January 25, 1939.

OPINION NO. 1688

INSURANCE COMPANIES; DUAL CAPACITY.

Where an insurance company carries on, in addition to its insurance business, an agency business as well, it operates under a dual capacity for the purposes of taxation.

TAXATION, GROSS INCOME; INSURANCE COMPANIES.

An insurance company which also operates as an agent of other insurance companies is taxable on its gross income from its agency business, notwithstanding Act 141, sec. 4. L. 1935.

TAXATION, NET INCOME; lNSURANCE COMPANIES.

An insurance company which also operates as an agent of other insurance companies is taxable on its net income from its agency business, notwithstanding Chapter 65, sec. 2031, R. L. 1935.

Honorable William Borthwick,
Tax Commissioner,
Territory of Hawaii,
Honolulu, T. H.

Sir:

This will acknowledge receipt of your letter of December 29, 1938. You state that Home Insurance Company is doing business both as an authorized insurance company engaged as a principal in the business of insurance, and also as the licensed agent of other insurance companies. (Sec. 6805, R. L. 1935.) For the first class of business it receives premiums and for the second class of business, commissions. You ask whether this company is liable to tax upon its commissions under Act 141, L. 1935 (Gross Income Tax) and Chapter 65, R. L. 1935 (Net Income Tax). You quote the following sections:

Act 141— *Section* 4 — *Exemptions* — "The provisions of this Act shall not apply to:

"(e) Insurance companies which pay the Territory of Hawaii a tax upon their gross premiums under the provisions of the Revised Laws of Hawaii 1935, Chapter 224;"

Chapter 65— Section 2031 —"Tax on corporations; exceptions. There shall be assessed, levied, collected and paid for each taxable year a tax of seven and one-half per centum upon the net income of every corporation doing business in or receiving or deriving income from sources within the Territory; provided, however, that all banks and insurance companies exclusively taxable under the provisions of other laws, and also all corporations, companies, associations or trusts conducted solely for charitable, religious, educational or scientific purposes, including fraternal beneficiary societies, shall not be taxable under this chapter."

I note that the company argues that the last paragraph of sec. 4 (1), Act 141, L. 1935, which provides:

"Provided, however, that the exemptions of this section 4 (1) shall apply only to the gross income of those persons enumerated in Section 4 (1) (f) to Section 4 (1) (i) both inclusive, from non-profit activities."

and sec. 4 (1) (c) of said Act which provides:

"Section 4. Exemptions. The provisions of this Act shall not apply to:
* * *

"(c) Public utilities (as that term is defined in the Revised Laws of Hawaii 1935, section 7940), with respect to their public utilities business, upon the gross income from which they pay an annual tax under the provisions of the Revised Laws of Hawaii 1935, chapter 69; * * *".

indicate an intent to exempt the commissions as well as the premiums, for purposes of the tax imposed by said Act 141. The company also argues that an ambiguity in a tax statute is strictly construed in favor of the taxpayer.

With respect to the last proposition it is enough to point out that this matter involves a claimed exemption and that exemptions from taxation are strictly construed against the exemption. *Re Taxes Henry A. White.* 33 Haw. 214, 218.

With respect to the last paragraph of section 4 (1) this of course was directed to the segregation of non-profit activities from other activities and was necessary for that purpose since in many instances the description of the exempt person was broad enough to cover profit activities as well as non-profit activities. The question here, however, is the question whether or not the description "insurance company" applies to this corporation when it is conducting the business of an insurance agent. The injustice of taxing a corporation which does solely an insurance agency business while

exempting its competitor doing an insurance agency business because it also does an insurance business, is apparent, and the question is whether the Legislature intended such a result.

With respect to the phraseology of section 4 (1) (c) as compared with section 4 (1) (e) it is apparent that the provisions of section 4 (1) (e) were adopted from the laws of West Virginia and Mississippi. The West Virginia act (Official Code of West Virginia, 1931, Ch. 11, Art. 13, as amended by 1st Sp. S. L. 1933, Ch. 33) provides in section 3:

"The provisions of this article shall not apply to: (a) Insurance companies which pay the state of West Virginia a tax upon premiums."

This provision is construed by the Attorney General of West Virginia as "applicable to an insurance company only so long as its business activities within the state are confined to the issuance of insurance, the collection of premiums therefor, and to such other activities as are necessary to be performed in order that the insurance business may be carried on by the company within the state". (Opinion dated April 21, 1937.)

The Mississippi Act (Gen. L. of Miss. 1934, Ch. 119, as amended) likewise provides in sec. 4:

"*Certain persons exempt from provisions*— There are, however, exempted from the provisions of this act:

"(a) Insurance companies which pay the state of Mississippi a tax upon premiums levied under the provisions of the laws of the State of Mississippi * * * ."

Neither of these acts exempts public utilities. In drafting section 4 (1) (c) the drafters perhaps used language more exact than the language used in section 4 (1) (e) and in the West Virginia and Mississippi acts, but the difference in phraseology does not indicate a difference in policy. The statement made by the company to the effect that a deliberate difference

was intended by the Legislature is not supported by anything in the House or Senate Journal. On the contrary sections 4 (1) (c) and 4 (1) (e) are the same as they stood in the original bill, Senate Bill No. 39, though then differently numbered. (Also the bill as originally introduced contained a comma before the word "which" in section 4 (1) (e).)

The common purpose of these two exemptions (sections 4 (1) (c) and 4 (1) (e)) plainly is to preserve the commutation of taxes previously provided by section 2140, R. L. 1935 (relating to Public Utilities) and section 6850, R. L. 1935 (relating to Insurance Companies). This is the same intention as is expressed in the above quoted section 2031 of Chapter 65, R. L. 1935, relating to net income tax. The real question is whether or not the taxpayer, *when doing an insurance agency business*, is an insurance company, within the meaning of section 6850, R. L. 1935 which provides that all insurance companies shall pay to the Treasurer taxes on certain gross premiums 'which taxes, when paid, shall be in settlement of all demands of taxes, licenses or fees of every character imposed by the laws of the Territory, excepting property taxes and the fees set forth in section 6849 for conducting the business of insurance in the Territory". This commutation of taxes, like an exemption, is subject to the rule of strict construction against the taxpayer. 2 Cooley on Taxation, 4th Ed., 1382, sec. 660. It is well settled that where an exemption from other taxes is granted in consideration of the imposition of a special tax, the exemption is to be interpreted in the light of the scope of application of the special tax. *Millers Mutual Fire Ins. Co. v. City of Austin*, 210 S. W. 825 (Texas, 1919).

The cases disclose two main lines of thought in defining an insurance company, (1) according to the powers in the company's charter and the law under which it is incorporated, and (2) according to the actual

activities of the company, which may include consideration of the question whether these activities are predominantly insurance business. (Note in 36 Columbia Law Review 456 [March 1936].) If the second method were used and a company were classified as an insurance company only when its activities were predominantly insurance business, it might be argued that the legislature intended each corporation to have only one classification, according to its principal activity, and that no company was intended to be classified in dual capacities. This is not the case, however, as will appear.

It has been decided that the tax imposed by section 6850, R. L. 1935, is a tax imposed for the privilege of doing an insurance business within the Territory. *Re Taxes C. Brewer & Co., Ltd.,* 23 Haw. 96. Consequently every company is an insurance company for the purposes of section 6850, R. L. 1935, which has received the privilege of doing an insurance business in the Territory. Section 6850, R. L. 1935 plainly contemplates classification according to the first method above, that is, according to the powers conferred; classification according to whether or not the activities of the company are predominantly insurance business has no relevancy whatsoever.

It is well recognized that when the rule of classification according to predominent characteristics does not apply, a taxpayer or his property may have dual capacities, one as an insurance company and the other another business, and it is sufficient that the tax applies to the other business. *National Savings and Loan Ass'n* v. *Gillis,* 35 F. (2d) 386, 391; *Fidelity and Casualty Co.* v. *Coulter,* 74 S. W. (Ky.) 1053 *(dictum).* Similarly, an exemption of a railroad company from taxation is to be construed as referring only to the property held for the transaction of the business of the railroad company as such, and does not apply to other property. *Ford* v. *Delta and Pine Land Co.,* 164 U. S. 662,41 L.

Ed. 590. Conversely a tax on all business of a fire insurance company has been held to apply only to business transacted by the fire insurance company as such and not to distinct lines of business, *St. Paul Fire and Marine Ins. Co.* v. *Lewis,* 144 Pac. (Kan.) 822; and a tax on an electric light company applies to the business transacted by the company by virtue of its authority as an electric light company and not to a distinct business, *Corn.* v. *Harrisburg Light and Power Co.,* 105 Atl. (Pa.) 80. These authorities all illustrate the same principle, namely, that an insurance company is only to be considered an insurance company when acting under its authority as an insurance company.

It is clear that the authority of an insurance company as such does not include the business of acting as an insurance agent. The statute recognizes that the privilege of acting as agent is a separate privilege, provides for the licensing of agents and imposes a separate fee therefor. (Secs. 6790, 6799, 6804-6807, 6849, R. L. 1935.)

In my opinion sec. 4 (1) (e) of Act 141, L. 1935, and sec. 2031 of Ch. 65, R. L. 1935, apply to the income of a company to the extent only that such income is derived by the company under its authority as an insurance company, and such sections do not apply to income derived by the company under its authority as an insurance agent.

Respectfully,

RHODA V. LEWIS,
Deputy Attorney General,

APPROVED:

J. V. HODGSON,
Attorney General.