations affecting the sale or use of imported goods . . . shall be accorded immediately and unconditionally. . ."

¹²⁹ 247 U. S. 165 (1918); see Charles Strom, 6 T. C. No. 81 [tax on income from fishing, not tax on fishing].

¹³⁰ See *Crowley v. Allen*, 52 F. Supp. 850, 854 (S. D. Cal. 1943), in the Supreme Court on another point *sub nom.* *Markham v. Allen*, — U. S. —, 66 St. Ct. 296 (1946), and cases there cited; Lockhart, *State Tax Barriers to Interstate Trade* (1940) 53 HARV. L. REV. 1253.

¹³¹ See *Queenside Hills Realty Co. v. Saxl*, — U. S. —, 66 S. Ct. 850 (1946).

¹³² See *Madden v. Kentucky*, 309 U. S. 83, 88 (1940).

¹³³ *Ashbury Hospital v. Cass County*, — U. S. —, 66 S. Ct. 61 (1946); *Lincoln Nat. Life Ins. Co. v. Read*, 325 U. S. 673 (1945).

¹³⁴ *United States v. Pink*, 315 U. S. 203 (1942); *Bacardi Corp. of America v. Domenech*, 311 U. S. 150 (1940).

like the police power or business dedicated to a public use will cover a narrow construction of a treaty.¹³⁵

¹³⁵ As said by Mr. Justice Frankfurter, in *Pearl Assurance Co. v. Harrington*, 38 F. Supp. 411, 413-4 (D. Mass. 1941), with reference to the treaties entered into with Great Britain:

"[They] permit regulations conventionally justified as exercises of the police power. The times admonished us to be fastidiously scrupulous in the observance of international agreements. . . . State legislation bunglingly or skillfully contrived to evade an international obligation undertaken by the United States should unhesitatingly be stricken down. But we find no such consequence in the act before us. It is . . . part of the historic policy of Massachusetts for the safe conduct of a financial enterprise on which its citizens are peculiarly dependent [to require the resident manager of an alien insurance company to be American]. A sensible and just reading of the treaties certainly does not withdraw the normal scope of the police power from the states."