

October 5, 1928.

## OPINION NO. 1506

## TAXATION — INCOME — EXEMPTIONS:

Property upon which Inheritance Tax is paid under Chapter 104, R. L. H. 1915, is not thereby exempted from Income Tax upon income derived therefrom in subsequent taxation periods.

Honorable Henry C. Hapai,  
Treasurer of Hawaii,  
Honolulu, T. H.

Sir:

Under date of September 14, 1928, you requested the opinion of this Department relative to the matters set forth in a letter to you from Mr. Henry Glass, Income Tax Assessor, under date of September 13, 1928, a copy of which letter you enclosed in your communication. As stated by Mr. Glass in his communication to you, and as further supplemented in an oral conference with the undersigned, the facts upon which you predicate your request are as follows:

Charles F. Hart, a domiciled resident of the Territory of Hawaii, died in 1910, leaving an estate which by the terms of his will passed to certain designated life tenants and remaindermen. Subsequently certain persons claiming to be the trustees of the property passing under the will filed a Petition in the Circuit Court of the Fourth Judicial Circuit, petitioning the court to change the scheme of the will and to authorize the transfer of the property held in trust to a corporation to be incorporated and known as the Niulii Mill and Plantation Company, Limited, the trustees to receive in return, 3,995 shares out of the total capital stock of 4,000 shares.

It is understood that this authority was granted by the Court and that the Niulii Mill and Plantation Company was thereafter duly incorporated and is now a going concern.

It is claimed by Theo. H. Davies & Company, Limited, agents for the Niulii Mill and Plantation Company, Limited, that income earned by the corporation is not taxable either to the corporation or to the life tenants, for the reason that an inheritance tax was paid on the property left by Charles F. Hart, which at the present time constitutes the major part of the property owned by the Niulii Mill and Plantation Company, Limited.

Section 1389, Revised Laws of Hawaii, 1925, as amended by Act 211, Session Laws of Hawaii, 1927, provides that corporations in the class of the Niulii Mill and Plantation Company, Limited, shall pay an income tax as therein provided. Section 1391, Revised Laws of Hawaii, 1925, provides that individuals returning income derived from stock held in Hawaiian corporations paying income tax under the aforesaid section, shall be entitled to a deduction in the amount of such income. The latter provision is undoubtedly intended to avoid the evil of double taxation.

Rules of statutory construction require that tax exemptions be construed strictly.

The exemption from income tax as claimed by the taxpayer cannot therefore be read into either section, the wording thereof being too explicit and clear to the contrary. It may be possible that the taxpayer relies upon that part of Section 1400, Chapter 104, Inheritance Tax, R. L. H. 1925, which provides as follows:

“All property so passing for which such exemption of Five Thousand Dollars (\$5,000.00) can be maintained, shall not be taxable as income under the provisions of any other law.”

and that part of Section 1391, R. L. H. 1925, providing that,

“In assessing the income of any person or corporation there shall not be included the amount received from any corporation as dividends upon the stock of such corporation if the tax of two per centum has been assessed upon the net profits of such corporation as required by this chapter, nor any bequest or inheritance otherwise taxed as such.”

These provisions, however, apply only to the return of such property as income, during the period the same was received, and do not under the rules of statutory construction give to the taxpayer an exemption of income derived thereafter from property subjected to the inheritance tax at the time of transfer. If such construction were possible a great part of the property in this jurisdiction would be exempt from income taxes. Clearly, the legislature did not intend such exemption.

In the instant case, the contention is emasculated by the interposition of a new and separate entity, viz. the Niulii Mill and Plantation Company, Limited, which entity is by fiction of the law considered independent and separate from the persons of its stockholders, and is subject to taxation as such separate and distinct entity. Likewise, any and all property held by it in its own right is to be considered the property of a separate and distinct entity and not the property of the stockholders. Whatever character may be given to the property when in the hands and control of persons paying an inheritance tax is lost when such property is transferred to a third person, in this case the Niulii Mill and Plantation Company, Limited.

You are therefore advised that any and all property passing to the life tenants and remaindermen under the terms of the will of Charles F. Hart, deceased, or by virtue of the intestate laws of the Territory of Hawaii, is subject to income tax when and where income is derived as such from such property subsequent to the taxation period when received, even though an inheritance tax has been paid upon the transfer thereof.

You are further advised that the Niulii Mill and

Plantation Company, Limited, is subject to the corporation income tax as provided for in Section 1389, supra, and that the stockholders thereof may claim deductions in individual returns as and for dividends paid by the corporation as provided for in Section 1391, supra.

Respectfully,  
H. T. KAY,  
First Deputy Attorney General.

APPROVED:

H. R. HEWITT,  
Attorney General.