

December 15, 1927.

OPINION No. 1459.

TAXATION—INCOME TAX; DEDUCTION FOR LOSSES:

Under Section 1391, R. L. 1926, losses in business ventures in California, by a resident of that State, such ventures being in no way related to the source of such resident's income earned in Hawaii, derived from property located in Hawaii, are not deductible as losses incurred in trade or business.

Harold C. Hill, Esq.,  
Income Tax Assessor, First Division,  
Honolulu, T. H.

Dear Sir:

Under date of November 8th you submitted a request for my opinion on the following matter, namely:

Whether losses to income sustained by Mrs. Alice Campbell Macfarlane, a resident of California, in business ventures in that state, such ventures being in no way related to the source of her income from the Estate of James Campbell, deceased, Honolulu, can be deducted in determining the amount of taxable income derived from said property.

Section 1388, R. L. 1925, covers the income tax rates on profits and incomes received by persons residing within the Territory from all property owned, etc., in the Territory, and sets a schedule on the amounts so received.

Section 1391, R. L. 1925—Income, How Computed—provides that there shall be deducted "all losses actually sustained during the taxation period next preceding incurred in trade or arising from losses by fire not covered by insurance, or losses otherwise actually incurred."

The above provision, if taken in its widest sense, might include the loss or impairment of capital assets by such causes as bad investments, the bankruptcy of a debtor, the failure of a bank, the enforcement of one's liability as an indorser, and the like; but, bearing in mind the purpose of the statute—to impose a tax on incomes, not on property or, capital—and taking the context into consideration, it seems that a more restricted meaning should be given the above words. Apparently the legislative purpose was to include only those losses which are incident to the property owned or to the business out of which the taxable income was produced, or capital invested in that business or property, located within the Territory.

The intention of the legislature in this instance was to provide revenue for the government of the Territory irrespective of what taxes were paid to other governments. This intention would limit the reason for the exemptions (deductions) to losses actually incurred or sustained to profits or income derived from sources wholly within the Territory.

The U. S. Treasury Department has indicated its adoption of this view, as applied to analogous provisions of the Federal Income Tax Law (although I find nothing in point on our Territorial law):

See, generally, Black on Income Taxes, Sec. 304, p. 444; and U. S. Treasury Dept. Decision 2090, 1914.

In so far as the income of Mrs. Macfarlane in Hawaii was concerned, during the years 1924-1925, she actually incurred no losses to her property here or to income gained within the Territory. Any losses sustained by her in California, in business ventures entirely disconnected from property owned or business conducted in Hawaii, can not be deducted, for the purposes of determining the amount of tax payable on income derived from sources within the Territory—deductions should

be allowable only if and to the extent that losses are connected with income from property located here.

The income of Mrs. Macfarlane from property or sources other than in Hawaii is not an item of income for the purposes of our income tax law; therefore, the losses sustained by reason of business ventures not connected with the source of her income here are not deductions attributable to any item of income from sources here, and are not nor could they be required by local legislation to be reported for income tax purposes in this Territory.

If Mrs. Macfarlane is taxed only upon so much of her income as she received from property located in Hawaii, her allowable deductions are correspondingly restricted. Thus, "losses" must be "actually incurred" from business conducted in or property owned by her within the Territory of Hawaii.

I accordingly advise you that I concur in your views on this matter and in the action taken by you in disallowing deductions for losses sustained in ventures in California by a resident of that State for the purpose of computing income tax on income derived from property located in Hawaii.

Very truly yours,

WILLIAM B. LYMER,  
Attorney General.