TERRITORY OF HAWAII

DEPARTMENT OF THE ATTORNEY GENERAL

HONOLULU

45 - C.

July 18, 1939.

OPINION NO. ~~1641~~ 1717

TAXATION: ACT 141, S. L. 1935:

The tax imposed by Act 141, S. L. 1935 does not accrue where an order is placed through an agent who represents the buyer, and the seller, who supplies the goods from mainland stock, is not doing business in the Territory.

SAME: INTERSTATE COMMERCE:

No unconstitutional burden on interstate commerce is imposed by a tax measured by the sale of goods, where the contract of sale is made in the Territory? the price is paid here, and the goods are delivered here.

SAME: DUE PROCESS OF LAW:

The legislature can and has taxed local business measured by gross proceeds of sales transacted in the Territory even though title does not actually pass in the Territory.

SAME: INTERSTATE COMMERCE:

When a sale is made of goods in transit even though title should pass through the transfer of the bill of lading while the goods were still in transit there would be no unconstitutional burden on interstate commerce, there being no risk of a cumulative burden of taxation to which local commerce is not exposed.

SAME: SAME:

If a mainland firm, acting through a local representative, sells goods to a local buyer which the seller and buyer arrange to have supplied to the buyer through interstate commerce, the sale cannot be taxed by the Territory because of the risk of a cumulative burden to which local commerce is not exposed.

SAME: SAME:

If a local firm sells goods to a local buyer, although the seller and buyer arrange to have the goods supplied to the buyer through interstate commerce, the seller is not exposed to the risk of cumulative taxation on the sale to the local buyer where he merely purchases the necessary goods on the mainland and has them shipped direct to the buyer, and local taxation of the sale is not an unconstitutional burden on interstate commerce.

Honorable Wm. Borthwick,

Tax Commissioner,

Territory of Hawaii,

Honolulu, T. H.

Dear Sir:

Your letter of April 6, as supplemented by your letter of June 22, present for our opinion certain situations as to the application of the tax imposed by Act 141, S. L. 1935.

In all of the situations listed below the company concerned is a Hawaiian Corporation having its principal office at Honolulu and a branch office at San Francisco.

(1) The A. Company has a general agency contract under which it represents a Hawaiian plantation which

forwards to it at Honolulu an order for certain goods. The A. Company forwards the order to its San Francisco office, which places the order, receives and pays the bill, and forwards the invoice to the head office at Honolulu. The A. Company at Honolulu bills the plantation for the cost, plus a percentage commission, and collects from the plantation.

(2) The A. Company at Honolulu receives an order from a customer whom it does not represent as agent, at a price which is quoted F.O.B. San Francisco, plus freight, etc. This order is forwarded to the San Francisco branch, which places the order, receives and pays the bill, and forwards the invoice to the head office at Honolulu, which in turn bills the customer and collects from him.

In this situation and in (3) below the goods are consigned to the A. Company at Honolulu, marked for the customer. The Company either (a) endorses the bill of lading to the customer, so that the goods are delivered directly to the customer, or (b) in some cases, to save demurrage, the goods are picked up and stored in the Company's warehouse until delivery can be made.

(3) The A. Company at Honolulu receives from a customer an order for goods exclusively handled by another local firm, hereinafter called the Supply Company. The A. Company, therefore, to fill the order

places an order with the Supply Company which bills the A. Company at Honolulu, and has the goods marked for the A. Company's customer, consigned to the A. Company, as in other cases. In this instance both the A. Company and the Supply Company claim interstate commerce.

(4) The A. Company sells goods which already are in transit to the A. Company, at a price which is quoted F.O.B. San Francisco. Upon arrival of the goods either (a) the customer is given a wharf order, or (b) the goods are taken to the A. Company's warehouse, segregated, and then delivered, or (c) the goods are picked up by a common carrier for delivery to the customer.

In four recent decisions the Supreme Court of the United States has clearly pointed out that interstate commerce must pay its way, and a tax is not invalid where imposed upon a local business and where under the facts the tax is not equally open to imposition by other states, causing interstate commerce to bear a double burden to which local commerce is not exposed.

In <u>Western Live Stock</u> v. <u>Bureau of Revenue,</u> 303 U. S. 250 (Feb. 28, 1938) 82 L. Ed. 823, there was involved the New Mexico privilege tax upon the gross receipts from the sale of advertising space. The magazine was sold in interstate commerce. The court assumed that the performance of the contract for the sale of advertising space involved the interstate distribution of the magazine (although it had not been alleged specifically that the contract with the advertiser required such interstate distribution or that the compensation paid for the advertising would not be earned without such distribution), and nevertheless held:

1. “Even interstate business must pay its way.”

2. Where a tax is invalid the characteristic vice is that the burden of the tax is of such a nature as to be capable of being imposed or added to by every state which the commerce touches so that without the protection of the commerce clause the commerce would bear cumulative burdens not imposed on local commerce. In addition to the tax being sustained on the ground noted in paragraph 3 below the court specifically sustained it on the ground that so far as the value contributed by the interstate circulation was taxed nevertheless the situation was such that this value could not again be taxed elsewhere, the subscriptions of the out-of-state subscribers of the magazine not being involved in the measure of the tax.

3. Taxation measured by gross receipts has been sustained when fairly apportioned to the commerce carried on within the taxing state, at least where the

tax is on a local business distinct from interstate commerce, and the court pointed out that the business of printing and publishing the magazine was distinct from the circulation of the magazine. So far as the advertising rates reflected the interstate distribution of the magazine this burden was held to be too remote.

In Coverdale v. Arkansas and Louisiana Pipe Line Co., 303 U.S. 604, 82 L. Ed. 1043, the tax was imposed on the production of power for use. It was held to be a tax on local business although the power produced was used to raise the pressure of gas to permit transportation of the gas to other states. The court pointed out that the tax imposed upon the production of power was of such nature that it could not be imposed by more than one state and that the increased cost of interstate commerce alone was not sufficient to invalidate the tax.

In J. D. Adams Manufacturing Co. v. Storen, 304 U.S. 307, 82 L. Ed. 1365, there was involved the Indiana gross income tax. The court decided that the tax was not upon domicile alone, nor upon the doing of business, nor a franchise fee, nor upon the act of manufacturing, nor in lieu of property taxes, and the court held that it was a straight tax upon the collection of gross income. The taxpayer manufactured road machinery and equipment, maintaining its factory and home office in Indiana and filling orders from other states, which were all subject to approval from the home office, by shipments made from the factory, receiving payment at the home office. The court held that the vice of the statute was that it included in the measure of the tax without apportionment receipts from interstate sales and was of such a character that it might be laid by states in which the goods were sold as well as by the state of Indiana in which they were manufactured. Thus, there was a risk of double taxation not borne by local commerce. The court specifically pointed out that the tax was not laid upon the manufacture of the goods (the local business) but was on the gross sales.

In Gwin White and Prince, Inc. v. Henneford, 83 L. Ed. Adv. Sh. 276 (Jan. 3, 1939), annotated in 39 Columbia Law Review, May 1939, p. 864, there was involved the Washington tax measured by the gross receipts of business. Appellant was engaged in marketing fruit shipped to other states, on a commission basis, and rendered services in aid of interstate commerce, which services were not confined to the state of Washington. It was held that the measure of the tax, which included the entire compensation, reached the entire interstate commerce service, both that rendered within and that rendered without the state, and such tax, at least where not apportioned to the activities carried on within the state, was an invalid burden upon interstate commerce, because of the risk of a multiple burden to which local commerce was not subjected.

It thus appears that in these four most recent cases the Supreme Court of the United States has been guided in every instance by the principle that a multiple burden upon interstate commerce, or the possibility of such a multiple burden to which local commerce is not subjected, renders a tax invalid. This feature is commented upon in 52 Harv. Law Rev. (Jan. 1939) 502.

The application of a local tax measured by sales where the goods are not on hand in the Territory at the time when the sale is made is the subject of only one of the above four cases, i.e. the J. D. Adams Manufacturing Company case. In that case the tax was attempted to be levied by the state in which the seller was situated, and in an article in 52 Harv. Law Rev. (Feb. 1939) 617, it is argued that the state in which the buyer is located may impose a tax and that the Supreme Court has never held to the contrary. In addition to presenting argument for this theory the article reviews the cases on the subject.

In Banker Bros. v. Pa. 222 U.S. 210, the taxpayer was doing business in Pennsylvania selling automobiles. No machines were kept in stock except those used for demonstration. As orders were received at a "f.o.b. factory" price, the taxpayer forwarded the order to the Pierce Company in New York state together with a partial cash payment which had been received from the purchaser. The automobile ordered was then shipped to the taxpayer who was billed for the balance of the price and the taxpayer received the automobile and in turn delivered it to the buyer upon his payment of the balance. The court decided that the taxpayer was not an agent of the Pierce Company and that the taxpayer in Pennsylvania occupied the position of a vendor to the Pennsylvania purchaser. The court said:

> "It is contended that Banker Brothers Company were agents and the Pierce Company an undisclosed principal. It is urged that the sale was an interstate transaction between the manufacturer and the purchaser, with Banker Brothers Company merely acting as an agent which looked after the delivery of the machine and collected the purchase price.
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> This is one of the common cases in which parties find it to their interest to occupy the position of vendor and vendee for some purposes under a contract containing terms which, for the purpose of restricting sales and securing payment, come near to creating the relation of principal and agent. But as between Banker Brothers Company and the Pittsburg purchaser, there can be no doubt that it occupied the position of vendor. As such it was bound by its contract to him and under the duty of paying to the state a tax on the sale.
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> The name of the Pierce Company was not mentioned in the order signed by the purchaser. Had there been a breach of its terms he would have had a cause of action against the Banker Brothers Company, with whom alone he dealt. If he had failed to complete the purchase the Pierce Company would have no right to sue him on the contract. The fact that he was liable for the freight by virtue of the agreement to 'pay the list price f.o.b. factory' did not convert it into a sale by the manufacturer at the factory; neither was that result accomplished because, with the machine, Banker Brothers Company also delivered to the buyer in Pittsburg a warranty from the manufacturer direct.
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> These were mere incidents of the interstate contract of sale between Banker Brothers Company and the purchaser in Pittsburg, who was not concerned with the question as to how the machine was acquired by his

vendor, or whether that company bought it from another dealer in the same city or from the manufacturer in New York. The contract was made in Pennsylvania, and was there to be performed by the delivery of the automobile and the payment of the balance of the purchase price. See American Steel & Wire Co. v. Speed 192 U.S. 500, American Express v. Iowa, 196 U.S. 133, 146. The court properly held it was not an interstate transaction, but taxable under the laws of Pennsylvania."

In Wiloil Corp. v. Pa. 294 U.S. 169, the situation was as follows: The taxpayer was assessed under the liquid fuels act for a tax upon liquid fuels sold within Pennsylvania. The appellant was a Pennsylvania corporation having its principal place of business in Pennsylvania and received an order in Pennsylvania for delivery within the state; the price specified was "f.o.b. Wilmington, Delaware". The contract was accepted in Pennsylvania. The order was filled by obtaining the fuel from a Delaware company, which, on the taxpayers order, shipped the fuel direct to the purchasers in Pennsylvania, who were named as consignees. It was held that the tax applied in spite of the inference that the parties intended delivery to the purchaser in Delaware on account of the F.O.B. notation. Appellant was free under the contract to supply the fuel by shipping from any place within or without Pennsylvania, and the billing was held to be merely a method of price fixing and not an indication of the source of shipment. The interstate transportation was held to be "not required or contemplated, it may be deemed as merely incidental."

The above two cases constitute the principal cases in the Supreme Court of the United States as to taxability of sales by the state where both seller and buyer are located, where delivery is made from goods not within the state at the time of the sale. Where the goods are within the state at the time of the sale the transaction undoubtedly is intrastate. Sonneborn Bros. v. Cureton 262 U.S. 506; see also Superior Oil Co. v. Miss. 280 U.S. 390. But under the Banker Bros. case and the Wiloil Corp. case it is not essential to taxability that the goods be within the taxing state at the time when the contract of sale is made. The Banker Bros. case establishes the principle that when the seller is doing business in the state, makes the contract within the state, receives the payment there, and makes delivery within the state, the fact that the seller in turn makes an interstate purchase in order to fill the order does not affect the taxability of the local sale. The only question left open by the Banker Bros. case is as to whether or not it is essential that the vendor himself receive the goods and in turn deliver them. The Wiloil case goes a step further and decides that even though the seller does not receive the goods and in turn deliver them but instead has the goods consigned directly to the purchaser no interstate sale is involved where this interstate shipment was not required or contemplated and was merely incidental. (The two cases are compared in a note in <u>38 Col. Law Rev. (Jan. 1938) 49, 57 et seq.)</u> Both the <u>Banker Bros.</u> case and the <u>Wiloil</u> case antedated the recent trend in which the Supreme Court of the U. S. has gone still further, and has laid down the test of multiple burden for determining the validity of taxes in relation to commerce.

There remain for consideration five other cases, only two of which, however, were decided after the Western Live Stock and other recent U. S. Supreme Court cases. In <u>National Cash Register Co.</u> v. <u>Taylor,</u> 11 N.E. (2d) 881, Nov. 1937 the taxpayer was an Ohio manufacturer authorized to do business in New York where it maintained an office. The question was as to the imposition of the New York City sales tax with respect to a special order received in New York City together with a cash payment, subject, however, to acceptance by the company in Ohio. Such special order was forwarded to Ohio, the machine was manufactured as ordered, and either shipped direct to the customer or else shipped to the New York office for delivery. It was held that such sales could not be taxed. The court pointed out: (1) that the special orders required delivery of goods manufactured by the taxpayer and that the taxpayer had no factory within the state, and (2) that the contract of sale did not become effective until the order was accepted in Ohio. The Wiloil Corp. case was distinguished on the ground that in the present situation interstate commerce was contemplated and required by the contract of sale.

In Sears Roebuck & Co. v. McGoldrick, 279 N.Y. 184, 18 N.E. (2d) 25, Nov. 29, 1938 the New York City tax was upheld in the following situation:

Sears Roebuck & Co. had stores in New York in which it kept a stock of goods. Its principal office was at Chicago, Illinois, and it also maintained a distributing point in Pennsylvania and a factory in New Jersey. The case involved what were termed "ship direct orders" covering bulky articles not kept in stock in the New York stores. There were samples on display in the stores, and the customer would be informed that the merchandise was not kept in stock but must be ordered from Pennsylvania or New Jersey. His order was taken and a sales slip made out which stated that the merchandise was to be shipped either from Pennsylvania or New Jersey direct to the customer in New York. The order was filled from one of these sources by direct shipment. Payment was made in New York and it was conceded that the contract of sale was made in New York. Such "ship direct orders" constituted only 15% of the business.

The court reasoned that it made no difference to the purchaser from what place the article was delivered and that the method employed by the taxpayer was entirely a matter of its convenience, and not an important feature of the contract. It was also pointed out that the company paid no more tax on the "ship direct orders" than on the sales made from the stock kept in New York. A further point was that there was no possibility of double taxation: "The sale was complete in New York City; the price was to be paid in New York City; it was a New York State contract governed by the laws of this state". The National Cash Register case, 11 N.W. (2d) 881, supra, was distinguished on the ground that there the contracts were made and the sales consummated in Ohio where the company accepted and executed the orders. The court cited the J. D. Adams Manufacturing Co. case, Coverdale v. Arkansas and Louisiana, Western Live Stock case, Wiloil Corp. and the Banker Bros. cases as well as other authorities.

In Compagnie Generale Trans Atlantique v. McGoldrick, 279 N.Y. 192, 18 N.E. (2d) 28, a companion case, the New York City tax was held invalid in its application to sales of oil delivered direct to ships in New York waters from tanks in New Jersey, though the seller was doing business in New York, and the contract was made in New York. The court held that the subject of the sale was the New Jersey product. See also State v. Southern Oil Service, 124 S.W. (2d) 704 (Tenn.) and Long v. Sherrill Terminal Co. 187 So. 412 (Ala.).

In Montgomery Ward & Co. Inc. v. Fry, 277 Mich., 260, 269 N.W. 166, the Supreme Court of Michigan took a view contrary to that held by the Court of Appeals in New York in the Sears Roebuck case but the Michigan case was decided October 5, 1936, prior to the Western Live Stock and other cases. The Michigan court also is in error in failing to cite or follow the Wiloil Corp. case. See also Lee v. Hector Supply Co. 183 So. 489 (Fla.) which fails to cite or consider the Wiloil Corp. case or any of the later cases.

In Baer's Appeal, 82 Pa. Superior Ct. 414, the question was as to the application of an annual fee of three dollars on each wholesale vendor of goods. The appellant did business by soliciting orders in the state, and as he obtained orders he filled them by purchasing from dealers in other states who by his order shipped direct to his vendees in Pennsylvania. He paid his vendors and his vendees paid him. It was held that the tax applied, and the court pointed out that he was not taxed on his purchases made in another state but instead was taxed on his sales within the state for delivery to vendees within the states and the tax was imposed where the taxpayer conducted the business and where he resided. The interstate commerce involved in his purchase out of the state of the thing he wanted to complete his sale by delivery in the state was held to be merely incidental.

With this review of the authorities we turn to the four situations presented above, which will be discussed under the same paragraph numbers.

A. (1) If you feel satisfied from your knowledge of local practices or otherwise that the A. Company, in placing the order for the plantation, paying for the goods, and in turn billing the plantation for the cost plus a commission, is acting as the agent of the plantation for the purpose of making the purchase, and is not acting as a vendor making a second sale to the plantation, then the tax should not be applied to the entire amount collected by the A. Company, but only to the commission received for the service rendered. The remainder of the sum received constitutes merely the return of money advanced. The plantation may or may not be liable to consumption tax, depending upon other facts.

(2) In the second situation there are two sales, first, the sale by the mainland firm to the A. Company, and secondly the sale by the A. Company to its local customer. Only the second sale is included in the measure of the tax, but as to it the tax clearly applies. Where the goods are picked up, stored in the A. Company's warehouse, and delivery is made from the warehouse the situation clearly comes within the Banker Bros. case. But it is not essential that the A. Company receive and transfer physical possession of the goods sold, and the Banker Bros. case did not so intimate. If the bill of lading is transferred after the goods have arrived, this being a delivery of the goods within the Territory is sufficient to bring the matter within the Banker Bros. case. But even if the bill of lading should

be received by the A. Company at Honolulu and negotiated while the goods were still in transit the result would be the same. From the standpoint of due process of law the Territory clearly has authority to tax the local business and measure the tax by such sales, by reason of the transactions here, whether or not title passes in the Territory, and the legislature has expressed its intent to include in the measure of the tax all the sales which it constitutionally may. Act 141, S.L. 1935, Sec. 2B; see Compania General de Tobacos v. Collector, 279 U.S. 306, 73 L. Ed. 704. From the standpoint of the interstate commerce clause, the tax is valid because the A. Company is not exposed to the hazard of taxation by any other state and therefore there is no risk of cumulative burdens not imposed on local commerce.

(3) Insofar as the A. Company is concerned the third situation does not differ materially from the second and the tax applies to the sale by the A. Company to the customer.

As to the local firm which supplies the A. Company, it is necessary to inquire whether that firm is merely an agent or is itself a vendor. In other words, are there two sales, (1) from the mainland firm represented by the Supply Company to the A. Company, and (2) from the A. Company to the customer; or are there three sales, (1) from the mainland firm to the Supply Company, (2) from the Supply Company to the A. Company, and (3) from the A. Company to the customer.

(a) Assuming that the Supply Company is merely an agent of the mainland firm, so that the sale which would be taxed would be a sale by the mainland firm, represented by its local agent, to the A. Company, the further question arises as to whether interstate commerce was required or contemplated. The fact that the goods were shipped marked for A. Company's customers would seem to indicate that arrangements were made between the parties for an interstate shipment. Added to this is the fact that the seller (the mainland firm) is exposed to hazards of taxation not borne by local commerce. We do not believe that the New York Court, in reaching opposite results in the Sears Roebuck and Compagnie Generale cases, made a satisfactory distinction. Compare Jagels "A Fuel Corp." v. Taylor, 255 App. Div. 965, 8 N.Y.S. (2d) 456, and see the criticism of the New York cases in 52 Harv. Law Rev. 617 supra. Until and unless further cases clarify the matter, and if the assumptions above made are true in fact, we do not believe this sale from the mainland firm to A. Company through a local agent should be taxed.

(b) Assuming on the other hand that the Supply

Company is not an agent but is itself the vendor to the A. Company the result will be different. As previously stated, the doctrine of the <u>Bankers Bros.</u> and <u>Wiloil Corp.</u> cases has been carried still further by the <u>Western Live Stock</u> and other cases. Where the mainland firm sells to the local Supply Company and the local Supply Company sells to the A. Company the Supply Company is not exposed to the hazard of taxation by the mainland state upon its sale to the A. Company. The mere filling of the local Supply Company's purchase order on the mainland could not expose it to taxation by the mainland state upon the resale of these goods, and the interstate commerce clause is not required as protection. The sale to the A. Company is local business within the Territory, which is not exposed to the hazard of double taxation any more than other local commerce. Upon the assumptions made in this paragraph (b), the sale to A. Company is taxable.

(4) In the fourth situation the sales are taxable. This is clear even under the <u>Banker Bros.</u> case since delivery was made and accepted in the Territory in each instance, either through the giving of wharf orders (it being immaterial whether the customer sent its own truck or a common carrier to pick up the goods) or through the actual segregation of the goods and delivery by the A. Company itself.

It will be noted that none of the many cases in which an out of state firm maintains a soliciting agent in the taxing state have been cited or discussed. Such cases are not relevant, and such a situation is not the subject of this opinion.

Respectfully,

Rhoda V. Lewis

RHODA V. LEWIS
Deputy Attorney General

APPROVED:

Ernest L. Kai

Acting Attorney General