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RACKETEERING, RICO AND THE REVENUE RULE IN *ATTORNEY GENERAL OF CANADA V. R.J. REYNOLDS*: CIVIL RICO CLAIMS FOR FOREIGN TAX LAW VIOLATIONS

Elizabeth J. Farnam

Abstract: When Congress passed the Racketeer Influenced Corrupt Organizations Act (RICO), it created a civil cause of action for any entity, including a foreign government, to recover for injury caused by a defendant's pattern of racketeering activity. However, Congress did not expressly indicate how the revenue rule, a conflict of laws doctrine that allows a court to decline to enforce a foreign government's tax claim or judgment, would relate to civil RICO claims. In *Attorney General of Canada v. R.J. Reynolds Tobacco Holdings, Inc.*, the United States Court of Appeals for the Second Circuit held that the revenue rule barred Canada's civil RICO suit for lost tax revenues caused by R.J. Reynolds' extensive tobacco smuggling scheme. This Note argues that the revenue rule should not block Canada's civil RICO suit. The rationale for the revenue rule, the constitutional separation of powers principle, would not be implicated if the court were to hear the case. In addition, the majority opinion impermissibly expanded the revenue rule to restrict the scope of RICO because the rule had previously only applied to claims based on foreign tax laws.

Between 1991 and 1997, R.J. Reynolds allegedly participated in an elaborate scheme to smuggle tobacco in contravention of Canadian tax laws.[1] In response, Canada brought a suit under the Racketeer Influenced Corrupt Organizations Act (RICO)[2] to recover, inter alia, lost tax revenues and increased law enforcement expenses. A federal district court in the Northern District of New York dismissed Canada's suit for failure to state a claim.[3] The United States Court of Appeals for the Second Circuit affirmed.[4] Specifically, the Second Circuit held that the revenue rule, which states that U.S. courts are not required to enforce foreign tax judgments,[5] bars the claim because the RICO damages would be calculated based on lost revenues.[6] Yet, had the plaintiff been New

1. *See* Attorney Gen. of Can. v. R.J. Reynolds Tobacco Holdings, Inc. [hereinafter Reynolds I], 103 F. Supp. 2d 134, 137–38 (N.D.N.Y. 2000), aff'd [hereinafter Reynolds II], 268 F.3d 103, 106–07 (2d Cir. 2001); United States v. Miller, 26 F. Supp. 2d 415, 419 (N.D.N.Y. 1998) (criminal case).

2. 18 U.S.C. §§ 1961–1968 (1994).

3. *Reynolds I*, 103 F. Supp. 2d at 144.

4. *Reynolds II*, 268 F.3d at 106.

5. *See* Banco Nacional de Cuba v. Sabbatino, 376 U.S. 398, 413–14 (1964); RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW OF THE UNITED STATES, § 483 (1987) [hereinafter RESTATEMENT].

6. *Reynolds II*, 268 F.3d at 106.

York State instead of Canada, the suit would have proceeded.[7] After *Attorney General of Canada v. R.J. Reynolds* [hereinafter *Reynolds II*],[8] the Second Circuit denied Canada's petition for rehearing, and Canada filed a petition for certiorari to the United States Supreme Court.[9]

The illicit tobacco trade emanating from the U.S. has become a global problem.[10] In recent years, American tobacco companies have apparently smuggled cigarettes into Canada, the European Union, Ecuador, Honduras, Belize, and Colombia.[11] Following the *Reynolds II* decision, other civil RICO cases have been pursued, most recently in Florida.[12] Thus, the issues presented in *Reynolds II* will likely be reconsidered in another circuit, if not in the U.S. Supreme Court. However, although RICO allows foreign states to assert claims to remedy racketeering injuries,[13] the *Reynolds II* decision now effectively nullifies their cause of action if they seek to recover lost tax revenue in the Second Circuit.[14]

This Note argues that the *Reynolds II* court should have allowed Canada's civil RICO suit to proceed. Part I explains the scope and purpose of RICO. Part II describes the revenue rule's origins, the debate surrounding the rule's validity, and the present state of the rule in U.S. law. Part III details the facts, history, and rationale of *Reynolds II*.[15] Finally, Part IV argues that *Reynolds II* was wrongly decided for two reasons. First, the Second Circuit incorrectly found that the case presented a separation of powers problem, leading the court to inappropriately apply the revenue rule to block Canada's claim. Second,

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7. *See* Missouri v. W.E.R., 55 F.3d 350, 357 (8th Cir. 1995) (State has a cause of action under civil RICO); United States v. Porcelli, 865 F.2d 1352, 1355 (2d Cir. 1988); Ill. Dep't of Revenue v. Phillips, 771 F.2d 312, 313 (7th Cir. 1985) (finding that the government stated a claim for civil RICO for repeated mailing of false tax returns, a mail fraud violation).

8. 268 F.3d 103.

9. Attorney General of Canada v. R.J. Reynolds, 268 F.3d 103, *petition for cert. filed*, 35 U.S.L.W. 3580 (U.S. March 19, 2002) (No. 01-1317); *see also* Cristin Schmitz, *U.S. Supreme Court Asked to Review Tobacco-Suit Dismissal*, THE LAWYERS WEEKLY, March 22, 2002 at 19.

10. *See generally Reynolds II*, 268 F.3d at 103; Republic of Ecuador v. Philip Morris, 188 F. Supp. 2d 1359 (S.D. Fla. 2002); European Community v. Japan Tobacco, Inc., 186 F. Supp. 2d 231 (E.D.N.Y. 2002); European Community v. RJR Nabisco, Inc., 150 F. Supp. 2d 456, 460 (E.D.N.Y. 2001).

11. *See generally Reynolds II*, 268 F.3d 103; *Philip Morris*, 188 F. Supp. 2d at 1359; *Japan Tobacco*, 186 F. Supp. 2d at 231; *European Cmty.*, 150 F. Supp. 2d at 460.

12. *See Philip Morris*, 188 F. Supp. 2d at 1359.

13. *See* Republic of the Philippines v. Marcos, 862 F.2d 1355, 1358 (9th Cir. 1988).

14. *See Japan Tobacco*, 186 F. Supp. 2d at 234.

15. *Reynolds II*, 268 F.3d at 106.

the *Reynolds II* court employed a novel expansion of the revenue rule that impermissibly restricted the scope of RICO.

I. IN RICO, CONGRESS CREATED BROAD REMEDIES TO FIGHT RACKETEERING

In 1970, Congress enacted RICO,[16] a remedial statute that provides both criminal penalties and civil remedies against defendants who participate in a pattern of racketeering activity.[17] The statute was a response to a two-decade investigation that revealed the enormous influence of organized crime on businesses, state and local governments, and labor unions.[18] This widespread impact[19] lead Congress "to seek the eradication of organized crime in the United States . . . by establishing new penal prohibitions, and by providing enhanced sanctions and new remedies to deal with the unlawful activities of those engaged in organized crime."[20]

Culpability under RICO arises out of a preliminary three-step analysis: the defendant must have committed racketeering activity, the defendant's activity must amount to a pattern, and the defendant must thereby influence an enterprise engaged in interstate commerce.[21] RICO defines racketeering activity by reference to specific state[22] and federal criminal laws prohibiting extortion, embezzlement, mail fraud, wire fraud, obstruction of justice, securities fraud, money laundering, obscene materials, terrorism, and drug activity.[23] To commit a pattern of racketeering, a defendant must have committed a minimum of two of the

16. 18 U.S.C §§ 1961–1968 (1994).

17. *Id.*

18. *See* THE ABA REPORT ON ORGANIZED CRIME AND LAW ENFORCEMENT 10 (1952–1953); PRESIDENT'S COMMISSION ON LAW ENFORCEMENT AND ADMINISTRATION OF JUSTICE, THE CHALLENGE OF CRIME IN A FREE SOCIETY 200–09 (1967); *see also* G. Robert Blakey, *The RICO Civil Fraud Action in Context: Reflections on* Bennett v. Berg, 58 NOTRE DAME L. REV. 237, 249 (1982).

19. Organized Crime Control Act of 1970, Pub. L. No. 91-452, 84 Stat. 922, 923 (1970); 18 U.S.C. § 1961 (detailing RICO's history). The Statement of Findings and Purpose notes that "organized crime in the United States is a highly sophisticated, diversified, and widespread activity that annually drains billions of dollars from America's economy by unlawful conduct and the illegal use of force, fraud, and corruption." *Id.*

20. S. REP. NO. 91-617, at 76 (1969).

21. 18 U.S.C. §§ 1961–1962; *see also* Sedima, S.P.R.L. v. Imrex Co., 473 U.S. 479, 496 (1985).

22. State laws must be punishable by more than one year imprisonment. 18 U.S.C § 1961.

23. *Id.*

listed crimes within a ten-year period.[24] In addition, the acts must have "continuity plus relationship"—the acts must have been related to each other and continue or threaten to continue.[25] Finally, the racketeering activity must have influenced an enterprise that is involved in interstate commerce.[26] For example, a defendant might invest proceeds of racketeering activity into a lawful business or undertake a smuggling scheme through a corporation.[27]

RICO allows foreign governments to recover losses resulting from racketeering activity.[28] RICO specifically permits a civil cause of action for any person whose business or property is injured due to a RICO violation.[29] RICO defines a person as "any . . . entity capable of holding a legal or beneficial interest in property."[30] Therefore, a foreign government is considered a person for the purposes of the RICO statute,[31] allowing foreign governments to file RICO claims.[32]

RICO provides substantial civil remedies for damages suffered due to RICO violations.[33] Eligible plaintiffs may sue for treble damages[34] and reasonable attorney's fees.[35] Compensable injuries may include intangible losses, such as the value of confidential business information.[36] The Second Circuit has recognized that lost tax revenue is a cognizable RICO injury.[37]

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24. *Id.* § 1961(5). In some cases, more than two acts may be required. *See, e.g,.* H.J. Inc. v. N.W. Bell Tel. Co., 492 U.S. 229, 237–38 (1988).

25. *H.J. Inc.*, 492 U.S. at 239.

26. 18 U.S.C § 1962(b).

27. *Id.* § 1962(a)–(d).

28. *Id.* § 1962(a)–(c).

29. *Id.* § 1964(c).

30. *Id.* § 1961(3).

31. Republic of the Philippines v. Marcos, 862 F.2d 1355, 1358 (9th Cir. 1988); *Cf.* Ill. Dep't of Revenue v. Phillips, 771 F.2d 312, 316 (7th Cir. 1985) (holding that state governmental units can sue under RICO).

32. *Cf.* Pfizer, Inc. v. India, 434 U.S. 308, 312–20 (1978) (applying the Clayton Act, 15 U.S.C. § 4 (1994), a statutory predecessor of RICO).

33. 18 U.S.C. § 1964(c).

34. "Treble damages" consist of three times the damages the plaintiff actually suffered. BLACK'S LAW DICTIONARY 397 (7th ed. 1999).

35. 18 U.S.C. § 1964(c).

36. *Cf.* Carpenter v. United States, 484 U.S. 19, 26–27 (1987) (relating to mail and wire fraud).

37. *See* United States v. Porcelli, 865 F.2d 1352, 1355 (2d Cir. 1988).

The purpose of RICO is both to compensate victims and to turn them into "private attorneys general"[38] who act to "fill prosecutorial gaps."[39] Congress seeks not merely to punish offenders for racketeering, but also to attack organized crime at its economic roots,[40] divesting the RICO enterprise of its illegal earnings.[41] By establishing both civil and criminal sanctions and incorporating a considerable array of state and federal crimes, Congress ensured that RICO would be a broad remedial statute.[42]

Congress expressly noted that RICO must be "liberally construed to effectuate its remedial purposes."[43] The United States Supreme Court has complied with this mandate by allowing RICO claims in many situations that Congress did not expressly mention.[44] For example, in *United States v. Turkette*,[45] the Court refused to limit the broad language of RICO by holding that both legitimate and illegitimate businesses could be prosecuted under civil RICO.[46] The Court has also allowed a RICO claim against an association of pro-life demonstrators, despite a lack of economic motive.[47] In fact, plaintiffs have successfully used the statute against an assortment of defendants, including manufacturers of farmers' silos,[48] a commercial bank that improperly calculated interest,[49] violators of the Employee Retirement Income Security Act,[50] and health insurers.[51]

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38. Rotella v. Wood, 528 U.S. 549, 557 (2000).

39. *See* Sedima, S.P.R.L. v. Imrex Co., 473 U.S. 479, 493 (1985).

40. United States v. Turkette, 452 U.S. 576, 585 (1981).

41. *Id.*

42. *See Sedima*, 473 U.S. at 481.

43. Pub. L. No. 91-452 § 904(a), 84 Stat. 922, 947 (1970). Liberal construction will tend to favor the plaintiff, while strict construction will tend to favor the defendant. *See generally* Craig W. Palm, Note, *RICO and the Liberal Construction Clause*, 66 CORNELL L. REV. 167 (1980).

44. *See* Sedima, S.P.R.L. v. Imrex Co., 741 F.2d 482, 487 (2d Cir. 1984), *rev'd*, 473 U.S. 479 (1985); *See also* Cedric Kushner Promotions, Ltd. v. King, 533 U.S. 158, 160 (2001) (holding an employee can be a person distinct from corporation); Salinas v. United States, 522 U.S. 52, 61–66 (1997) (holding conspiracy defendant himself need not have committed racketeering acts); Nat'l Org. for Women v. Scheidler, 510 U.S. 249, 256–62 (1994) (holding economic motive not required).

45. 452 U.S. 576 (1981).

46. *Id.* at 587.

47. *Scheidler*, 510 U.S. at 261.

48. *See generally* Klehr v. A.O. Smith Corp., 521 U.S. 179 (1997) (product defect action against manufacturers of farmers' silos).

49. *See generally* Haroco, Inc. v. Amn. Nat'l Bank & Trust Co., 747 F.2d 384, 399 (7th Cir. 1984) ("Congress appears to have preferred a broad statute, even if overinclusion might result.").

50. 29 U.S.C. §§ 1001–1461 (1994). *See generally* Crawford v. La Boucherie Bernard Ltd., 815 F.2d 117 (D.C. Cir. 1987) (ERISA violations).

51. *See generally* Humana Inc. v. Forsyth, 525 U.S. 299 (1999) (claim against health insurers).

The Ninth Circuit has even allowed the Philippines to proceed with a civil RICO claim against its former president, Ferdinand Marcos, and his wife.[52] The Philippines alleged that the Marcoses misappropriated government money, committed mail and wire fraud, and transported stolen property into the United States in a pattern of racketeering activity.[53] The court held that the Philippines government had standing to bring a RICO claim.[54]

The U.S. Supreme Court has also been willing to admonish lower federal courts for attempting to narrow RICO's broad language through judicial "statutory amendment."[55] For example, in *Sedima, S.P.R.L. v. Imrex Co.*,[56] a Belgian corporation filed a civil RICO claim against an American corporation based on mail and wire fraud.[57] The Second Circuit created an additional standing requirement that a civil RICO plaintiff must demonstrate racketeering injury above and beyond the injury caused by the underlying unlawful acts.[58] Furthermore, the Second Circuit held that a civil RICO defendant must have been previously convicted of the underlying crimes.[59] The Supreme Court reversed, holding that the additional requirements limited civil claims in a manner inconsistent with the history, language, and policy of RICO.[60] Thus, the Court refused to allow lower courts to invent restrictions on civil RICO claims that would limit the statute's scope.

II. THE REVENUE RULE PERMITS COURTS TO DISMISS FOREIGN TAX CLAIMS

The revenue rule is an American conflict of laws principle[61] that permits a court to decline to enforce foreign tax judgments or hear

52. Republic of the Philippines v. Marcos, 862 F.2d 1355, 1375 (9th Cir. 1989).

53. *Id.* at 1357–58.

54. *Id.*

55. Sedima, S.P.R.L. v. Imrex Co., 473 U.S. 479, 500 (1985).

56. *Id.* at 479.

57. *Id.* at 483–84.

58. *Id.* at 481.

59. *Id.* at 493.

60. *Id.*

61. EUGENE F. SCOLES, ET AL., CONFLICT OF LAWS, 1189 (3d ed. 2000). American application of the rule does not depend on the existence of a similar rule in a foreign jurisdiction: "[A] court normally does not make its own rule dependent upon what the doctrine of a foreign state on a point may be nor varies its own rule according to the foreign conflict-of-laws rule." *Id.*

foreign tax claims,[62] despite the general rule that foreign judgments are usually recognized in U.S. courts.[63] The rule arose over two hundred years ago in England, when Lord Mansfield announced in *Holman v. Johnson*[64] that "no country ever takes notice of the revenue laws of another."[65] In American case law, the rule evolved into a domestic revenue rule, which was applied and then almost completely abolished between sister states of the United States, and an international revenue rule.[66] Federal courts have seldom applied the rule, so scarce case law exists clarifying its scope. Recently, the rule has been applied to causes of action arising under U.S. statutes.[67]

A. The Revenue Rule in the United States

The English revenue rule gave rise to two distinct lines of American cases.[68] The domestic revenue rule consists of sister states' refusal to enforce each other's tax claims or judgments.[69] The international revenue rule involves the enforcement of foreign states' tax claims and judgments.[70]

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62. *See* RESTATEMENT, *supra* note 5 and accompanying text.

63. *See* Hilton v. Guyot, 159 U.S. 113, 201–202 (1895) (recognizing international comity doctrine).

64. 98 Eng. Rep. 1120, 1 Cowp. 341 (K.B. 1775).

65. *See id.* at 1121; Boucher v. Lawson, 95 Eng. Rep. 53 (K.B. 1734) (Lord Hardwicke, C.J.). In these cases, 18th Century British courts chose to uphold contracts that violated foreign law in order to protect the British smuggling trade. *See also* State *ex rel.* Okla. Tax Comm'n v. Rodgers, 193 S.W.2d 919, 923 (Mo. Ct. App. 1946); William J. Kovatch, Jr., *Recognizing Foreign Tax Judgments: An Argument for the Revocation of the Revenue Rule*, 22 HOUS. J. INT'L L. 265, 272–77 (2000).

66. *See generally Rodgers*, 193 S.W.2d 919, 922–26; Kovatch, *supra* note 65.

67. *See generally* United States v. Boots, 80 F.3d 580 (1st Cir. 1996); United States v. Trapilo, 130 F.3d 547, 548–49 (2d Cir. 1997); European Cmty. v. RJR Nabisco, Inc., 150 F. Supp. 2d 456, 472 (E.D.N.Y. 2001); *Reynolds II*, 268 F.3d 103, 106 (2d Cir. 2001). *Cf.* United States v. Pierce, 224 F.3d 158 (2d Cir. 2000).

68. *See generally* Milwaukee County v. M.E. White Co., 296 U.S. 268, 271 (1935); Her Majesty the Queen in Right of the Province of British Columbia v. Gilbertson, 433 F. Supp. 410, 411 (1977), *aff'd*, 597 F.2d 1161 (9th Cir. 1979).

69. *See Milwaukee County*, 296 U.S. at 271.

70. *Gilbertson*, 433 F. Supp. at 411. A third related rule states that one nation will not enforce the penal laws of another. *See* Huntington v. Attrill, 146 U.S. 657, 665 (1892). One early justification for the revenue rule was that tax laws were akin to penal laws, and therefore unenforceable. *See, e.g.*, Oklahoma v. Gulf, Colo. & Santa Fe Ry., 220 U.S. 290, 299 (1911). The U.S. Supreme Court disaggregated penal laws from revenue laws by holding that taxes are not considered penal. *Milwaukee County*, 296 U.S. at 271.

The first federal court case to apply the domestic revenue rule was *Moore v. Mitchell*.[71] In *Moore*, Judge Learned Hand stated that it might be embarrassing for the courts of one state to examine the tax laws of a foreign state, because tax laws, like penal laws, are "provisions for the public order" of another state, and traditionally tax laws were viewed as a reflection of society's morals.[72] He reasoned that the state courts should not entertain suits under sister state tax laws because courts are not in a position to scrutinize other states' public policy, and should not interfere with interstate or foreign relations.[73] Although *Moore* dealt with the domestic revenue rule, courts have recognized that the reasoning also applies internationally.[74]

B. International Revenue Rule

The U.S. Supreme Court has taken only a passing notice of the international revenue rule. The case law and scholarly interpretations of the revenue rule display a pattern of decline through the middle of the 20th century, with a resurgence after 1979.[75] After this revival, the rule was extended to apply to causes of action based on U.S. statutes, with varying results.[76]

1. Federal Court Interpretations

In *Banco Nacional de Cuba v. Sabbatino*,[77] Justice White noted in a dissenting opinion that "courts customarily refuse to enforce the revenue

71. 30 F.2d 600 (2d Cir. 1929), *aff'd on other grounds*, 281 U.S. 18 (1930).

72. *Id.* at 604. (Hand, J., concurring).

73. *Id.*

74. *See Milwaukee County*, 296 U.S. at 271–73. The U.S. Supreme Court eliminated the domestic revenue rule's application to sister state tax judgments based on the Constitutional Full Faith and Credit Clause. *Id.* U.S. Const. art. IV, § 1. Soon thereafter, numerous state courts and legislatures determined that sister state tax *claims* would also be entertained, even without constitutional mandate. *See* Buckley v. Huston, 291 A.2d 129, 131 (N.J. 1972) (collecting cases); State ex rel. Okla. Tax Comm'n v. Rodgers, 193 S.W.2d 919, 927 (Mo. Ct. App. 1946). Many other states opted to enact statutes providing for reciprocal enforcement of tax claims. *See, e.g.*, CONN. GEN. STAT. § 12-35c (2000); IDAHO CODE § 63-1403 (2000); WASH. REV. CODE § 4.24.141 (2000).

75. *See infra* notes 77–102 and accompanying text.

76. *See generally* Reynolds II, 268 F.3d 103 (2d Cir. 2001); Republic of Ecuador v. Philip Morris, 188 F. Supp. 2d 1359 (S.D. Fla. 2002); European Community v. Japan Tobacco, Inc., 186 F. Supp. 2d 231 (E.D.N.Y. 2002); European Community v. RJR Nabisco, Inc., 150 F. Supp. 2d 456, 460 (E.D.N.Y. 2001).

77. 376 U.S. 398 (1964).

and penal laws of a foreign state, because no country has an obligation to further the governmental interests of a foreign sovereign."[78] However, the U.S. Supreme Court has never applied the revenue rule.

In 1979, almost a decade after Congress enacted RICO, the Ninth Circuit became the first American court to directly apply the international revenue rule in *Her Majesty the Queen in Right of the Province of British Columbia v. Gilbertson.*[79] In that case, British Columbia sought to enforce a Canadian income tax judgment obtained against the defendants, citizens of Oregon, for logging work performed in Canada.[80] The *Gilbertson* court applied the revenue rule to bar British Columbia's claim. The court characterized the international revenue rule as "well recognized"—in fact, so well recognized that it had never been challenged in a U.S. court.[81] Still, the *Gilbertson* court acknowledged that the rule may have only been dicta in the 18th century English cases that originally announced it.[82] Consequently the Ninth Circuit turned to the reasoning of *Moore*,[83] even though the *Moore* court had analyzed the domestic revenue rule.[84] The *Gilbertson* court held that the revenue rule was appropriate because to scrutinize foreign tax judgments might interfere with international relations by embarrassing a foreign government.[85]

The 1979 *Gilbertson* case marked a turning point for the revenue rule. Before *Gilbertson*, the U.S. Supreme Court had disavowed the rule in respect to sister state tax judgments,[86] state courts and legislatures had largely rejected the revenue rule with respect to sister state tax claims,[87] and federal courts had never applied the international revenue rule.[88]

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78. *Id.* at 448 (White, J., dissenting on other grounds).

79. 433 F. Supp. 410 (D. Or. 1977), *aff'd*, 597 F.2d 1161 (9th Cir. 1979).

80. *Gilbertson*, 597 F.2d at 1162. The judgment was actually a certificate of tax assessment against the defendants. In Canada, the certificate had the same effect as a judgment. *Id.*

81. *Id.* at 1164. The district court in *Gilbertson* coined the term revenue rule. *Reynolds I*, 103 F. Supp. 2d 134, 139 (N.D.N.Y. 2000).

82. *Gilbertson*, 597 F.2d at 1164.

83. *Id.* at 1164, (quoting *Moore*, 30 F.2d 600 (2d Cir. 1929)). *See supra* notes 71–74 and accompanying text.

84. *Gilbertson*, 597 F.2d at 1164.

85. *Id.*

86. *See* Milwaukee County v. M.E. White Co., 296 U.S. 268, 271 (1935).

87. *See* Buckley v. Huston, 291 A.2d 129, 131 (N.J. 1972).

88. *Gilbertson*, 597 F.2d at 1164.

However, in 1979, the Ninth Circuit's opinion in *Gilbertson* revived the revenue rule.[89]

2. *Scholarly Criticisms of the Revenue Rule*

The revenue rule has been the subject of scholarly criticism for more than 150 years,[90] but the rule was increasingly criticized in the middle of the 20th century.[91] The abolition of the domestic revenue rule for sister state judgments enhanced the skepticism of the revenue rule.[92] In addition, many states began to enforce the tax claims of sister states, based on a belief that the revenue rule was outdated and not justified.[93] Some commentators argued that tax laws should be enforced, but only tax penalties, such as fines, should be denied enforcement under the penal rule.[94] Just two years before *Gilbertson* was decided, Robert A. Leflar, a leading theorist on American conflicts law, wrote that the domestic revenue rule was "senseless[]", and that "the old [revenue] rule will eventually be changed by all the states, either through legislation or by judicial reexamination."[95]

Scholarly legal opinion seems to have remained generally adverse to the revenue rule until at least a decade after the enactment of RICO, when the Ninth Circuit revived the doctrine in *Gilbertson*.[96] The criticism

89. *Id.* at 1166.

90. *See* Reynolds II, 268 F.3d 103, 124 (2d Cir. 2001). ("In academic literature, there is a long history of criticism of the revenue rule as creating improper incentives for moral and commercial conduct.") (collecting cases and secondary sources). *See, e.g.*, JAMES KENT, 3 COMMENTARIES ON AMERICAN LAW 335–36 (8th ed. 1854) (stating that rule is "unsound and immoral"); *The Anne*, 1 F. Cas. 955, 956, 1 Mason 508, No. 412 (C.C.D. Mass. 1818).

91. *See, e.g., Milwaukee County*, 296 U.S. at 268; Banco Frances e Brasileiro S. A. v. Doe, 331 N.E.2d 502, 505–06 (N.Y. 1975); State *ex rel.* Okla. Tax Comm'n v. Neely, 282 S.W.2d 150, 151 (Ark. 1955); *but see* City of Philadelphia v. Cohen, 184 N.E.2d 167, 169 (N.Y. 1962). *See generally* Arthur T. von Mehren & Donald T. Trautman, *Recognition of Foreign Adjudications: A Survey and Suggested Approach*, 81 HARV. L. REV. 1601 (1968); Eugene F. Scoles, *Interstate and International Distinctions in Conflict of Laws in the United States*, 54 CAL. L. REV. 1599, 1607–08 (1966); Albert A. Ehrenzweig, CONFLICT OF LAWS § 49, at 174 (1962); Robert A. Leflar, *Extrastate Enforcement of Penal and Governmental Claims*, 46 HARV. L. REV. 193 (1932).

92. Much of the academic criticism of the domestic rule also applies to the international rule because the underlying principles are the same. *See supra* note 74.

93. *See* State *ex rel.* Okla. Tax Comm'n v. Rodgers, 193 S.W.2d 919, 927 (Mo. Ct. App. 1946); HERBERT F. GOODRICH & EUGENE F. SCOLES, HANDBOOK OF THE CONFLICT OF LAWS 99–100 (4th ed. 1964).

94. EDWARD S. STIMSON, CONFLICT OF LAWS 441–42 (1963).

95. ROBERT A. LEFLAR, AMERICAN CONFLICTS LAW § 49 (3d ed. 1977).

96. 433 F. Supp. 410 (1977), *aff'd*, 597 F.2d 1161 (9th Cir. 1979).

subsided following *Gilbertson*, but many scholars still advocated the abolition of the revenue rule.[97] For example, in 1970, one commentator wrote: "Most cases usually relied upon as authorities [for the penal and revenue rules] are more than half a century old and the lawyer's prospect of avoiding the application of foreign law on this ground is minimal."[98] Additionally, the Restatement (Third) of Foreign Relations Law of the United States, notes that "the rationale for not recognizing or enforcing tax judgments is largely obsolete."[99] Recently, a few courts have also had reservations about the validity of the revenue rule.[100]

Since the *Gilbertson* court's revival of the revenue rule, courts have been faced with questions of whether to apply the revenue rule when the foreign state's claim is based on a federal statute.[101] It is against this sparse common law backdrop that modern courts must define the revenue rule's relationship to American statutes.

C. *Modern Applications of the Revenue Rule to Statutory Claims*

In recent years, several courts have addressed the revenue rule in cases where a U.S. statute rather than a foreign revenue law created the cause of action.[102] In *United States v. Boots*,[103] the First Circuit held that the rule barred criminal prosecution under the federal wire fraud statute[104] where the defendant attempted to defraud a foreign government of

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97. *See, e.g.*, Barbara A. Silver, *Modernizing the Revenue Rule: The Enforcement of Foreign Tax Judgments*, 22 GA. J. INT'L & COMP. L. 609, 613 (1992); Richard E. Smith, Note, *The Nonrecognition of Foreign Tax Judgments: International Tax Evasion*, 1981 U. ILL. L. REV. 241, 263–67 (1981).

98. ALBERT A. EHRENZWEIG, CONFLICTS IN A NUTSHELL 78 (2d ed. 1970).

99. RESTATEMENT, *supra* note 5, Reporter's Note 2 .

100. *See, e.g.*, Reynolds I, 103 F. Supp. 2d 134, 140, n.3 (N.D.N.Y. 2000) ("Were the Court writing on a clean slate . . . it would be inclined to find the Revenue Rule to be outdated (to the extent it was ever properly recognized by courts in the United States in the first instance) and the rationales for the rule to be largely unpersuasive, at least with respect to the recognition of foreign tax judgments."); *see also* United States v. Trapilo, 130 F.3d 547, 550 n.4 (2d Cir. 1997).

101. *See generally* United States v. Boots, 80 F.3d 580 (1st Cir. 1996); *Trapilo*, 130 F.3d at 547; European Community v. RJR Nabisco, Inc., 150 F. Supp. 2d 456, 472 (E.D.N.Y. 2001); Reynolds II, 268 F.3d 103, 106 (2d Cir. 2001). *Cf.* United States v. Pierce, 224 F.3d 158 (2d Cir. 2000).

102. *See generally Boots*, 80 F.3d at 580–87; *Trapilo*, 130 F.3d at 549; *European Community*, 150 F. Supp. 2d at 472; *Reynolds II*, 268 F.3d at 106. *Cf.* United States v. Pierce, 224 F.3d 158 (2d Cir. 2000).

103. 80 F.3d 580.

104. 18 U.S.C. § 1343 (1994).

taxes.[105] The *Boots* defendants had allegedly conspired to smuggle tobacco into Canada.[106] The First Circuit reasoned that prosecution would "functionally" enforce a foreign tax law because the "sole object" of the defendants' scheme was to deprive Canada of revenues.[107] Furthermore, proof of fraud would require the trial court to evaluate Canada's tax laws and rule on defendants' challenges to their validity.[108] Such a ruling could implicate U.S. foreign policy.[109] Although the *Boots* case would probably not interfere with foreign policy and did not call for direct enforcement of a foreign tax judgment, the court refused to apply the revenue rule on a case-by-case basis.[110] The *Boots* court instead held that even the possibility of interfering with foreign relations mandated dismissal.[111] Thus, in the First Circuit, the revenue rule mandates dismissal whenever evaluation of a foreign revenue law is necessary.

In *United States v. Trapilo*[112] and the related case *United States v. Pierce*,[113] the Second Circuit expressly rejected the reasoning of *Boots*.[114] In *Trapilo*, the defendants had allegedly smuggled liquor across a Native American reservation to avoid paying Canadian taxes.[115] The *Trapilo* court found that the scheme to defraud Canada of tax revenues was cognizable under the wire fraud statute.[116] According to the statute, the prosecution needed only to show that the defendants "devised or intend[ed] to devise any scheme or artifice to defraud."[117] Thus, a wire fraud conviction could result regardless of the scheme's actual success.[118] Consequently, the Second Circuit had no occasion to pass on the validity

105. *Boots*, 80 F.3d at 586–87.
106. *Id.* at 583.
107. *Id.* at 587.
108. *Id.*
109. *Id.*
110. *Id.* at 588.
111. *Id.*
112. 130 F.3d 547 (2d Cir. 1997).
113. 224 F.3d 158 (2d Cir. 2000).
114. *Trapilo*, 130 F.3d at 549, *Pierce*, 224 F.3d at 167.
115. *Trapilo*, 130 F.3d at 549.
116. 18 U.S.C. § 1343 (1994); *see also Trapilo*, 130 F.3d at 551.
117. *Trapilo*, 130 F.3d at 549.
118. *Id.* at 552.

of Canadian laws, as long as the prosecutors could show that the defendants intended to use the wires to defraud Canada of taxes.[119]

The *Trapilo* court held that the revenue rule did not mandate dismissal every time a foreign revenue law was implicated.[120] Instead, the revenue rule should be applied only in cases that would interfere with the separation of powers.[121] For example, the claim might be barred if the court would otherwise have to decide a foreign relations question more properly reserved to the political branches.[122] However, the separation of powers principle was not disturbed in *Trapilo* because the court was implementing Congress' purpose by applying the federal wire fraud statute.[123]

Similarly, in *Pierce*, the Second Circuit held that evidence of a foreign revenue law was necessary for a conviction under the wire fraud statute where the victim was a foreign government and the injury was lost tax revenues.[124] A necessary element of the wire fraud statute was a scheme to defraud, which depends on the existence of a property interest.[125] To show the Canadian property interest in taxes, the government needed to prove that Canada actually imposed taxes on alcohol transported across the border.[126] The government failed to introduce any evidence of the Canadian taxes[127] and the conviction could not be upheld.[128] In sum, the *Trapilo* court held that the revenue rule does not bar prosecution of a scheme to defraud the Canadian government of tax revenues, and the

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119. *Id.* "At the heart of this indictment is the misuse of the wires in furtherance of a scheme to defraud the Canadian government of tax revenue, not the validity of a foreign sovereign's revenue laws." *Id.*

120. *Id.* at 553.

121. *Id.* The separation of powers principle is a political framework in which the government is divided into three branches, each of which exercises a distinct type of authority. The separation of powers is not absolute. A system of checks and balances creates some overlap—for example, the executive veto—that restrains the power of each branch. *See* United States v. Nixon, 418 U.S. 683, 707 (1974); The Federalist No. 47 (James Madison).

122. *Trapilo*, 130 F.3d at 553. *See* United States v. Curtiss-Wright Export Corp., 299 U.S. 304, 320 (1936) (holding that the executive branch exercises primary control over foreign affairs.)

123. *Trapilo*, 130 F.3d at 553.

124. *United States v. Pierce*, 224 F.3d 158, 160 (2d Cir. 2000). Following *Trapilo*, all of the defendants except Regina and Lyle Pierce entered into plea arrangements. Subsequently, the Pierces were convicted and sentenced. *Pierce* is the appeal of that conviction. *Id.* at 164.

125. *Id.* at 165.

126. *Id.* at 166.

127. *Id.* at 167.

128. *Id.* at 164.

revenue rule only operates where there are significant separation of powers concerns.[129] The *Pierce* court added that in order to sustain a conviction, the government must introduce evidence of each element of the wire fraud statute, including evidence that Canada imposed taxes and as a result held a property interest.[130]

Although the Second Circuit in *Pierce* did not discuss the revenue rule, one can assume that if the prosecution had introduced evidence of the Canadian taxes to prove that a property right existed, the defendants would also have had the opportunity to introduce contrary evidence that the tax laws were either invalid or nonexistent. In fact, because the sentencing under the money laundering statute varies according to the amount of money involved, the court would need to first establish that the Canadian laws were valid and in force and then determine the degree to which the defendants actually violated the foreign law.[131] Notwithstanding this possible evaluation of foreign tax laws, the *Pierce* court allowed the case to proceed, choosing to wait and see if separation of powers concerns arose instead of applying the revenue rule to dismiss the case.[132] Although the question was not resolved in *Pierce*, it is possible that the court's application of foreign revenue laws would have violated neither the separation of powers nor the revenue rule. Overall, Second Circuit precedent has established that it is within a court's discretion to determine whether separation of powers problems may arise, and to allow a case to proceed when interference with foreign affairs is not imminent.

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129. United States v. Trapilo, 130 F.3d 547, 553 (2d Cir. 1997).

130. *Pierce*, 224 F.3d at 167.

131. *See* Reynolds II, 268 F.3d 103, 138 (2d Cir. 2001) (Calabresi, J., dissenting); United States v. Chmielewski, 218 F.3d 840, 843 (8th Cir. 2000) ("It is no intrusion [into foreign jurisdictions and jurisprudences] to gauge the severity of [the defendant's] domestic crime by measuring the damage done to his extraterritorial victims. In doing so, we consider a foreign loss not to uphold a foreign law, but to uphold our own law . . . which directs us to consider the loss caused by fraud as a measure of a just punishment.").

132. The *Trapilo* court "assumed . . . that the government would prove at trial . . . that the defendants conspired to 'participate in an illegal venture to smuggle liquor from the United States into Canada where it would be sold on the 'black market' *to avoid the payment of Canadian taxes and duties*.'" *Pierce*, 224 F.3d at 167, (quoting *Trapilo*, 130 F.3d at 552) (emphasis added by the *Pierce* court). By extension, the *Trapilo* court probably would have assumed that the trial court would have determined that the Canadian taxes were valid and that the defendants had violated them.

Finally, in *European Community v. RJR Nabisco, Inc.*,[133] a U.S. district court in the Eastern District of New York held that the revenue rule did not bar a suit by a foreign sovereign to recover civil RICO damages for lost tax revenues.[134] The European Community brought a civil RICO suit against various tobacco companies and related entities for smuggling tobacco from the United States into Europe to evade European taxes.[135] The court thoroughly analyzed the origin of the revenue rule and concluded that the rule had been called into serious doubt. Furthermore, to the extent that the rule existed at all, its application was discretionary.[136] The *European Community* court cited *Trapilo* and *Pierce* for the proposition that the revenue rule should apply only when the case would encroach upon the foreign relations powers of the political branches.[137] The revenue rule was not applicable to a suit based on civil RICO, because the separation of powers was not implicated.[138] RICO, an American law, provided the rule of decision in the case and foreign law need only be applied in the calculation of damages.[139] In addition, the suit actually promoted the United States' interest in enforcing RICO in eliminating racketeering activity.[140] The *European Community* court rejected the argument that the existence of tax treaties with Canada precluded Canada's civil suit, noting that the enforcement of a statute to combat racketeering activity did not conflict with the U.S. tax treaties because the RICO claim is not simply an alternative tax enforcement mechanism.[141] The district court also rejected the argument that American courts might not have the ability to interpret foreign revenue laws, noting that American courts frequently interpret

133. 150 F. Supp. 2d 456 (E.D.N.Y. 2001). The court eventually held that the European Community (EC) was unable to demonstrate injury separate from that of the member states, and the claim was dismissed. The EC failed to allege the injury needed to bring suit under RICO. Because the EC's budget is a set amount, the loss of revenues to member states did not similarly affect the revenues of the EC. *Id.* at 501–02.

134. *Id.* at 483–84.

135. *Id.* at 462–71 (detailing the complex facts of the smuggling scheme)..

136. *Id.* at 483. *See also* RESTATEMENT, *supra* note 5; Silver, *supra* note 97 at 611–12.

137. *European Cmy.*, 150 F. Supp. 2d at 483.

138. *Id.* at 484.

139. *Id.* at 483–84.

140. *Id.*

141. *Id.* ("[A]djudication of this case in no way involves the judiciary in second-guessing the adequacy, legitimacy, or propriety of any action taken or judgment made by Congress or the Executive Branch with respect to the ability of foreign sovereigns to enforce their tax laws.").

and apply other types of foreign laws.[142] Therefore, even though courts have struggled with the application of the revenue rule to federal statutory claims, until *Reynolds II*, courts in the Second Circuit chose not to apply the revenue rule to block cases based on U.S. federal statutes, primarily because there were no separation of powers problems presented.[143]

IV. *ATTORNEY GENERAL OF CANADA V. R.J. REYNOLDS*

A. *Facts and Procedural History*

The case of *Attorney General of Canada v. R.J. Reynolds* [hereinafter *Reynolds I*] emerged from an alleged scheme, facilitated by R.J. Reynolds Tobacco Holdings, Inc. (R.J. Reynolds) and other defendants,[144] to smuggle tobacco into Canada to avoid increased Canadian tobacco taxes.[145] In 1991, the Canadian government doubled its cigarette taxes, increasing the average price per carton from $26 to $48.[146] Soon thereafter, R.J. Reynolds and the other defendants allegedly developed a smuggling operation to avoid paying the increased taxes.[147] The defendants purportedly exported cigarettes out of Canada, falsely declaring that they were not for consumption in Canada, and sold them to known smugglers who then covertly transported the cigarettes back into Canada for sale on the black market.[148] Over time, the scheme evolved.[149]

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142. *Id.* at 484, n.16.

143. *See* United States v. Trapilo, 130 F.3d 547, 552 (2d Cir. 1997); *European Community*, 150 F. Supp. 2d at 483–84.

144. American companies R.J. Reynolds Tobacco Holdings, Inc. (Holdings), Northern Brands International, Inc. (NBI), R.J. Reynolds Tobacco Company (RJR US), R.J. Reynolds Tobacco International, Inc. (International), and R.J. Reynolds Tobacco Company Puerto Rico (RJR PR), and RJR-MacDonald (RJR MacDonald), a Canadian company, and Canadian Tobacco Manufacturers Council (CTMC), [hereinafter defendants].

145. *See* Reynolds II, 268 F.3d 103, 105–10 (2d Cir. 2001).

146. *Id.* at 106.

147. Plaintiff's Complaint for Damages and Injunctive and Declaratory Relief at 5–9, Reynolds I, 103 F. Supp. 2d 134 (N.D.N.Y. 2000) (No. 99-CV-2194) [hereinafter Plaintiff's Complaint]. The scheme was developed first by RJR MacDonald, and later expanded to involve other defendants. RJR Macdonald is a subsidiary of RJR Nabisco, now called RJR Holdings, as is RJR International. The subsidiaries of RJR Holdings are alleged to have participated in the smuggling scheme individually and through their agents, alter egos, subsidiaries, division or parent companies. The Canadian Tobacco Manufacturers Council is named as an agent of RJR Macdonald. *Id.*

148. *Reynolds II*, 268 F.3d at 106.

The defendants began to export Canadian cigarettes from Canada through the Foreign Trade Zones in New York, where they were shipped to a Native American reservation and then smuggled back into Canada.[150] Perhaps in response, Canada imposed a $6 per carton excise tax on cigarettes.[151] Around that time, the defendants began to produce cigarettes in Puerto Rico that were made to resemble Canadian RJR-MacDonald cigarettes.[152] These cigarettes were then smuggled into Canada.[153] The defendants then created Northern Brands International (NBI), allegedly to insulate RJR MacDonald from selling directly to smugglers and to conceal the smuggling scheme.[154] The defendants made several hundred million dollars in profit from the increased Canadian sales.[155] In 1994, Canada lowered its cigarette taxes, but the defendants allegedly continued the smuggling until 1998.[156] In 1997 and 1998, NBI and 21 individuals were indicted in connection with the smuggling operation.[157]

The Attorney General of Canada (Canada) filed a civil RICO[158] complaint in a federal district court in the Northern District of New York.[159] Canada's complaint alleged that the defendants violated and conspired to violate RICO by using a corporation to conduct a pattern of racketeering activity including continuous instances of mail and wire fraud.[160] Canada alleged that the defendants' RICO violations were the proximate cause of injury to its property in the form of lost tax revenues, increased law enforcement costs, and revenue lost when Canada repealed tax laws, allegedly in reaction to the defendants' conduct.[161] Canada requested actual damages based on those costs, treble damages, and reasonable attorney's fees.[162]

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149. *Id.*

150. *Id.*

151. *See* Plaintiff's Complaint at 14–15.

152. *Reynolds II*, 268 F.3d at 107.

153. *See* Plaintiff's Complaint at 32–33.

154. *See id.* at 27–29.

155. *Reynolds II*, 268 F.3d at 107.

156. Plaintiff's Complaint at 36–39.

157. *See* United States v. Miller, 26 F. Supp. 2d 415, 419 (N.D.N.Y. 1998).

158. 18 U.S.C. § 1964(c) (1994).

159. Reynolds I, 103 F. Supp. 2d 134, 138 (N.D.N.Y. 2000).

160. *Reynolds II*, 268 F.3d at 107–08.

161. *Id.* at 108.

162. *Id.* at 107–08 (detailing Canada's alternative claims).

The defendants moved to dismiss,[163] arguing that the suit was no more than an attempt to enforce Canadian revenue laws.[164] The district court dismissed the case, holding that Canada's claim for damages based on taxes was indeed barred by the revenue rule.[165] In particular, the district court held that Canada could not meet RICO's injury requirement, because to do so would require an evaluation of Canadian revenue laws.[166] Canada appealed.[167]

B. The Second Circuit's Majority Opinion

The Second Circuit affirmed the district court decision in *Reynolds II*, holding that Canada's RICO claim was essentially one for lost taxes, barred by the revenue rule.[168] The court reasoned that RICO did not abrogate the common law revenue rule.[169] Instead, the court noted, the revenue rule was well established and applicable to any direct or indirect enforcement of tax laws.[170] In addition, the majority reviewed the U.S./Canada tax treaty framework and found that the policy of the executive branch was to limit foreign tax collection assistance.[171] Therefore, to offer tax collection assistance to Canada might violate the separation of powers principle by interfering with the executive's foreign policy authority.[172] Thus, the Second Circuit affirmed dismissal of the suit.[173]

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163. *Id.* at 108 (explaining that the defendants moved to dismiss pursuant to Fed. R. Civ. P. 12(b)(6)). *See also Reynolds I*, 103 F. Supp. 2d at 139 (listing alternative bases for dismissal).

164. *Reynolds I*, 103 F. Supp. 2d at 139.

165. *Reynolds I*, 103 F. Supp. 2d at 143. The district court also held that RICO does not provide the equitable relief Canada requested and that claims for increased law enforcement costs are not allowed. Canada appealed all three holdings but the Second Circuit disposed of the case based on the revenue rule. *Reynolds II*, 268 F.3d at 109.

166. *Reynolds I*, 103 F. Supp. 2d at 143–44.

167. *Id.*

168. *Reynolds II*, 268 F.3d at 130–31.

169. *Id.* at 106.

170. *Id.* at 130–31, 134.

171. *Id.* at 124.

172. *Id.* at 114.

173. *Id.* at 109.

1. Direct and Indirect Enforcement of Revenue Laws

The majority held that the revenue rule mandated dismissal because this case involved an action by Canada to enforce its tax laws "directly and indirectly," notwithstanding the claim's origin under RICO.[174] According to the *Reynolds II* court, it is the substance of the action, not the form, that counts.[175] The majority, relying on foreign case law,[176] held that the fact that the claim was based on a U.S. statute was immaterial because the claim's ultimate effect would be to reimburse Canada for lost taxes.[177] In the Canadian case *United States v. Harden*,[178] the United States government sought to enforce a tax settlement agreement in Canada.[179] The Canadian Supreme Court held that the "whole object" of that case was the collection of U.S. taxes, making its remedy a direct enforcement of tax laws.[180] The *Reynolds II* court also cited an Irish High Court case for the proposition that even indirect enforcement of a foreign revenue law mandates dismissal of the case.[181] The *Reynolds II* court elevated the substance of the remedy being sought over the form of the action and found that the RICO claim for treble damages would amount to a direct enforcement of Canadian tax laws.[182]

2. Statutory Abrogation of the Revenue Rule

The *Reynolds II* majority held that RICO did not abrogate the revenue rule because the rule was "well established" when RICO was enacted and Congress did not express an intent to abolish the common law rule.[183] The Second Circuit cited principles of statutory construction requiring a court to construe a statute to preserve the common law,

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174. *Id.* at 130–31.

175. *Id.* at 130.

176. United States v. Harden [1963] S.C.R. 366, 371 (Can.).

177. *Reynolds II*, 268 F.3d 103 at 130–31 (quoting Peter Buchanan Ltd. v. McVey, [1954] I.R.89, 102–03 (Ire.)).

178. [1963] S.C.R. at 371.

179. *Harden*, [1963] S.C.R. at 371.

180. *Id.* at 372–73.

181. *Reynolds II*, 268 F.3d at 130 (citing *Peter Buchanan Ltd.*, [1954] I.R. at 102).

182. *Reynolds II*, 268 F.3d at 131 (dismissing Canada's claims for increased law enforcement costs as an indirect enforcement of the revenue laws of Canada).

183. *Id.* at 126.

absent clear evidence of congressional intent to the contrary.[184] Because the court found that the revenue rule was in existence long before Congress enacted RICO,[185] and Congress did not explicitly mention the revenue rule in RICO's legislative history,[186] the Second Circuit held the statute did not abrogate the common law rule.[187]

In support of its conclusion that the revenue rule was well established in 1970, the Second Circuit cited several United States cases[188] and asserted that while neither the United States Supreme Court nor the Second Circuit had yet defined the scope of the rule, each had acknowledged its existence.[189] The *Reynolds II* court also cited a few foreign revenue rule cases.[190] The Second Circuit conceded that the rule had been severely criticized, but asserted that the legislature, not the courts, should change the common law revenue rule.[191]

3. *The Role of Separation of Powers*

The *Reynolds II* majority explained that the justifications for the revenue rule include respect for the sovereignty of foreign nations[192] and avoidance of extraterritorial application of foreign law.[193] Because revenue laws often reflect a state's public policy, forum state judicial scrutiny of those laws could potentially embarrass a foreign state.[194] In addition, the court reasoned that the laws of one sovereign state should not have effect within the borders of another, and no nation has the obligation to further the sovereign interests of another.[195] The court conceded that "concerns about sovereignty and extraterritorially are . . . not absolute, and are not implicated in every case involving foreign tax laws."[196] However, the Canadian revenue laws at issue were

184. *Id.* at 129.
185. *Id.* at 126.
186. *Id.* at 129.
187. *Id.*
188. *Id.* at 111–12.
189. *Id.* at 108.
190. *Id.* at 111 n.5.
191. *Id.* at 124–25.
192. *Id.* at 111–12.
193. *Id.* at 114.
194. *Id.* at 112.
195. *Id.*
196. *Id.* at 113.

the product of a social policy to combat smoking.[197] Therefore, the claim implicated the rationale underlying the revenue rule because the Canadian revenue laws were the product of Canada's sovereignty.[198]

The *Reynolds II* majority also reasoned that the Canadian claim could potentially impact U.S. foreign policy.[199] The Second Circuit distinguished the case at issue from a criminal prosecution, in which the executive branch of the United States government would ultimately oversee prosecutorial discretion.[200] Executive oversight is absent in a civil case.[201] The majority agreed with the First Circuit's opinion in *United States v. Boots*,[202] which held that cases involving the application of foreign tax laws encroach on foreign relations and courts should refrain from hearing them.[203] The *Reynolds II* court thus adopted *Boots* in the civil setting, while noting that Second Circuit precedent had rejected *Boots* in the criminal law setting.[204] The *Reynolds II* court concluded that the case was properly dismissed because it could conflict with U.S. foreign policy.[205]

The *Reynolds II* court relied heavily on U.S. tax treaties.[206] The lack of general enforcement provisions in the treaties provided evidence that the political branches intended to "to define and limit" foreign tax enforcement assistance.[207] The court reasoned that the treaties implied an intent to keep the revenue rule intact.[208] The Second Circuit reasoned that the executive should negotiate treaties to determine whether U.S. courts should enforce foreign tax laws, but U.S. courts should not hear claims for direct or indirect enforcement of foreign taxes.[209]

In sum, the *Reynolds II* majority held that allowing a foreign sovereign to directly or indirectly enforce its tax laws in U.S. courts

197. *Id.*

198. *Id.*

199. *Id.* at 123.

200. *Id.*

201. *Id.*

202. 80 F.3d 580 (1st Cir. 1996).

203. *Id.* at 587–88; *see also supra* notes 103–11 and accompanying text.

204. *Reynolds II*, 268 F.3d at 123; *see also supra* notes 112–24 and accompanying text.

205. *Reynolds II*, 268 F.3d at 122.

206. *Id.* at 115–22.

207. *Id.* at 115.

208. *Id.*

209. *Id.* at 130.

could potentially implicate U.S. foreign relations.[210] The court decided that Canada's RICO claim was an impermissible attempt to enforce its tax laws.[211] The court affirmed the dismissal because tax laws are an aspect of sovereignty and the U.S. treaty framework evinces an intent to restrict enforcement of foreign tax laws.[212]

C. *The* Reynolds II *Dissent*

Judge Calabresi dissented, reasoning that Canada's suit should be allowed to proceed and the revenue rule should not bar the RICO claim.[213] The dissent argued that the claim did not involve the enforcement of a Canadian tax judgment or claim.[214] Instead, the dissent characterized the suit as a United States cause of action created by Congress to remedy injuries caused by racketeering activities.[215] According to the dissent, the Canadian tax laws would be involved only in the calculation of damages.[216]

Judge Calabresi first summarized the majority's arguments for applying the revenue rule. First, courts should not promote extraterritorial effect of foreign laws.[217] Second, foreign policy implications of the claim give rise to potential separation of powers problems.[218] Third, the judiciary has a limited ability to interpret foreign laws.[219] The dissent then repudiated each of those justifications.[220]

According to the dissent, even though the claim might promote Canadian interests, it primarily involved enforcement of RICO.[221] While the United States has no obligation to further Canada's sovereign interests,[222] Judge Calabresi asserted that the suit would promote

210. *Id.* at 123.
211. *Id.* at 130–131.
212. *Id.* at 115.
213. *Id.* at 135. (Calabresi, J., dissenting).
214. *Id.*
215. *Id.*
216. *Id.*
217. *Id.* at 136.
218. *Id.* at 136–37.
219. *Id.* at 137–38.
220. *Id.* at 136–39.
221. *Id.* at 136.
222. *See* Banco Nacional de Cuba v. Sabbatino, 376 U.S. 398, 448 (1964) (White, J., dissenting).

American interests by discouraging racketeering activity.[223] Given this primary goal, for the dissent the incidental protection of Canadian interests in pursuing that goal would be permissible.[224]

Judge Calabresi also argued that the separation of powers doctrine would not be violated by this claim.[225] According to the dissent, the political branches created the RICO cause of action.[226] For the dissent, adjudicating Canada's RICO suit would amount to an implementation of Congress' policy to eliminate organized crime.[227] Therefore, the dissent reasoned, refusing to hear the case would actually hinder the Congressional objective underlying RICO.[228]

Judge Calabresi recognized that the most relevant justification for the revenue rule was that U.S. courts may not have the capacity to interpret complex foreign tax laws because they may differ greatly from U.S. law.[229] However, the dissent found this argument unpersuasive because the Second Circuit had already rejected it in *Pierce*.[230] The *Pierce* court held that the prosecution must introduce evidence of foreign tax laws to show that the defendants intended to defraud Canada of a property interest.[231] Further, a court must determine the extent to which those laws were violated to apply the sentencing guidelines.[232] Thus, the dissent reasoned, *Pierce* required a three-step determination: first, did the defendant violate the wire fraud statute;[233] second, to what extent did the defendant cause injury by violating the Canadian laws;[234] and third, what sentence should be imposed given that amount of injury.[235] This inquiry was acceptable to the Second Circuit in *Pierce*.[236] In *Reynolds II*, there would be a parallel three step analysis:[237] first, did the defendant violate

223. *Reynolds II*, 268 F.3d at 136 (Calabresi, J., dissenting).

224. *Id.*

225. *Id.* at 137.

226. *Id.*

227. *Id.*

228. *Id.*

229. *Id.*

230. 224 F.3d 158, 167 (2d Cir. 2000).

231. *Id.* at 165. *See also supra* note 124-32 and accompanying text.

232. *Reynolds II*, 268 F.3d at 138 (Calabresi, J., dissenting).

233. *Id.*

234. *Id.*

235. *Id.*

236. *Id.*

237. *Id.*

RICO;[238] second, to what extent did the defendant cause damage by violating the Canadian laws;[239] and third, what amount of civil damages should be imposed given the amount of injury.[240] Because the interpretation of foreign law is involved only in the second step, and that step would be identical in each case, *Pierce* should control and the case should be allowed to proceed.[241] Thus, the dissent rejected the argument that the court would be incapable of interpreting foreign tax laws to measure damages.[242]

Therefore, the relevance of the revenue rule to a civil RICO claim presented a difficult question. The *Reynolds II* majority held that Canada's claim would directly and indirectly enforce Canadian tax laws and hearing the case would violate the separation of powers principle.[243] In contrast, the dissent argued that the claim would further Congress' goals under RICO and indeed would not interfere with U.S. foreign policy.[244]

V. *REYNOLDS II* WAS WRONGLY DECIDED

The revenue rule should not bar Canada's civil claim under RICO, because according to Second Circuit precedent,[245] the revenue rule does not apply unless separation of powers problems arise.[246] Canada's civil RICO suit is actually in accord with the policy of the political branches of the United States. Congress has provided Canada with a cause of action under RICO, and that is the foreign policy pronouncement that is relevant to this suit. The fact that Canadian revenue laws will be used to calculate damages does not automatically destroy Canada's claim, because the revenue rule does not mandate abstaining from jurisdiction solely because proof of a foreign revenue law is necessary.[247]

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238. *Id.*

239. *Id.*

240. *Id.*

241. *Id.* at 138–39.

242. *Id.* at 138.

243. *Id.* at 130–131.

244. *Id.* at 136 (Calabresi, J., dissenting).

245. *See* United States v. Trapilo, 130 F.3d 547, 553 (2d Cir. 1997).

246. *See supra* note 137 and accompanying text.

247. *See supra* notes 120–23 and accompanying text.

Moreover, the liberal construction demanded by the statute means that the common law revenue rule cannot be expanded to apply to a RICO claim. A RICO cause of action is different from a tax claim, and the use of the revenue rule to bar a federal statutory cause of action is a novel expansion of the doctrine. The revenue rule in this sense cannot be characterized as a long-established feature of the common law, and it should not be allowed to restrict the federal RICO statute.

A. *Canada's Suit Poses No Threat to U.S. Foreign Policy and Does Not Implicate the Separation of Powers Doctrine*

The primary justification for the revenue rule is that it allows courts to avoid overstepping their limited authority in the area of foreign affairs, thus maintaining the separation of powers.[248] The United States Supreme Court has stated that not every case or controversy that touches foreign relations is beyond the judicial power.[249] Only if the application of foreign revenue laws infringes upon the separation of powers should the court decline to exercise jurisdiction in the case.[250]

The revenue rule should not be applied in every case involving foreign revenue laws.[251] The U.S. Supreme Court, in *Milwaukee County v. M.E. White Co.*,[252] confirmed that the revenue rule does not address jurisdiction, but the merits of the case.[253] The Restatement (Third) of Foreign Relations Law also states that a court can use discretion when deciding whether to entertain a case involving foreign revenue laws.[254] According to Second Circuit precedent, the revenue rule should only apply where the court finds separation of powers problems.[255] Under this authority, it is necessary to examine the separation of powers implications of allowing a foreign government to bring RICO claims in order to decide whether the revenue rule should apply.

Enforcing Canada's civil RICO claim does not interfere with the political branches' foreign policy goals. Because Canada's suit is

248. *See supra* notes 192–96 and accompanying text.

249. Baker v. Carr, 369 U.S. 186, 211 (1962).

250. *Trapilo*, 130 F.3d at 553.

251. *Id.*

252. 296 U.S. 268 (1935).

253. *Id.* at 272.

254. RESTATEMENT, *supra* note 5.

255. *See Trapilo*, 130 F.3d at 553; *see supra* notes 120–23 and accompanying text.

different from a tax claim,[256] much of the separation of powers analysis that the *Reynolds II* court employed is not applicable in this case. The *Reynolds II* court discussed U.S. tax treaties and concluded that those treaties do not provide for assistance with collection of foreign taxes except in limited circumstances.[257] Therefore, the majority concluded the policy of the political branches is to refuse to assist with foreign tax collection.[258] However, because *Reynolds II* involved a RICO suit, not a tax claim, nothing in the treaty framework conflicts with a civil RICO claim.[259] Instead, what is salient is that Congress enacted RICO to allow plaintiffs, including foreign governments,[260] to bring claims in response to racketeering activity. It is not uncommon for Congress to adopt divergent policies in various areas of law. While Congress chooses not to provide for enforcement of every tax claim, it can at the same time create a cause of action for foreign governments to collect damages for racketeering activity. Such goals are not in conflict because the courts can adjudicate RICO claims without opening the door to "general enforcement" of foreign tax claims.

The policy behind RICO is the relevant foreign policy for the purposes of determining whether a separation of powers problem exists within a RICO claim. Congress intended foreign governments to have a cause of action under RICO.[261] Because RICO established Canada's cause of action, the *Reynolds II* court would not be forced to formulate foreign policy, adjudicating the claim would implement the policy established by Congress.[262] Furthermore, the *Trapilo* court held that the fact that a foreign tax law must be examined does not necessarily force the court to make an impermissible foreign relations choice.[263]

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256. *See infra* Section V.B.1.

257. Reynolds II, 268 F.3d 103, 115 (2d Cir. 2001).

258. *Id.*

259. *See infra* notes 271–87 and accompanying text.

260. *See* Republic of the Philippines v. Marcos, 862 F.2d 1355, 1358 (9th Cir. 1988); *cf.* Pfizer, Inc. v. Gov't of India, 434 U.S. 308, 311–19 (1978) (interpreting similar civil enforcement provision in the Clayton Act, 15 U.S.C. § 4 (1994)).

261. *Marcos*, 862 F.2d at 1358.

262. *See Reynolds II*, 268 F.3d at 137 (Calabresi, J., dissenting) (stating that the concern for separation of powers is "misplaced whenever the legislative and executive branches have created the cause of action. Under the circumstances, the courts cannot be said to be formulating foreign policy, they are simply implementing the policy established by the other branches").

263. United States v. Trapilo, 130 F.3d 547, 553 (2d Cir. 1997).

The *Reynolds II* court's dismissal of Canada's civil RICO claim actually frustrates Congress' chosen policy to eliminate organized crime. Although U.S. federal courts are not obligated to further the interests of other sovereigns,[264] they are obligated to further America's interests as defined by the political branches.[265] Courts are normally bound to entertain suits brought under federal statutes such as RICO.[266] Congress enacted RICO to encourage private parties, including foreign governments, to help eliminate racketeering activity.[267] RICO's private enforcement provision serves domestic interests and Congress chose to allow foreign governments to participate in serving those interests, even if the result would further Canada's interests too.[268] The chosen policies behind RICO would be partially ineffectual if the claims of foreign governments were not entertained. Furthermore, the revenue rule may harm the very foreign relations that it is presumed to protect. It seems likely that Canada would be more offended by the dismissal of its apparently viable RICO claim than it would be by an evaluation of its revenue laws after it had willingly submitted to the court's jurisdiction. Therefore, the *Reynolds II* court erred by applying the revenue rule to bar Canada's civil RICO claim because the suit does not interfere with the separation of powers.

B. The Second Circuit Employed a Novel Use of the Revenue Rule That Impermissibly Restricted RICO

A civil RICO suit's liability, remedy, and purpose differ greatly from a tax collection suit. Therefore, the revenue rule should not apply equally to both types of cases. The *Reynolds II* majority impermissibly expanded the revenue rule to a U.S. statutory claim, and in doing so, defied Second Circuit precedent and the goals of Congress.

264. Banco Nacional de Cuba v. Sabbatino, 376 U.S. 398, 448 (1964) (White, J., dissenting).

265. *Reynolds II*, 268 F.3d at 136 (Calabresi, J., dissenting).

266. W.S. Kirkpatrick & Co. v. Envtl. Tectonics Corp., 493 U.S. 400, 409 (1990).

267. Rotella v. Wood, 528 U.S. 549, 557 (2000).

268. *Reynolds II*, 268 F.3d at 136 (Calabresi, J., dissenting).

1. A RICO Claim is Not a Tax Claim

The Second Circuit's holding in *Reynolds II* rested on the false premise that Canada's RICO claim was nothing more than a tax claim.[269] The *Reynolds II* court analyzed the case as if it were identical to a suit to collect taxes.[270] The assertion that RICO claims are just indirect tax claims, and the concomitant assumption that the revenue rule applies equally to both, involves a sleight of hand that ignores the differences between the two types of claims. The basis of liability for the RICO claim, the amount of the damages available, and the very purpose of the civil RICO suit are much broader than a basic tax collection suit.

First, both the basis for liability and the rule of decision for Canada's claim is U.S. federal statutory law.[271] The gravamen of Canada's claim is that the defendants' ongoing tobacco smuggling scheme violated RICO, causing Canada economic injury.[272] Congress created the RICO civil cause of action and the rule of decision in this case also derives from the federal statute.[273] In contrast, in *Gilbertson*,[274] British Columbia tried to directly enforce a tax judgment that was explicitly based on the defendant's violation of Canadian tax laws.[275] Therefore, *Reynolds II* and *Gilbertson* cannot be compared because the *Gilbertson* claim did not purport to be based in any American law.

Second, the amount of relief available in Canada's RICO suit greatly exceeds Canada's lost tax revenues.[276] In contrast, a claim for tax collection might include payment of the tax owed, interest, and penalties that are typically more modest than the taxes owed.[277] Canada's RICO remedy would amount to three times Canada's actual lost tax revenues and the cost of attorneys' fees,[278] bringing the total far above the

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269. *Reynolds II*, 268 F.3d at 115.

270. *See id.* at 130–31 (Calabresi, J., dissenting).

271. 18 U.S.C. §§ 1961–1968 (1994).

272. *Reynolds II*, 268 F.3d at 106.

273. European Community v. RJR Nabisco, Inc., 150 F. Supp. 2d 456, 476 (E.D.N.Y. 2001).

274. Her Majesty the Queen in Right of the Province of British Columbia v. Gilbertson, 433 F. Supp. 410 (D. Or. 1977), *aff'd*, 597 F.2d 1161 (9th Cir. 1979).

275. *Id.* at 1162.

276. *See Reynolds II*, 268 F.3d at 131.

277. *See, e.g.*, I.R.C. § 6700(a) (2002) ($1,000 penalty for promoting abusive tax shelters); § 6663(a) (seventy-five percent penalty for fraudulent underpayment); *Id.* at § 6672(a) (2002) (100 percent penalty for willful evasion).

278. 18 U.S.C. § 1964(c) (1994).

damages allowed in a tax collection suit. RICO also allows for equitable remedies such as divestiture of the defendant's interest, restrictions on future investments, and dissolution of the enterprise.[279] The remedial difference demonstrates that a RICO claim is more than merely an action for collection of taxes. In fact, Congress allowed treble damages and attorneys' fees to encourage plaintiffs to bring civil RICO suits in order to deter and eliminate racketeering activity.[280] According to the Second Circuit, there is "an extraordinary disparity" between tax collection techniques and RICO damages.[281]

Third, the purpose of Canada's RICO suit is not only to compensate for injury, but also to deter future racketeering behavior, to divest RICO enterprises of ill-gotten gains, and to turn plaintiffs into private attorneys general.[282] Because prosecutors might not identify all RICO violations, giving those harmed by racketeering an incentive to sue will increase the total number of RICO claims and further the Congressional goal of ending organized crime. Holding the defendants accountable would significantly raise the stakes of smuggling. While some of these defendants have been subject to criminal RICO liability,[283] Congress created civil RICO liability because it believed that criminal liability was insufficient to eliminate organized crime.[284]

RICO's treble damages provisions also punish the defendant for profiting from racketeering behavior. Treble damages divest the RICO enterprise of any ancillary benefits received from racketeering beyond the actual monetary damages that the plaintiff sustained. For example, the defendants' market share jumped from twelve percent in 1992 to approximately twenty percent in 1994.[285] Tobacco companies have a special incentive to smuggle their highly addictive products because consumer use of the smuggled tobacco will likely lead to increased long-term consumption and bolster brand loyalty even after the smuggling has ceased.[286] Unlike a tax collection action, a civil RICO action aims to

279. *Id.* § 1964(a).

280. Rotella v. Wood, 528 U.S. 549, 557 (2000).

281. United States v. Porcelli, 865 F.2d 1352, 1367 (2d Cir. 1989) (Newman, J., dissenting).

282. *Id.*; *see also supra* notes 38–42 and accompanying text.

283. *See* United States v. Miller, 26 F. Supp. 2d 415, 419 (N.D.N.Y. 1998).

284. *See* United States v. Harden, [1963] S.C.R. 366, 371 (Can.). *See also Reynolds II*, 268 F.3d 103, 131 (2d Cir. 2001).

285. *See* Plaintiff's Complaint at 12.

286. *See* U.S. DEPT. OF HEALTH AND HUMAN SERVS., PUBLIC HEALTH SERV., THE HEALTH CONSEQUENCES OF SMOKING: NICOTINE ADDICTION 6–9 (1988).

punish the defendant for these broader gains from illicit behavior, thereby reducing the incentive to smuggle.

While a tax claim targets those who fail to pay taxes, RICO targets those who engage in conspiracy and racketeering behaviors.[287] While a tax claim is intended only to collect revenue for the state, a RICO claim benefits a much broader circle of those indirectly injured by racketeering.[288] Given these distinctions, a RICO claim should not be characterized as merely an attempt to collect taxes. The *Reynolds II* court's essential mischaracterization of Canada's claim compromised the court's analysis.

2. Reynolds II *Impermissibly Expanded the Scope of the Revenue Rule by Applying It to Block a RICO Claim*

When Congress enacted RICO in 1970, the revenue rule was in serious doubt. The rule had never been applied to a federal statutory claim[289] and its scope was undefined.[290] Thus, Congress would not have contemplated the expansion of the revenue rule to interfere with a RICO claim. Congress did not expressly abrogate the common law rule. However, it was unnecessary for Congress to address the revenue rule, given its maligned status and dubious application to a statutory cause of action. In addition, Congress inserted a liberal construction clause into RICO, to ensure that future courts would not narrow the statute.

The *Reynolds II* court expanded the revenue rule by applying it to a statutory claim.[291] The majority cites only one case in which the rule barred a U.S. federal statutory action, *United States v. Boots*.[292] However, the Second Circuit expressly rejected *Boots*.[293] In fact, all of the subsequent cases from the Second Circuit allowed the statutory claims to proceed notwithstanding the involvement of foreign tax laws. [294] In

287. 18 U.S.C. § 1961 (1994).

288. Republic of the Philippines v. Marcos, 862 F.2d 1355, 1366 (9th Cir. 1988).

289. *Gilbertson*, decided in 1979, was the first case to apply the international revenue rule. *See* Her Majesty the Queen in Right of the Province of British Columbia v. Gilbertson, 597 F.2d 1161, 1164 (9th Cir. 1979).

290. Reynolds II, 268 F.3d 103, 109 (2d Cir. 2001).

291. *Id.* at 135 (Calabresi, J., dissenting).

292. 80 F.3d 580 (1st Cir. 1996).

293. United States v. Trapilo, 130 F.3d 547, 553 (2d Cir.1997).

294. *See Trapilo*,130 F.3d at 547; United States v. Pierce, 224 F.3d 158 (2d Cir. 2000); European Community. v. RJR Nabisco, 150 F. Supp. 2d 456, 483 (E.D.N.Y. 2001).

contrast, all of the American cases relied on by the *Reynolds II* majority apply the revenue rule in situations where the cause of action is based on a foreign revenue law or judgment.[295] It was not until *Boots* was decided in 1996 that the revenue rule was used as a defense to a U.S. statutory claim, more than 25 years after RICO's promulgation.[296]

Despite the confusion surrounding the revenue rule, under *Gilbertson*, the revenue rule primarily prohibits a suit by a foreign sovereign for the enforcement of a tax judgment rendered in another country.[297] The Second Circuit has held that not all cases involving foreign taxes mandate dismissal under the revenue rule.[298] Unlike *Gilbertson* and most other revenue rule cases, the source of liability here is an American statute, not a foreign revenue law. The *Reynolds II* majority refered to the Canadian case *United States v. Harden*[299] for the proposition that the revenue rule blocks claims that are only "indirectly" for tax revenues. However, *Harden* involved a stipulation of settlement of a foreign tax claim,[300] which is more analogous to a tax judgment than a RICO claim, because the liability is derived from violating tax laws, not racketeering. A RICO claim cannot be equated with a claim to enforce a foreign revenue law.[301] To apply the revenue rule to block a statutory cause of action is a novel expansion of the common law rule that did not exist at all before 1996.[302] Even now, it is questionable whether the revenue rule should ever apply to a cause of action based on a U.S. statute.

The *Reynolds II* court's novel expansion of the revenue rule was also impermissible because RICO is a broad remedial statute and expanding the revenue rule inappropriately narrows the scope of the statute. Remedial statutes should be liberally construed to effectuate Congressional purpose and discourage evasions by wrongdoers.[303] RICO itself contains a liberal construction clause, which codifies this rule of statutory construction. It is within the Congressional purpose of RICO to

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295. *Reynolds II*, 268 F.3d at 109–11 (explaining that the early English cases use the revenue rule in a different sense). *See also supra* note 65 and accompanying text.

296. *Boots*, 80 F.3d at 587–88.

297. Her Majesty the Queen in Right of the Province of British Columbia v. Gilbertson, 597 F.2d 1161, 1166 (9th Cir. 1979).

298. *See* United States v. Trapilo, 130 F.3d 547, 553 (2d Cir. 1997).

299. [1963] S.C.R. 366, 371 (Can.).

300. [1963] S.C.R. at 371.

301. *See supra* notes 270–88 and accompanying text.

302. United States v. Boots, 80 F.3d 580, 588 (1st Cir. 1996).

303. Westinghouse Elec. Corp. v. Pac. Gas & Elec. Co., 326 F.2d 575, 580 (9th Cir. 1964).

punish and deter schemes such as the one at issue in *Reynolds II*.[304] The *Reynolds II* court used the revenue rule as an exception to bar an otherwise valid RICO suit. Although exceptions to remedial statutes should be narrowly construed, the court instead adopted an expansive new version of the revenue rule, one at odds with Second Circuit precedent. Restricting RICO through the revenue rule is contrary to the Supreme Court's practice of rejecting limitations on the statute's application and reading RICO broadly.[305]

To justify its novel expansion of the revenue rule, the *Reynolds II* court asserted that statutes are interpreted to preserve well established common law. However, although Congress did not expressly abrogate the common law revenue rule in enacting RICO, it was not necessary for Congress to do so. The revenue rule's existence was uncertain when RICO was promulgated, in part because the domestic revenue rule had been virtually abolished.[306] In 1970, the revenue rule had never been applied in the international context.[307] The few cases that mentioned the revenue rule failed to define it precisely,[308] so the scope of the rule was ambiguous. It is not clear that Congress would have believed that the rule was still being applied when it drafted the RICO statute.

Where the scope of the common law rule is ambiguous, a new extension of the rule cannot be logically called "well established." Had the application of the revenue rule to block U.S. statutes been firmly embedded in the common law at the time that RICO was promulgated, then there might be a presumption favoring its continued existence.[309] Because this is a novel use of the revenue rule, and the revenue rule was never used to deprive a foreign country of a statutory cause of action prior to the enactment of RICO, the revenue rule cannot be used to restrict the scope of the statute. In addition, the United States Supreme Court has held that the common law should not prevail where it would frustrate the purpose of a remedial statute, or to lessen its scope or obviate the remedial purpose of the statute for a significant class of

304. *See* United States v. Porcelli, 865 F.2d 1352, 1355 (2d Cir. 1989).

305. *See* Sedima, S.P.R.L. v. Imrex Co., 473 U.S. 479, 500 (1985). *See also supra* notes 43–60 and accompanying text.

306. *See supra* notes 90–100 and accompanying text.

307. *See supra* note 81 and accompanying text.

308. *See* Reynolds II, 268 F.3d 103, 109 (2d Cir. 2001).

309. Miles v. Apex Marine Corp., 498 U.S. 19, 32 (1990).

plaintiffs.[310] Rules of statutory interpretation do not require courts to adhere to the common law if to do so would be at odds with obvious legislative purpose or lessen the plain scope of the statute.[311] Congress need not affirmatively proscribe every common law rule that might frustrate the statute's goals.[312] In sum, the existence of the revenue rule was in question at the time that RICO was enacted, and its scope remains ambiguous.[313] Such an indeterminate rule should not be applied to lessen the scope of RICO.

VI. CONCLUSION

RICO is a broad statute designed to attack organized crime with formidable civil sanctions. The Second Circuit's attempt to restrict the scope of RICO with the revenue rule violated canons of statutory construction, and RICO's liberal construction clause, because it used a common law doctrine with only weak support to narrow the statute and frustrate its purpose. In addition, the separation of powers issues in the case were not significant enough to warrant dismissing the case. This application of the revenue rule could encourage international tax evasion and smuggling by depriving foreign governments of a powerful cause of action for behaviors that take place primarily on American soil. Canada has petitioned to the U.S. Supreme Court, and a similar case will likely be appealed to the Eleventh Circuit.[314] Thus, the issue of international smuggling in tobacco is far from resolved. Given Congress' purpose in enacting RICO was to seek the eradication of organized crime and to divest wrongdoers of their ill-gotten gains the denial of a civil cause of action to foreign governments does not just deny foreign governments of tax revenues—it deprives RICO of the deterrent effect that Congress intended to create.

310. Isbrandtsen Co. v. Johnson, 343 U.S. 779, 783 (1952).

311. *Id.* at 782–83.

312. United States v. Texas, 507 U.S. 529, 534 (1993).

313. *Reynolds II*, 268 F.3d at 109.

314. Republic of Ecuador v. Philip Morris, 188 F. Supp. 2d 1359 (S.D. Fla. 2002).