

January 13, 1961

Honorable Earl W. Fase
Director of Taxation
State of Hawaii
Honolulu, Hawaii

Attention: Mr. John A. Bell
Deputy Director of Taxation

Dear Sir:

This is in response to your request for our advice with regard to whether the "blockage theory" is applicable in the valuation of large blocks of stocks under the Hawaii inheritance tax statute, Section 122-25, R.L.H. 1955, as amended. The pertinent portion of Section 122-25 reads as follows:

Sec. 122-25. Valuation. All property, the transfer of which is subject to tax under the provisions of this chapter, shall be appraised at its full cash value as of the date of death. Whenever, by reason of the provisions of this chapter, it becomes necessary to appraise or ascertain the value of any stocks, bonds or securities, such as are customarily bought or sold in open market in the city of Honolulu or elsewhere, the value of such stocks, bonds or securities shall be ascertained by taking the price for which such stocks, bonds or securities were bought and sold upon the date of death, or if there were no sales upon such day, then by ascertaining the range of the market and the average of prices as thus found running through a reasonable period of time before and after the date of death. . . .

The phrase "full cash value" found in our old ad valorem taxes statute, Civil Law, Section 820 and the phrase "fair and reasonable value" in Section 21, Act 40, 2d Sp. S.L. 1932 have been interpreted to be terms of like import. In Re Taxes B. P. Bishop Estate, 33 Haw. 149. Cases from other jurisdictions have held that "full cash value" is commonly construed to mean "fair market value". Kaiser Co. v. Reid,

184 P.2d 879; Rogan v. County Com'rs of Calvert County, 71 A.2d 47. Consequently it is reasonable to interpret the phrase "full cash value" found in Section 122-25 to mean fair and reasonable value or fair market value. It should be noted that the phrase "full cash value" is used in a general sense and refers to the valuation of all property. However a more specific method of valuation is set forth in the statute with regard to certain types of negotiable securities. In the case of stocks, a specific method of valuation is set forth in the second sentence of Section 122-25 which indicates that the value of stocks sold in the open market in Honolulu or elsewhere is ascertained by taking the price for which such stocks were bought and sold upon the date of death or if there were no sales on the date of death, then by ascertaining the range of the market and the average of prices through a reasonable period of time before and after the date of death. It is an old and familiar principle that where there is a specific provision and a general provision in the same statute, the specific provision must control, and the general provision must be taken to affect only such cases within its general language as are not within the provisions of the particular provision. 50 Am.Jur. § 367. Since the specific provision pertaining to the valuation of stocks prescribes the stock exchange price method to be utilized in arriving at its fair and reasonable value, the particular question involved is whether the "blockage theory" is permissible to be utilized in the present instance. The "blockage theory" in short is one which recognizes that a large block of stock may not be as readily liquidated as a few shares and thus resulting in a lower valuation of the large block of stocks if they were to be put on sale at a given date. 2 Paul, Federal Estate and Gift Taxation, Sec. 18.27 (1942).

There are numerous Hawaii cases which allowed the blockage theory to be applied under the old ad valorem taxes statute, Section 1320, R.L.H. 1925. See Re Taxes, Waialua Agricultural Company, Ltd., 30 Haw. 755; In re Taxes, Ewa Plantation Company, Ltd., 30 Haw. 775; Re Taxes, Consolidated Railway, Ltd., 32 Haw. 312. However, Section 1320, R.L.H. 1925 clearly provided within the statute that the market quotation as well as other facts and circumstances which reasonably and fairly reflected upon the valuation of the stocks were to be considered in the valuation method utilized. In our instant situation, there is no language in Section 122-25 which gives rise to the inclusion of "such other facts and circumstances" in the valuation of stocks for our inheritance tax purpose. Section 122-25 clearly states that where the stocks are of the kind that are traded on the open market, "the value of such stocks, bonds or securities shall be ascertained by taking the price for which such stocks, bonds or securities were bought

and sold upon the date of death." The averaging provision becomes applicable when no sales are found on the date of death. It is of particular significance to note that the amendment which added the stock valuation method for the first time in 1911 was accompanied by a Senate Judiciary Committee report of our Legislature, Report No.284 (The Sixth Legislature, Hawaii, Senate Journal 1911, pp. 893, 894) which stated that the purpose of the amendment was to provide "a more certain method of fixing the value of certain negotiable securities." In view of the certainty that our Legislature desired in amending our then existing statute, it appears as a matter of legislative intent that stocks be valued on the unit price basis prevailing on the stock market for inheritance tax purposes without regard to the number of stocks being held.

Case law from other jurisdictions have taken contrary positions on the adoption of the "blockage theory" for state inheritance tax purposes. If one were to adopt the Minnesota view, no "blockage theory" would be allowable. State v. Wagner, 46 N.W.2d 676 (1951). The Minnesota court feels that the "blockage theory" discriminates against beneficiaries of small estates which may be administered at about the same time as a large estate where the estates contain blocks of the same stock. The Wagner case also held that the Minnesota inheritance tax is imposed upon the privilege of receiving property rather than upon the privilege of transferring it and as such the "blockage theory" of the Federal estate tax statute which applies its tax on the privilege of transferring a decedent's property should not apply. As such the Minnesota court in the Wagner case states that because "our inheritance tax is imposed upon the value of what the beneficiary receives, there is as much reason to look to evidence of what the beneficiary would have to pay for the stock he receives as there is to look to evidence of what he might realize in money from selling it." Obviously the sudden demand for stocks would cause the market value of a stock to rise.

The Minnesota statute which was interpreted in the Wagner case as not allowing the use of the "blockage theory" when there is a market or sales value was worded in broader terminology than our Section 122-25. The pertinent statutory provisions of the Minnesota statute M.S.A. 291.23 read as follows:

"Every inheritance, . . . upon-which a tax is imposed under this chapter shall be appraised at its full and true value immediately upon the death of decedent, . . ."

Minnesota statute, M.S.A. 272.03, subd. 8 defined "full and true value" as follows:

"'Full and true value' means the usual selling price at the place where the property to which the term is applied shall be at the time of assessment; being the price which could be obtained at private sale and not at forced or auction sale."

Our inheritance tax statute, Section 122-25 which sets forth the stock exchange price method on the date of death is a much narrower valuation scheme than one worded in the manner of the Minnesota statutes quoted above which rely on such phrase as "the price which could be obtained at private sale and not at forced or auction sale."

The New Jersey view on the "blockage theory" is one which allows the consideration of the "blockage theory" among other relevant elements of valuation even in a situation when there is market or sale value established for a stock on a stock exchange. Newbery v. Walsh, 120 A.2d 242. However, the New Jersey view is one which does not permit consideration of the "blockage theory" as a dominant, decisive or exclusive criterion of taxable value. The Newbery case held that the application of the "blockage theory" must be supported by requisite proofs which "embrace information concerning such matters as the amount of the outstanding stock, the number of shareholders, the recorded number of shares traded in each week or month . . . , the favorable or unfavorable technical position of the company, the attractive or unattractive state and trend of the market etc., all of course within the reasonable proximity in point of time to the essential date." The New Jersey statute prescribed that the inheritance tax be computed upon the "clear market value" of the property transferred. R.S. 54:34-5, N.J.S.A. Here again the valuation method is couched in a broad phrase "clear market value" and not in the more specific stock exchange price method set forth in Section 122-25 of our inheritance tax statute.

There appears to be no Hawaii case which deals with the application of the "blockage theory" under our inheritance tax statute, Section 122-25, R.L.H. 1955, as amended. While the "blockage theory" was adopted in the application of the ad valorem taxes under Section 1320, R.L.H. 1925, which permitted the use of stock market quotation and other facts and circumstances which affected valuation, it should not be considered as controlling in the application of the inheritance

tax because the language of Section 122-25 does not include the liberality and breadth of the ad valorem tax statute.

In view of the clear and specific valuation method set forth in Section 122-25 which prescribes the ascertainment of valuation of stocks bought and sold in the city of Honolulu or elsewhere by taking the price for which such stocks were bought and sold upon the date of death or by use of the averaging method should there be no sales on the date of death, the tax office should adhere to the long established practice of assessing stocks for inheritance tax purposes at their unit sales price as quoted on the stock exchange. This advice adheres to the position stated in an opinion of the Attorney General of Hawaii dated October 24, 1934 pertaining to the same subject matter. No significant change in the law has transpired since the previous opinion and there appears to be no cogent reason to change our position in view of the evident legislative intent to provide certainty in the valuation of these negotiable securities prescribed in Section 122-25, R.L.H. 1955, as amended. See Senate Judiciary Committee Report No. 284, The Sixth Legislature Hawaii, Senate Journal 1911, pp. 893, 894.

In addition this office subscribes to the Minnesota view with regard to the application of the "blockage theory" in our inheritance tax statute primarily because it is compatible with the intent of our statute which prescribes certainty of the valuation method. The Hawaii inheritance tax statute, Section 122-25 is also a tax on the privilege of receiving as in the Minnesota statute and not a tax on the transfer of the decedent's property as applied by the Federal estate tax statute. See Chase v. Commissioner, 33 N.W.2d 706; see also In Re Madison's Estate, 159 P.2d 630. In Chase v. Commissioner, supra, at page 711, the Minnesota court clearly stated that under its inheritance tax statute, "the thing burdened is the right to receive. . . . With reference to the federal tax, a transfer and not a succession tax was used in Reinecke v. Northern Trust Co., 278 U.S. 339, 49 S.Ct. 123." The distinction is evidenced by the differentiation of the rates applied to the various classes of beneficiaries under Section 122-5, R.L.H. 1955 as amended, dependent on the legal relationship between the decedent and the beneficiaries. A spouse of the decedent is given an exemption of \$20,000 while a child is allowed an exemption of only \$5,000. Such a distinction in the privilege of exemption can only be justified by the legislative policy of granting a spouse a greater privilege of receiving a decedent's property. Consequently, it appears only reasonable to adopt the Minnesota view that the application of the inheritance tax on the privilege of receiving means that there is as much reason to look to evidence of what the beneficiary would have to pay for the stock

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he receives as there is to look to evidence of what he might realize in money from selling it. In addition, the valuation of large blocks of the same stock at a lesser value than a small lot of the same stock would involve a disregard of the uniformity or equality required in the assessment of like properties. Maqoun v. Illinois Trust & Savings, 170 U.S. 283; 51 Am. Jur. Sections 150, 153; see also Section 116-2.1(2), R.L.H. 1955, as amended.

Very truly yours,

/s/ Shuichi Miyasaki

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APPROVED:

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