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Op. No. 65-13

STATE OF HAWAII

DEPARTMENT OF THE ATTORNEY GENERAL

Honolulu, Hawaii 96813

April 21, 1965

The Honorable Philip P. Minn
Chairman, House Governmental Financing Committee
Iolani Palace
Honolulu, Hawaii

Dear Sir:

This opinion is in response to your letter of April 12, 1965, to the Attorney General in which you request his opinion as to "the various legal ramifications with reference to a prohibition against a visible pass-on of the general excise tax in various retail activities."

It is our opinion that legislation prohibiting the visible pass-on of the general excise tax from the seller to the buyer is legally valid. 47 Am. Jur., Sales and Use Taxes §§ 1 and 2. Such legislation will not affect the present practice of the application of Hawaii's General Excise Tax Law by the State Tax Office upon the gross receipts of a sale, including any portion attributable to tax. However, such legislation might likely result in a ruling by the Internal Revenue Service that a Hawaii taxpayer-consumer would not be permitted to deduct from his federal income tax return that amount now deductible for state sales taxes when such taxpayer-consumer itemizes his deductions.

Hawaii's General Excise Tax Law is silent as to whether the seller can pass on the general excise tax of a sale to the buyer and the Supreme Court of Hawaii has never been presented the question. However, the Circuit Court in Territory v. Sundstrom, Criminal No. 29707, December 10, 1957, ruled that Hawaii's General Excise Tax Law does not prohibit the pass-on of that tax from the seller to the buyer. The pass-on can be made either visibly as an additional item added on to the sale price or may be included in the sale price without separate identification. The matter of the "visible pass-on" of the tax is entirely a matter of contractual agreement between the seller and the buyer. (See General Excise Tax Memorandum No. 4, (Hawaii, July 5, 1957)).

Legislation prohibiting the visible pass-on of the general excise tax from the seller to the buyer will not affect

the present practice of the application of Hawaii's General Excise Tax Law by the State Tax Office upon the gross receipts of a sale, including any portion attributable to tax. The incidence of the tax is upon the seller and the Tax Office will look to the seller for the tax upon the seller's total gross receipts whether there is a visible pass-on or not. If the general excise tax is included in the sale price without separate identification, the amount subject to the tax is of course the listed sale price. If the tax is added to the listed sale price and is separately listed as the general excise tax, the total amount collected by the seller (which includes the amount stated as the general excise tax) shall be considered as the gross receipts of the seller and must be reported as taxable income. (See General Excise Tax Memorandum No. 4, supra.)

If the listed sale price includes the general excise tax without separate identification, the seller must comply with Section 117-14.6(d), Revised Laws of Hawaii 1955, as amended. That section provides that no retailer shall advertise or hold out to the public in any manner, directly or indirectly, that the tax imposed by Section 117-14.6 is not considered as an element in the price to be charged to the consumer and any person violating the provisions thereof may be fined an amount not exceeding $50.00 for each offense. Section 117-14.6(d) has been interpreted to mean that it is permissible for a seller to advertise or to hold out to the public that the listed sale price "includes the general excise tax" but it is not permissible for the seller to advertise or to hold out that the listed sale price is the total price "with no tax", thereby implying that no general excise tax will be charged at all. (See Memorandum dated February 24, 1958, from Rhoda V. Lewis, Deputy Attoryney General, to Jack H. Mizuha, Attorney General.)

The most serious consequence of legislation prohibiting the visible pass-on of the general excise tax entails the matter of whether or not a Hawaii taxpayer-consumer would be permitted to deduct from his federal income tax return that amount now deductible for state sales taxes when such taxpayer-consumer itemizes his deductions. We realize that such a ruling must come from the Internal Revenue Service itself. However, in the past the Internal Revenue Service has indicated that it would not allow Hawaii's general excise tax to be deducted from a Hawaii taxpayer-consumer's federal income tax return if Hawaii's general excise tax is not separately stated. (See letter dated July 26, 1957, from the Internal Revenue Service to Dr. Robert Kamins, Director of the Legislative Reference Bureau. Also letter dated

April 23, 1957, from Dr. Kamins to Rhoda V. Lewis, Deputy Attorney General.)

The requirement that a state general excise tax, such as Hawaii's, be separately stated in order that taxpayers may deduct the payment of such tax is found in Section 164(c) (1) of the 1954 Internal Revenue Code. That section relates to the deduction of retail sales taxes and gasoline taxes in computing taxable income. It provides that in the case of any State or local sales tax, if the amount of the tax is separately stated, then, to the extent that the amount is paid by the consumer (otherwise than in connection with the consumer's trade or business) to his seller, such amount shall be allowed as a deduction to the consumer as if it constituted a tax imposed on, and paid by, such consumer. (See Revenue Ruling 58-564, Internal Revenue Bulletin No. 47, (Nov. 24, 1958)).

Section 1.164-5 of the Income Tax Regulations, relating to the deductibility of State and local sales and gasoline taxes under Section 164 of the Code, provides in part, that the requirement that the amount of the tax must be separately stated will be deemed complied with where it clearly appears that at the time of sale to the consumer, the tax was added to the sales price and collected or charged as a separate item. The fact that, under the law imposing it, the incidence of such State or local tax does not fall on the consumer, is immaterial. (See Revenue Ruling 58-564, supra.)

It appears therefore that legislation prohibiting the visible pass-on of Hawaii's general excise tax from the seller to the buyer might not fulfill the requirement of Section 164(c) (1) of the 1954 Internal Revenue Code that the sale tax be separately stated and that as a result, a Hawaii taxpayer-consumer might not be permitted to deduct Hawaii's general excise tax from his federal income tax return.

To summarize, the legal ramifications arising from the enactment of legislation prohibiting the visible pass-on of Hawaii's general excise tax from the seller to the buyer and the conclusions applicable to such ramifications are: (1) that such legislation is legally valid, (2) that such legislation will not affect the present practice of the application of Hawaii's General Excise Tax Law by the State Tax Office upon the gross receipts of a sale, including any portion attributable to tax, and (3) that such legislation might result in the Internal Revenue Service ruling that a Hawaii taxpayer-consumer would not be permitted to

deduct from his federal income tax return that amount now deductible for state sales tax when such taxpayer-consumer itemizes his deductions.

Very truly yours,

/s/ Melvin K. Soong

Melvin K. Soong
Deputy Attorney General

Approved:

/s/ Bert T. Kobayashi

Bert T. Kobayashi
Attorney General