STATE OF HAWAII

DEPARTMENT OF THE ATTORNEY GENERAL

Honolulu, Hawaii 96813

March 15, 1965

Honorable Edward J. Burns
Director of Taxation
State of Hawaii
Honolulu, Hawaii

Dear Sir:

This is in response to a request for an opinion concerning the taxability of travel agents under our general excise tax (chapter 117, Revised Laws of Hawaii 1955, as amended). Since numerous correspondence and reports are attached to the request but questions are not stated with specificity, we take the liberty of stating what we believe are the five questions to which our opinion is sought, namely:

(1) If a local travel agent sells to persons in Hawaii tickets for surface or air transportation to points outside the state of Hawaii, is the local travel agent subject to the Hawaii general excise tax on the commissions earned for the sale of such tickets?

(2) If a local travel agent sells to persons in Hawaii tours to points outside the state of Hawaii and sends its own tour director along with the tour group, is the local travel agent subject to the Hawaii general excise tax on the commissions, fees, or net return (after payment of hotel accommodations, transportation costs, and other related items) earned for the sale and conducting of such tours?

(3) If a local travel agent, receiving a tour group from a mainland travel agent, either conducts the local tour himself or refers the group to another local tour company, or else handles the arranging of hotel and other accommodations, is the local travel

agent subject to the Hawaii general excise tax on the commissions or fees earned for the rendering of such services?

(4) If a person from the mainland, acting as a tour conductor, brings a tour group to Hawaii and then returns to the mainland, is such a person subject to the Hawaii general excise tax for the commissions, fees, or net return (after payment of hotel accommodations, transportation costs, and other related items) derived from the sale and conducting of these tours?

(5) If a local branch office of a mainland travel agency provides services to tourists in Hawaii who are members of tour groups originating in the mainland through the parent company's sales and promotional efforts, is the local branch office subject to the Hawaii general excise tax for all or portions of the commissions, fees, or net return (after payment of hotel accommodations, transportation costs, and other related items) earned by the parent company for the sale and conducting of these tours?

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No question appears to be raised as to the total moneys received by the local travel agent, a portion of which are in turn distributed to the airlines, steamship companies, railroads, hotels, buses and the like. All of the questions are concerned with the commissions, fees, or net return (after payment of hotel accommodations, transportation costs, and related items) earned by the travel agent for services rendered.

The Hawaii general excise tax, as applied to travel agents, is measured by the amount of commissions earned for services rendered to travelers. The subject of the tax is the privilege of doing business and other activities in the state of Hawaii. The significant factor, therefore, in considering the questions presented is not that travelers are moving in interstate commerce but whether the activities engaged in by travel agents are of a local character severable from interstate commerce and whether such activities engaged in outside the state of Hawaii are incidental to the privilege of engaging in business within the state of Hawaii.

From this general observation, we shall discuss the five questions in the order presented.

Question No. 1

> If a local travel agent sells to persons in Hawaii tickets for surface or air transportation to points outside the state of Hawaii, is the local travel agent subject to the Hawaii general excise tax on the commissions earned for the sale of such tickets?

We are of the view that the local travel agent is subject to the Hawaii general excise tax on the commissions earned for the sale of tickets for surface or air transportation to points outside the state of Hawaii.

It is our understanding that the local travel agent, selling surface or air transportation at the same price that the airlines or steamship companies sell their tickets, retains a percentage of the price as his commissions. The question being raised is whether or not such commissions are taxable under the Hawaii general excise tax law.

The principal contention made against taxability is that under such circumstances as stated the Hawaii tax would be violative of Art. I, section 8 of the United States Constitution. 1/ The constitutional provision would invalidate the Hawaii tax if, under the circumstances stated above, said tax creates an undue or discriminatory burden on interstate commerce.

It is well settled that not every local tax that affects commerce is a regulation in the constitutional sense. As the Court in Nippert v. City of Richmond, 327 U.S. 416, 425 (1946) said:

> "As has been so often stated but nevertheless seems to require constant repetition, not all burdens upon commerce, but only undue or discriminatory ones are forbidden."

1/ Art. I, section 8 of the United States Constitution reads in part as follows: "The Congress shall have Power . . . To regulate Commerce . . . among the several States . . ."

Neither is it sufficient merely to determine whether or not interstate commerce is involved to resolve the constitutional problem presented. Central Greyhound Lines, Inc. v. Mealey 334 U.S. 653, 655 (1948). As Mr. Justice Stone stated in McGoldrick v. Berwind-White Coal Mining Co., 309 U.S. 33, 46-47 (1940):

> "Not all state taxation is to be condemned because, in some manner, it has an effect upon commerce between the states, and there are many forms of tax whose burdens, when distributed through the play of economic forces, affect interstate commerce, which nevertheless fall short of the regulation which the Constitution leaves to Congress." (Emphasis added.)

It is clear that if a local activity is so related to interstate commerce that it cannot be separated from it, the taxed local activity would create an undue burden on interstate commerce and thus fall within the interdiction of the Commerce Clause of the United States Constitution. Michigan-Wisconsin Pipe Line Co. v. Calvert, 347 U.S. 157, 166 (1954); Texas Transport Co. v. New Orleans, 264 U.S. 150 (1924). The Court in the Calvert case recognized that the local activity could be so integrated with interstate commerce that multiple taxation would result, thus stating what is considered to be the test for determining whether or not the taxation of a local activity creates an undue burden on interstate commerce:

> "And if a genuine separation of the taxed local activity from the interstate process is impossible, it is more likely that other states through which the commerce passes or into which it flows can with equal right impose a similar levy the goods, with the net effect of prejudicing or unduly burdening commerce." Id. at 166. (Emphasis added.)

The test that an activity or goods may be potentially subjected to multiple taxation, as stated in the quotation from the Calvert case, was modified in a recent case, General Motors Corp. v. Washington, 377 U.S. 436 (1964), to the extent that to defeat a state tax on the ground of multiple taxation the taxpayer must show actual, not merely potential, overlapping tax in some other state. In General Motors, the taxpayer claimed that the products taxed by the state of Washington and which were manufactured outside the state of

Washington were subject to an out-state license tax, measured by sales before shipment. Not being satisfied with the potential multiple burden test, the Court said that the taxpayer failed to show that there was actually a "burden upon interstate commerce in a constitutional sense."

Where the locally taxed activity is separate and distinct from the transportation and intercourse of an interstate character, as contra-distinguished from a locally taxed activity that is so related to interstate commerce that it cannot be separated from it, the local tax is not within the prohibition of the Commerce Clause "merely because in the ordinary course such interstate transaction is induced or occasioned by the business." Dept. of Treasury v. South Bend Tribune, N.E.2d 275 (Ind. 1939). In Albuquerque Broadcasting Co. v. Bureau of Revenue, 184 P.2d 416, 429 (N.M. 1947), the court stated:

> "If an intrastate incident is sufficiently disjoined from interstate commerce though indirectly a burden thereon, it may be a 'taxable event,' open to state taxation, if it does not discriminate against interstate commerce."

In Western Live Stock v. Bureau of Revenue, 303 U.S. 250 (1939), the Supreme Court of the United States recognized the multiple taxation test in upholding the New Mexico gross receipts tax. The taxpayer in Western Live Stock published a trade journal that had both advertisers and subscribers who lived out of the state of New Mexico. The question before the Court was whether or not the distribution of the trade journal interstate caused the gross receipts tax on the business of publishing the trade journal to be violative of the Commerce Clause. The Court held that the tax was not objectionable in that "The tax is not one which in form or substance can be repeated by other states in such manner as to lay an added burden on the interstate distribution of the magazine." Id. at 260. See also, Alaska v. Arctic Maid, 366 U.S. 199 (1961).

The New York court has held that the New York general business tax on business receipts derived from local activities performed by the taxpayer for domestic exporters, such activities as coordinating and expediting movement from inland points to ocean carriers, was valid as a tax on local activities. The test the court used was "whether plaintiff's local New York City activity [was] 'such an integral part of the interstate process, the flow of commerce, that it [could not] realistically be separated from it.'" Mohegan International

Corp. v. City of New York, 211 N.Y.S.2d 161, 163 (1961), cert. denied, 366 U.S. 764 (1961).

The Hawaii supreme court recently held in Re Taxes, Armstrong Perry, 46 Haw. 269 (1963), that the imposition of the Hawaii general excise tax on services rendered by the taxpayer in Hawaii, measured by the amount of commissions earned, was not violative of the Commerce Clause of the United States Constitution. In Armstrong Perry the commissions received by a manufacturer's representative domiciled in Hawaii for services rendered in obtaining local orders for the manufacturer's products were held taxable under the Hawaii general excise tax law. The imposition of the tax was attributable to the services rendered by the taxpayer.

From the foregoing cases, we conclude that the Hawaii general excise tax is applicable to the commissions earned by a travel agent doing business in Hawaii even though interstate commerce may be involved. The taxed local activity is separable from interstate commerce, and the Hawaii tax is being measured by the commissions earned while engaged in business in Hawaii. Thus, the Hawaii general excise tax is not violative of the Commerce Clause of the United States Constitution.

Question No. 2

> If a local travel agent sells to persons in Hawaii tours to points outside the state of Hawaii and sends its own tour director along with the tour group, is the local travel agent subject to the Hawaii general excise tax on the commissions, fees, or net return (after payment of hotel accommodations, transportation costs, and other related items) earned for the sale and conducting of such tours?

We are of the view that the local travel agent is subject to the Hawaii general excise tax for the commissions, fees, or net return (after payment of hotel accommodations, transportation costs, and other related items) earned for the sale and conducting of tours even where certain services are rendered outside of the state of Hawaii.

It should be noted that there may be instances where the local travel agent may merely sell a tour to a group

of persons in Hawaii and "wholesale" such a tour to a travel agent on the mainland, thus not sending his own tour conductor along with the tour group. Under such circumstances the reasoning found in the discussion under Question No. 1 would be applicable, and the Hawaii general excise tax would apply to the local travel agent.

A more difficult question is presented where certain services are rendered outside the state of Hawaii by the local travel agent. For example, if the local travel agent personally conducts the tour group in the mainland or in a foreign country, there may be raised the argument that the imposition of taxes for services rendered outside the state of Hawaii violates the Due Process Clause 2/ as well as the Commerce Clause of the United States Constitution.

That a state may exercise its taxing power only within its jurisdictional limits is clear. The Due Process Clause requires that a state may not impose a privilege tax upon "the exercise or enjoyment of a right or privilege in another state derived from the laws of that state and therein exercised and enjoyed." 51 Am.Jur. Taxation section 58. The privilege of engaging in business in the instant case is confined to the jurisdiction of the state of Hawaii. There is, therefore, no Due Process Clause violation.

We believe that the multiple taxation test should be sufficient to justify the imposition of the Hawaii general excise tax even where services are rendered outside the state of Hawaii by the taxpayer. It is difficult to conceive of a gross receipts or an equivalent type of tax being imposed upon a group of tourists traveling through the mainland. Therefore, it is quite reasonable to state that the Hawaii travel agent would not be subjected to a gross receipts or an equivalent type of tax in any other state while he is conducting the tour group throughout the different states of the United States. The great difficulty in the enforcement of any tax imposed upon a tour director traveling through a state, furthermore, decreases the possibility of multiple taxation.

On the strength of the cases cited under Question No. 1 showing the separate and distinct character of the travel agent's business from interstate commerce and on the basis

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2/ Art. XIV, Sec. 1. ". . . No State shall . . . deprive any person of life, liberty, or property, without due process of law . . ."

of the relative freedom from multiple taxation of the commissions, fees, or net return (after payment of hotel accommodations transportation costs, and other related items), we are of the opinion that the Hawaii general excise tax is applicable to the local travel agent even where certain services are rendered outside the state of Hawaii. Furthermore, although an argument can be made that these services rendered by a tour director outside the state of Hawaii constitute an important part of the total activities of the local travel agent, it should be borne in mind that the general excise tax is a tax imposed on the privilege of engaging in business in Hawaii. As the Court stated in Western Live Stock v. Bureau of Revenue, 303 U.S. 250, 258 (1938):

> ". . . the carrying on of a local business may be made the condition of state taxation, if it is distinct from interstate commerce, and the business of preparing, printing and publishing magazine advertising is peculiarly local and distinct from its circulation whether or not that circulation be interstate commerce."

The fact that services are rendered in aid of interstate movement of travelers does not diminish the significance of the separateness from interstate commerce of the travel agent's business. His business is to facilitate the free flow of travel both within the state and between the states. Nonetheless, the essential ingredients of the business operation is localized--his customers, sales and promotion work, personnel, and business offices.

Here, the locally taxed activity is separate and distinct from interstate commerce, although affecting interstate commerce, and that aspect of interstate commerce affected falls short of the regulation which the Constitution of the United States leaves to Congress. Furthermore, since there is little or no danger of multiple taxation in the present case, there is no likelihood of an undue burden being placed on interstate commerce. Therefore, we conclude that the local travel agent is subject to the Hawaii general excise tax for the commissions, fees, or net return (after payment of hotel accommodations, transportation costs, and other related items) earned for the sale and conducting of tours even where certain services are rendered outside the state of Hawaii.

Question No. 3

If a local Travel agent, receiving a tour group from a mainland travel agent, either conducts the local tour himself or refers the group to another local tour company, or else handles the arranging of hotel and other accomodations, is the local travel agent subject to the Hawaii general excise tax on the commissions or fees earned for the rendering of such services.

The question raised here is similar to that raised in Question No. 1 in that all the services rendered are in Hawaii by a travel agent doing business in Hawaii, although interstate commerce is involved. In this case, however, the local travel agent is on the destination side of the travel stream. This fact does not change the legal conclusion reached in Question No. 1.

It is our opinion that the local travel agent is subject to the Hawaii general excise tax on the commission or fees earned for the services rendered tourists on behalf of a mainland travel agent.

Question No. 4

If a person from the mainland, acting as a tour conductor, brings a tour group to Hawaii and then returns to the mainland, is such a person subject to the Hawaii general excise tax for the commissions, fees, or net return (after payment of hotel accommodations, transportation costs, and other related items) derived from the sale and conducting of these tours?

It is our opinion that a person from outside the state of Hawaii who comes to Hawaii conducting a tour group from the mainland United States and who then returns to the mainland United States is not subject to the Hawaii general excise tax.

Present here is the converse situation found in Question No. 2 where a local travel agent has a tour conductor traveling along with the tour group throughout the various states of the United States or through various foreign countries. Such services rendered by the tour conductor in the

various states outside of Hawaii constitute incidental services only to the principal business being done in Hawaii. Where incidental activities are rendered outside the state of Hawaii, there would be no need to apportion the gross receipts of a person doing business both within and without the state of Hawaii. Dravo Contracting Co. v. James, 114 F.2d 242 (4th Cir. 1940). It is doubtful, futhermore, that the state where the incidental services had been rendered would tax such services. Moreover, the Due Process Clause of the Federal Constitution prohibits state taxation of a privilege which is not within its jurisdiction. See 51 Am. Jur. Taxation § 61. In this case the privilege of doing business is being exercised outside the state of Hawaii, and that which is being done in Hawaii is in aid or furtherance of the business being done outside Hawaii. It should be noted that the kind of services rendered in Hawaii and the extent and degree to which these services are being rendered may change so that a tax imposed upon such activity may become a proper exercise of a state taxing power. See General Motors Corp. v. Washington, 377 U.S. 436 (1964). In the present case, however, we are assuming that tour parties from outside Hawaii, with a tour conductor from outside Hawaii, are but an incidental part of the principal business of the travel agent who is doing business outside the state of Hawaii. It is not our purpose to draw fine lines and delicate formulas because in passing upon the constitutionality of a state tax the Court is concerned "with its practical operation, not its definition or the precise form of descriptive words which may be applied to it." Lawrence. v. State Tax Commission, 286 U.S. 276, 280 (1932). The incidence of a gross receipts tax, should such a tax be imposed upon a tour director under the circumstances indicated in this question, would be upon the person doing business outside Hawaii. We believe that such would be the case although we are by no means suggesting a formula to be rigidly adhered to, for as the Court stated in Wisconsin v. J. C. Penney Co., 311 U.S. 435, 444 (1940):

> "The Constitution is not a formulary. It does not demand of states strict observance of rigid categories nor precision of technical phrasing in their exercise of the most basic power of government, that of taxation. For constitutional purposes the decisive issue turns on the operating incidence of a challenged tax. A state is free to pursue its own fiscal policies, unembarrassed by the Constitution, if by the

> practical operation of a tax the state has exerted its power in relation to opportunities which it has given, to protection which it has afforded, to benefits which it has conferred by the fact of being an orderly, civilized society."

Question No. 5

> If a local branch office of a mainland travel agency provides services to tourists in Hawaii who are members of tour groups originating in the mainland through the parent company's sales and promotional efforts, is the local branch office subject to the Hawaii general excise tax for all or portions of the commissions, fees, or net return (after payment of hotel accommodations, transportation costs, and other related items) earned by the parent company for the sale and conducting of these tours?

We are of the opinion that the branch operation in Hawaii of a mainland United States tour agency is subject to the Hawaii general excise tax on an apportioned basis. Our understanding is that the local branch office services the clients of the parent company on tour in Hawaii. It is not clear what kind of services are being rendered, although representation has been made that servicing of complaints is one of the functions of the local branch office. We believe that there is sufficient doing of business in Hawaii to subject the branch office to taxation on an apportioned basis.

Where a mainland-based firm does business in Hawaii through a branch office, such a firm is considered to be doing business both within and without the state of Hawaii and may come within the provisions of section 117-18, Revised Laws of Hawaii 1955, as amended, with reference to the imposition of the Hawaii general excise tax. It should be noted that the Hawaii statute recognizes that "if under the Constitution or laws of the United States the entire gross income of such person cannot be included in the measure of this tax, there shall be apportioned to the State and included in the measure of the tax that portion of the gross income which is derived from activities within the State, to the extent that such apportionment is required by the Constitution or laws of the United States." The Hawaii statute, in other words,

recognizes that apportionment is to take place where the entire gross income of a taxpayer doing business both within and without the state of Hawaii cannot be subjected to the Hawaii general excise tax. The factual situation presented in the question to which an opinion is requested does not involve the taxation of the entire gross receipts of the taxpayer doing business both within and without the state of Hawaii. On the contrary, only that portion of the business being done in Hawaii or the earnings that would be attributable to that portion is being made the measure of the Hawaii general excise tax. Therefore, it seems that the primary question is whether the locally taxed activity is so related to interstate commerce that multiple taxation can result. This is the question which the court faced in Detroit and Cleveland Navigation CO. v. Michigan Dept. of Revenue, 69 N.W.2d 832 (Mich. 1955), to which it stated at page 835:

> "A consideration of the foregoing and other authorities leads us to conclude that a tax based upon gross receipts is not valid, however apportioned, if the transaction taxed is essentially a part of, and inseparable from, interstate commerce. Where, however, the activity is deemed sufficiently 'local' in character, it may be subject to a tax if that tax is properly apportioned and allocated to prevent the imposition of a multiple burden, and is non-discriminatory. The primary inquiry concerns the relationship of the transaction taxed to interstate commerce. . . ."

Even without section 117-18, Revised Laws of Hawaii 1955, as amended, the local activity of a branch which is distinct and separable from interstate commerce should be taxable under the Hawaii general excise tax, and the cases discussed under Question No. 1 indicate so. See also General Motors Corp. v. Washington, 377 U.S. 436 (1964). Section 117-18 serves primarily to clarify the method of apportionment. The cases cited under Question No. 1 clearly show that if the locally taxed activity is separable from interstate commerce, even though such a local tax may constitute an indirect burden on interstate commerce, such a local tax is not violative of the Commerce Clause of the United States Constitution.

It is our view, therefore, that the local branch office of a mainland-based firm is subject to the Hawaii general excise tax for the business done in Hawaii. Section 117-18, Revised Laws of Hawaii 1955, as amended, should provide

adequate guidelines for the determination of the measure of the tax. Note, further, that the person who questions the apportionment formula has the burden of showing by "'clear and cogent evidence' that it results in extraterritorial values being taxed." Butler Brothers v. McColgan, 315 U.S. 501, 507 (1942).

Summary

On the basis of the foregoing, for each of the questions presented, we conclude and summarize as follows:

Question No. 1: If a local travel agent sells to persons in Hawaii tickets for surface or air transportation to points outside the state of Hawaii, is the local travel agent subject to the Hawaii general excise tax on the commissions earned for the sale of such tickets?

Answer: Yes.

Question No. 2: If a local travel agent sells to persons in Hawaii tours to points outside the state of Hawaii and sends its own tour director along with the tour group, is the local travel agent subject to the Hawaii general excise tax on the commissions, fees, or net return (after payment of hotel accommodations, transportation costs, and other related items) earned for the sale and conducting of such tours?

Answer: Yes.

Question No. 3: If a local travel agent, receiving a tour group from a mainland travel agent, either conducts the local tour himself or refers the group to another local tour company, or else handles the arranqing of hotel and other accommodations, is the local travel agent subject to the Hawaii general excise tax on the commissions or fees earned for the rendering of such services?

Answer: Yes.

Question No. 4: If a person from the mainland, acting as a tour conductor, brings a tour group to Hawaii and then returns to the mainland, is such a person subject to the

Hawaii general excise tax for the commissions, fees, or net return (after payment of hotel accommodations, transportation costs, and other related items) derived from the sale and conducting of these tours?

Answer: No.

Question No. 5: If a local branch office of a mainland travel agency provides services to tourists in Hawaii who are members of tour qroups originating in the mainland through the parent company's sales and promotional efforts, is the local branch office subject to the Hawaii general excise tax for all or portions of the commissions, fees, or net return (after payment of hotel accommodations, transportation costs, and other related items) earned by the parent company for the sale and conducting of these tours?

Answer: Yes.

Respectfully submitted,

Clifford I. Arinaga

CLIFFORD I. ARINAGA
Deputy Attorney General

APPROVED:

Bert T. Kobayashi

BERT T. KOBAYASHI
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