TAX FOUNDATION
OF HAWAII

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November 14, 2017

Rules Office
Hawaii Department of Taxation
830 Punchbowl Street, Room 221
Honolulu, HI 96813

Re: **Comments on Proposed Rules Relating to County Surcharge**

Ladies and Gentlemen:

The Notice of Public Hearing relating to these proposed rules states that the Department's intent is to simplify the county surcharge rules by deleting the requirement that the taxpayer have nexus with the county imposing the surcharge. We cannot agree with the fundamental premise of the rules.

I. Nexus

"Nexus" commonly refers to the requirement under the Commerce Clause of the U.S. Constitution that a person or entity have a substantial presence in the jurisdiction that is trying to tax it. *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992). The Hawaii Legislature has delegated the power to enact a surcharge on the GET and has prescribed standards and parameters for doing so, but the surcharge is imposed by county ordinance. *See* HRS § 248-2.6; Rev. Ord. of Honolulu §§ 6-60.1 to 6-60.3. Thus, although the county surcharge is administered by the Department, it *is not* a state tax, it is a county tax.

Courts in other states with local taxing jurisdictions have applied constitutional provisions to require nexus with the local jurisdiction imposing the challenged tax even when nexus is present with the state in which the local jurisdiction is located. *City of Los Angeles v. Shell Oil Co.*, 4 Cal. 3d 108, 119, 480 P.2d 953, 959-60, 93 Cal. Rptr. 1, 8, *cert. denied*, 404 U.S. 831 (1971); *Associated Dry Goods Corp. v. City of Arvada*, 197 Colo. 491, 593 P.2d 1375 (1979); *Dravo Corp. v. City of Tacoma*, 80 Wash. 2d 590, 496 P.2d 504 (1972). As will be seen from the discussion that follows, these holdings follow from due process and equal protection principles, both of which are mandated by the Hawaii Constitution, art. I, sec. 5. Thus, although the Hawaii Supreme Court apparently has not ruled on the issue, a demonstrable connection between the surcharging county and the prospective taxpayer should be necessary to satisfy constitutional requirements. Dispensing with the nexus requirement altogether is inappropriate and raises constitutional concerns.

Associated Dry Goods Corp. v. City of Arvada, 197 Colo. 491, 593 P.2d 1375 (1979), involved a taxpayer with a store in Denver that occasionally sold merchandise to residents of Arvada that either came to Denver or telephoned the Denver store. The Denver store had the merchandise delivered to Arvada residents either by common carrier, U.S. mail, or company-owned trucks. The City of Arvada sought to require the taxpayer to collect city use tax on the merchandise sold to Arvada residents. The Supreme Court of Colorado held that due process required a nexus between the taxing jurisdiction (the City of Arvada) and the taxpayer, and that the delivery of merchandise to the city, without any selling activities taking place within the city, did not establish nexus. The City unsuccessfully argued that nexus was not required because the taxpayer admittedly had nexus with the State of Colorado.

In *Dravo Corp. v. City of Tacoma*, 80 Wash. 2d 590, 496 P.2d 504 (1972), the taxpayer contracted with the City of Tacoma to build a dam on land it acquired in Lewis County. The City imposed its business and occupations tax ("B&O tax") on the taxpayer's gross income from the contract, and the taxpayer paid the tax and sought a refund, claiming that the tax was unconstitutional because it was on activity in the State but outside the City. The court emphasized that "the city has no power either to authorize, license, or tax activities beyond its territorial limits," but held that the activities of negotiating and executing the contract occurred within Tacoma and gave the city the requisite nexus to impose its B&O tax. None of the court's reasoning would have been necessary if it were willing to hold that the taxpayer's nexus with the State satisfied any requirement that there be nexus with any taxing locality.

In *City of Los Angeles v. Shell Oil Co.*, 4 Cal. 3d 108, 480 P.2d 953, 93 Cal. Rptr. 1, *cert. denied*, 404 U.S. 831 (1971), the City sought to tax the gross income from selling petroleum products without apportionment as long as the products were shipped from a bulk terminal in the City. The taxpayer contended that apportionment was required to properly reflect selling activity in the City. The court, pointing to two cases from the 1950's, *City of Los Angeles v. Belridge Oil Co.*, 42 Cal. 2d 283, 271 P.2d 5 (1954), and *City of Los Angeles v. Belridge Oil Co.*, 48 Cal. 2d 320, 309 P.2d 417 (1957), reiterated that the City could constitutionally measure its business tax as to persons engaged in selling by reference to gross receipts attributable to selling within the City, even though various events outside the City contributed to those gross receipts; however, gross receipts attributable to selling activities conducted outside the city should not be included. *Id.* at 113, 480 P.2d at 955, 93 Cal. Rptr. at 3-4. The court noted that the California Constitution did not contain a provision like the Commerce Clause of the U.S. Constitution, but other provisions in the state and federal constitutions, such as equal protection, forbade unapportioned or improperly apportioned taxes on intercity business. *Id.* at 119 & n.8, 480 P.2d at 599-60 & n.8, 93 Cal. Rptr. at 8 & n.8. The court agreed with the taxpayer and held that the tax was not properly apportioned. One corollary of the court's reasoning is that a taxpayer must have taxable activity in the jurisdiction seeking to tax income from that activity before the tax can be sustained.

II. Allowable Apportionment Methodology Standard

In several of the existing rules, the Department allowed for the use of "any reasonable allocation method that clearly, fairly, and properly reflects the gross income to the appropriate taxation district;

provided that the allocation method is documented." The proposed rules replace every occurrence of that standard with a standard like this:

> (b) If services are used or consumed in more than one taxation district, gross income shall be allocated using any reasonable method; provided that the method is consistently used by the taxpayer and supported by verifiable data that reasonably quantifies the proportionate benefit received by each taxation district.

Proposed § 18-237-8.6-03(b). To harmonize this language with that of the exported services rules being held concurrently, we suggest that "by each taxation district" be changed to "in each taxation district."

We also urge the Department to act on our other comments contained in our letter of September 12, 2017, a copy of which is attached for ease of reference.

Thank you for the opportunity to submit comments.

Very truly yours,

Thomas Yamachika

Thomas Yamachika
President

Encl.: Copy of *Associated Dry Goods Corp. v. City of Arvada*, 197 Colo. 491, 593 P.2d 1375 (1979)
Copy of *Dravo Corp. v. City of Tacoma*, 80 Wash. 2d 590, 496 P.2d 504 (1972)
Copy of *City of Los Angeles v. Shell Oil Co.*, 4 Cal. 3d 108, 480 P.2d 953, 93 Cal. Rptr. 1
Letter of September 12, 2017

Page 1375

593 P.2d 1375
197 Colo. 491
ASSOCIATED DRY GOODS CORPORATION, d/b/a the Denver Dry Goods Company, a Virginia Corporation, Plaintiff-Appellant,
v.
CITY OF ARVADA, Colorado, a Municipal Corporation, Don M. Harwell, and S. W. Tanner, Defendants-Appellees.
No. 28314.
Supreme Court of Colorado, En Banc.
May 7, 1979.

[197 Colo. 492] Holland & Hart, Jay W. Tracey, Jr., Michael D. Martin, R. Alan Poe, Denver, for plaintiff-appellant.

Benjamin P. King, Jr., Deputy City Atty., Arvada, for defendants-appellees.

ROVIRA, Justice.

Associated Dry Goods Corporation, a Virginia corporation d/b/a The Denver Dry Goods Company (The Denver), sought review, pursuant to C.R.C.P. 106(a)(4), against the City of Arvada (City), a municipal corporation; Don M. Harwell, Hearing Officer; and S. W. Tanner, Treasurer, of an order of Harwell that The Denver was doing business in Arvada and requiring The Denver to obtain a use tax license from Arvada and collect use tax for the City.

The district court entered a judgment in favor of the defendants, and The Denver appealed to the Colorado Court of Appeals. The case was transferred to this court pursuant to section 13-4-110(3), C.R.S. 1973, because the constitutionality of the city ordinance was being challenged. We reverse.

The Denver is engaged in the business of selling merchandise at retail through several branch stores located in the Denver metropolitan area. None of these stores are located in the City of Arvada.

Through its various stores, The Denver sells merchandise to customers who reside in many parts of the state. These sales of merchandise take place at The Denver's stores, and the purchasers ordinarily take

Page 1376

the merchandise with them when they leave the stores.

Some purchasers request that the merchandise that they have purchased be delivered to them at their residences. In such cases, The Denver delivers the merchandise to the purchaser through its own delivery trucks and employees or arranges to have the merchandise delivered by common carrier or through the United States Mail.

In 1977 The Denver was served with a notice from the defendant Harwell that a hearing had been scheduled for the purpose of determining whether The Denver was engaged in business within the City of Arvada pursuant to Arvada Use Tax Ordinance 1336, section 9-19(b)(3), Code of the City of Arvada. [1] The Denver and the City entered into a stipulation of facts which provided as follows:

[197 Colo. 493] (1) The Denver Dry Goods Company (The Denver) does not directly, indirectly or by a subsidiary maintain an office, sales room, warehouse or other place of business within the City of Arvada.

(2) The Denver does not specifically solicit business from persons residing in the City of Arvada.

(3) The Denver does sell merchandise to residents of Arvada at its stores outside of the City of Arvada.

(4) The Denver does occasionally arrange for merchandise purchased outside of the City of Arvada to be delivered to purchasers in the City of Arvada either by parcel post or by common carrier.

(5) The Denver has in the past delivered merchandise purchased outside the City of Arvada to purchasers in the City of Arvada through the use of its own delivery trucks and employees.

(6) Specifically, on April 22, 1977, The Denver delivered merchandise purchased outside the City of Arvada to 6185 West 61st Avenue, Arvada, Colorado, through the use of its own delivery truck and employees.

Harwell entered an order which provided that in all cases in which The Denver delivered merchandise within the City of Arvada through the use of its own employees or vehicles, or where The Denver arranged delivery of merchandise through common carrier or United States Mail, The Denver was engaged in business within the City of Arvada pursuant to section 9-19 of the Code of the City of Arvada. The order required The Denver to either cease the activities which were found to constitute doing business or obtain a use tax license and begin collecting a use tax for the City.

The Denver appealed the order of the hearing officer to the trial court contending that the Arvada Use Tax Ordinance was unconstitutional as applied to its business operations.

The trial court entered its order on May 9, 1978, and concluded that where deliveries were made in Arvada by employees of The Denver that section 9-19(b) (3) of the City Code of Arvada was applicable. The trial court further held that, since The Denver had established itself as doing business in Arvada, all deliveries made by The Denver, whether by agent, parcel post, common carrier or by other means, are subject to the Arvada Use Tax.

[197 Colo. 494] I.

The issue presented by the facts of this case is whether The Denver is subject to the Arvada Use Tax by reason of its delivery of goods, purchased outside the City by Arvada residents, to those residents within the City. Stated another way, may

Page 1377

Arvada constitutionally impose a use tax collection liability on The Denver, under the facts as stipulated by the parties?

The Denver argues that section 9-19(b)(3), as applied, violates the due process clause of the Fourteenth Amendment to the United States Constitution, U.S.Const. Amend. XIV, § 1, and Colo. Const. Art. II, Sec. 25.

An analysis of the cases which have considered whether a vendor, by its acts or course of dealing, has subjected itself to the taxing power of a jurisdiction leads to the conclusion that due process requires some link or nexus, some minimum connection between a taxing jurisdiction and the person or transaction it seeks to tax.

In Miller Brothers Co. v. Maryland, 347 U.S. 340, 74 S.Ct. 535, 98 L.Ed. 744 (1954), Maryland attempted to require a merchant in Delaware to collect a Maryland use tax on sales to Maryland residents. The Delaware merchant delivered purchases by its own vehicles to Maryland locations and by common carrier delivery to Maryland addresses. The United States Supreme Court held that while the inhabitants of Maryland incurred a liability for the use tax when they used, stored or consumed the goods in Maryland, the burden of collecting or paying their tax could not be shifted to the Delaware merchant "in the absence of some jurisdictional basis not present here." 340 U.S. at 347, 74 S.Ct. at 540.

The City concedes that with respect to interstate commerce, federal due process requires some minimum connection in order for a state to require a non-resident vendor to collect a use tax on sales to residents of that state. Further, it admits that, where the vendor's only contact with the state and its residents is through mail and common carrier, there is not sufficient nexus to require the vendor to collect a use tax.

The City's position is that any contact above and beyond mail and common carrier will establish the minimum connection or nexus to support taxation. National Geographic Society v. California, 430 U.S. 551, 97 S.Ct. 1386, 51 L.Ed.2d 631 (1977); Scripto v. Carson, 362 U.S. 207, 80 S.Ct. 619, 4 L.Ed.2d 660 (1960); Standard Pressed Steel v. Department of Revenue of Washington, 419 U.S. 560, 95 S.Ct. 706, 42 L.Ed.2d 719 (1975).

The cases relied upon by the City reflect that the vendor had greater contact with the taxing jurisdiction than is present here. In National Geographic, supra, the vendor maintained an office and employees in California to solicit advertising, and the court concluded that such activities provided sufficient nexus as required by the due process [197 Colo. 495] clause of the Fourteenth Amendment and the Commerce Clause to support the imposition of a use tax collection liability.

In Scripto v. Carson, supra, the vendor had ten independent contractors (salesmen) soliciting in the state, and in Standard Pressed Steel v. Department of Revenue of Washington, supra, which involved a gross receipts tax, the vendor sent its engineer to live in the state of Washington to assist the purchaser in the use of its products and to maintain good will.

We believe, as did the Miller Brothers court, that "there is a wide gulf between this type of active and aggressive operation within a taxing state and the occasional delivery of goods sold at an out-of-state store with no solicitation other than the incidental effects of general advertising."

We do not agree that the use by The Denver of its vehicles and employees to deliver goods sold to Arvada residents establishes that it is doing business in Arvada and therefore is subject to the use tax ordinance of that city. [2]

Such a holding is in accord with this court's prior views concerning municipal taxation. In considering the "occupational

Page 1378

tax" imposed by the City and County of Denver, we held it to be permissible when applied to persons working at business establishments within the city limits. Denver v. Duffy Storage and Moving Company, 168 Colo. 91, 450 P.2d 339 (1969), but unconstitutional when applied to persons who merely traveled in Denver but conducted their business at a federal enclave not within the jurisdiction of the municipality. Johnson v. Denver, 186 Colo. 398, 527 P.2d 883 (1974). The standard set forth in those cases is that the taxpayer must be engaged in a business having a fixed or transitory situs in the taxing jurisdiction. Cf. Englewood v. Wright, 147 Colo. 537, 364 P.2d 569 (1961).

A similar standard is utilized by the Supreme Court of California in addressing issues analogous to the one in the instant case. That court has repeatedly held that local taxes can be imposed on sales which culminate in delivery within the municipality only to the extent that selling activities occur within the city. Delivery alone is an insufficient nexus. City of Los Angeles v. Belridge Oil Company, 48 Cal.2d 320, 309 P.2d 417 (1957); City of Los Angeles v. Shell

Oil Company, 4 Cal.3d 108, 93 Cal.Rptr. 1, 480 P.2d 953 (1971).

II.

In the alternative, the City argues that the due process analysis utilized by the United States Supreme Court in Miller Brothers, supra, is inapplicable to the inter-city delivery in this case. The basis for this [197 Colo. 496] contention is that both the city where The Denver is located and Arvada, where delivery occurred, are subdivisions of the state, which has intervened and defined the power to tax to include the tax imposed by Arvada in this case by the enactment and subsequent amendment of section 29-2-105(1)(b), C.R.S. 1973 (1977 Repl. Vol. 12).

Arvada relies principally upon the 1977 amendment to the statute, Colo.Sess.Laws 1977, ch. 389, 29-2-105 at 1398, for the proposition that the sale should be considered to have occurred at the place of delivery, therefore justifying Arvada's taxation of the transaction.

We note at the outset the long-standing rule of statutory construction in this state that taxing powers and taxing acts will not be extended beyond the clear import of the language used, nor will their operation be enlarged by analogy. Bedford v. Johnson, 102 Colo. 203, 78 P.2d 373 (1938); Rocky Mountain Prestress, Inc. v. Johnson, 194 Colo. 560, 574 P.2d 88 (1978). All doubts will be construed against the government and in favor of the taxpayer. City of Denver v. Sweet, 138 Colo. 41, 329 P.2d 441 (1958); Rocky Mountain Prestress, Inc., supra.

The Colorado constitution gives a home rule city the authority to impose an exercise tax on the use, storage or consumption of tangible personal property as it deems appropriate, so long as it is a matter of purely local concern. Colo. Const. Art. XX, Sec. 6; Berman v. City and County of Denver, 156 Colo. 538, 400 P.2d 434 (1965).

By the enactment of article 2 of title 29, C.R.S. 1973, the legislature granted incorporated towns, cities, and counties the authority to impose a use tax, but only on "construction and building materials and motor and other vehicles on which registration is required." Section 29-2-109(1), C.R.S. 1973. Of course, a home rule city has all the powers granted by statute to incorporated municipalities unless expressly restricted by its charter. Colo. Const. Art. XX, Sec. 6. As such, if the merchandise delivered by The Denver was within the scope of section 29-2-109, C.R.S. 1973, the City could invoke the provisions of section 29-2-105, C.R.S. 1973, to attempt to circumvent the due process analysis of Miller Brothers, supra. [3]

However, section 29-2-109, C.R.S. 1973, does not address the imposition of a use tax

Page 1379

on the merchandise which was sold by The Denver.

Because article 2 of title 29, C.R.S. 1973, does not expand the power of the City of Arvada to impose a use tax under the facts of this case, the City has not successfully invoked any provision thereof to circumvent the due process principles of Miller Brothers, supra. The constitutional analysis[197 Colo. 497] utilized there resolves the intercity tax scheme in this case just as it governed the interstate tax policies in that case. As explained above, delivery alone is an insufficient nexus for the inclusion of The Denver in the municipal use tax scheme of the City of Arvada.

The judgment of the district court is therefore reversed.

CARRIGAN, J., does not participate.

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1 Section 9-19

"b. For purposes of this section, a non-resident vendor engages in business in the City of Arvada when selling, leasing, delivering or conducting any activity in connection therewith in the City of Arvada for the use, storage, consumption or distribution within the City of Arvada. This term shall include, but not be limited to:

"(3) Delivery in the City of Arvada by a non-resident vendor or his agent, of goods purchased outside the City by a resident of the City of Arvada."

2 Because delivery by employees is not a sufficient nexus on which to base this municipal tax, A fortiori, delivery by mail or by common carrier is not a sufficient connection. National Bellas Hess v. Illinois, 386 U.S. 753, 87 S.Ct. 1389, 18 L.Ed.2d 505 (1967).

3 This is not to say that section 29-2-105, C.R.S. 1973, would allow the imposition of the use tax if the property subject to taxation were either building material or a motor vehicle. We do not reach the merits of the City's statutory analysis of section 29-2-105, C.R.S. 1973, because the applicability of that section is precluded in this case by section 29-2-109, C.R.S. 1973.

Page 1

93 Cal.Rptr. 1
4 Cal.3d 108, 480 P.2d 953
CITY OF LOS ANGELES, Plaintiff and Respondent,
v.
SHELL OIL COMPANY, Defendant and Appellant.
L.A. 29670.
Supreme Court of California,
In Bank.
Feb. 22, 1971.
Rehearing Denied March 26, 1971.

Page 2

[4 Cal.3d 111] McCutchen, Black, Verleger & Shea, G. William Shea, Franklin H. Wilson and Frank A. Caput, Los Angeles, for defendant and appellant.

[480 P.2d 954] Roger Arnebergh, City Atty., Bourke Jones and James A. Doherty, Asst. City Attys., for plaintiff and respondent.

SULLIVAN, Justice.

Defendant Shell Oil Company (Shell) appeals from a judgment, entered after a nonjury trial, awarding plaintiff City of Los Angeles (the City) the sum of $57,103.27 as a deficiency of business license taxes levied against Shell by the City for the years 1958--1961.

Shell is a large oil company which operates throughout the United States. Its headquarters are in New York, and its marketing activities are carried on through a network of regional, division, and district offices.

Among the facilities maintained by Shell in Los Angeles are a 'division office' and a 'bulk terminal.' The division office is a general sales and marketing headquarters subordinate in the company hierarchy to the San Francisco 'regional office' and superior to the various 'district offices' located within the division--which includes areas outside the City itself. The bulk terminal is essentially a storage depot which is fed by pipeline from the out-of-city Wilmington refinery.

Among the functions of the division office is that of supervising wholesale sales of gasoline to retail service stations located in the districts which comprise the division. The gasoline so sold is delivered to the customer either directly from the Wilmington refinery or by truck from the Los Angeles bulk terminal. Deliveries of each kind are made to both in-city and out-of-city customers. [1]

Pursuant to the Los Angeles Municipal Code (hereafter L.A.M.C.) the City levied an assessment against Shell for unpaid business license taxes for the years 1958--1961, inclusive. After administrative hearings Shell paid a portion of the assessment and agreed to the validity of certain other portions of the City's claim relating to deliveries made to in-city customers. [4 Cal.3d 112] Remaining in controversy were, generally speaking, those portions of the alleged deficiency relating to both refinery and bulk terminal deliveries to out-of-city customers. When the Los Angeles Board of Review upheld the City's position on these matters, and Shell refused to pay the deficiency, the City commenced the present action. Judgment was entered in favor of the City, and this appeal followed.

Shell on this appeal no longer resists that portion of the alleged deficiency relating to sales of gasoline delivered from the Wilmington refinery directly to out-of-city wholesale and retail customers. Thus the only part of the assessment remaining in controversy is that relating to wholesale sales of gasoline delivered from Shell's incity bulk terminal to retailers outside the City. The City seeks to base the tax upon Shell's total gross receipts from such sales; Shell contends that the tax can be based only upon that portion of such gross receipts attributable to its selling activities within the City.

I

Preliminarily we set forth certain provisions of the Los Angeles Municipal Code

Page 3

applicable to the assessment here involved and a tax ruling of the City interpreting them. We also refer to pertinent decisions of this court relating to the code provisions.

L.A.M.C. section 21.03, subdivision (a), provided: '(a) Subject to the provisions of this Article, a business tax registration certificate must be obtained and a business tax must be paid by every person engaged in any of the businesses or occupations specified in Sections 21.50 to 21.198, inclusive, of this Article; and a business tax is hereby imposed in the amount prescribed in the [480 P.2d 955] applicable section. No person shall engage in any business or occupation subject to tax under the provisions of this Article without obtaining a registration certificate and paying the tax required thereunder.'

L.A.M.C. section 21.166 provided: '(a) Every person Manufacturing and selling any goods, wares or merchandise at Wholesale, or Selling any goods, wares or merchandise at Wholesale, and not otherwise specifically taxed by other provisions of this Article, [2] shall pay for each calendar year or portion thereof the sum of $8.00 for the first $20,000 or less of gross receipts, and, in addition thereto, the sum of 40 cents per year for each additional $1,000 of gross receipts or fractional part thereof in excess of $20,000; * * * (b) For the purpose of this section, a wholesale sale or sale at wholesale means a sale of goods, wares or merchandise for the [4 Cal.3d 113] purpose of resale in the regular course of business.' (Italics added.) Effective January 1, 1960, the rate of tax was increased.

In 1954 and 1957 this court held in the Belridge cases (City of Los Angeles v. Belridge Oil Co. (1954) 42 Cal.2d 823, 271 P.2d 5, and (1957) 48 Cal.2d 320, 309 P.2d 417) that although the City could constitutionally measure its business tax as to persons engaged in 'selling' by reference to gross receipts arising from transactions having certain 'extraterritorial elements,' only those gross receipts which were 'directly attributable' to selling activities within the City could constitutionally be utilized for this purpose.

In those cases the products sold never entered the territorial limits of the City, but the main office of the defendant company was located in Los Angeles and substantial elements of its sales activity took place there. (See 42 Cal.2d at pp. 825--826, 271 P.2d 5.) It was argued on the first appeal that the City could not constitutionally base its business tax upon the gross receipts of the company because to do so would be to impose a tax on business carried on outside the City, but we concluded that the tax was based on the activity of 'selling' within the Clty and that there was 'no (constitutional) objection to basing the rate of such tax on the gross receipts attributable to such selling activities, even though various extraterritorial events contribute to such gross receipts.' (42 Cal.2d at p. 831, 271 P.2d at p. 10.)

However, we went on to express an important corollary to this principle: '(E) ven though the city can tax the activity of selling it can only base the tax on such selling activities as are carried out within its territorial limits. For this reason it is only those gross receipts which are attributable to selling activities within the city which should form the basis for the rate of tax. Gross receipts attributable to selling activities conducted outside the city, should not be included.' (42 Cal.2d at pp. 831--832, 271 P.2d at pp. 10--11.) We pointed out that if the tax were to be based upon gross receipts attributable to selling activities outside the city, 'it would unjustly discriminate against those firms whose selling activities in Los Angeles compose but a small fraction of the total sales effort and whose gross receipts are in large part attributable to selling activities in other areas.' (42 Cal.2d at p. 832, 271 P.2d at p. 11.) Thus, we concluded, 'a just and reasonable construction (of the L.A.M.C. sections in question) requires that the measure of the tax be limited to those

Page 4

gross receipts attributable to selling activities within the City of Los Angeles.' (42 Cal.2d at p. 833, 271 P.2d at p. 11.)

On retrial the parties in Belridge were confronted with the problem of determining which of the company's gross receipts were in fact 'attributable' to in-city selling activities within the meaning of our [480 P.2d 956] opinion. That the parties found this task a difficult one is manifested by the fact that [4 Cal.3d 114] they finally entered into a stipulation providing in substance that All of the defendant company's gross receipts were attributable 'in part' to its selling activities within the City and 'in part' to its selling activities without the City, but that not more than 20 percent of its gross receipts were attributable to the defendant's selling activities within the City 'under any method of allocation which is fairly calculated to determine the defendant's gross receipts derived from or attributable to sources within the City * * * and to determine the defendant's gross receipts derived from or attributable to sources outside the City * * *.' (City of Los Angeles v. Belridge Oil Co., Supra, 48 Cal.2d 320, 321, 309 P.2d 417.) The stipulation also reserved the City's right to maintain on appeal 'that there should be no allocation of receipts * * * and that the tax should be measured by defendant's total gross receipts.' (48 Cal.2d at p. 322, 309 P.2d at pp. 417--418.) The trial court held in essence that the matter of 'attribution' should be determined under a 'fair' method of allocation such as that reflected in the stipulation of the parties and that therefore the tax should be based on 20 percent of total gross receipts.

On appeal the City pressed the argument which it had reserved in the stipulation, to wit, that the first Belridge decision did not require an allocation of defendant's gross receipts but permitted taxation based on total gross receipts. In our opinion we pointed out that this argument misinterpreted the principle of the first Belridge decision by failing to give sufficient consideration to that aspect of the principle represented by what we have termed the 'corollary' thereto. In essence we reiterated that although a tax upon a 'selling' business may be measured by reference to gross receipts derived from transactions having 'extraterritorial elements,' only those gross receipts 'attributable' to incity selling activities could be considered. We concluded: 'Having heretofore held that only that portion of the gross receipts directly [3] attributable to defendant's selling activities carried on in the city of Los Angeles may be taxed under section 21.166, and the parties having stipulated that by a method of allocation 'fairly calculated to determine the defendant's gross receipts' 20% Thereof was derived from selling activities in the city of Los Angeles, we conclude that the trial court was correct in applying the tax formula to 20% Of defendant's gross receipts.' (48 Cal.2d at p. 324, 309 P.2d at p. 419.)

Following the Belridge decisions the city clerk, pursuant to authority granted him in the municipal code, [4] adopted Ruling 14. Part I of the [4 Cal.3d 115] Ruling, which set forth substantive guidelines for the determination of 'direct attribution' within the meaning of the Belridge cases, will be discussed below. Part II of the Ruling undertakes to give reasons why the adopted guidelines had been considered necessary or appropriate. Here it was stated that the Ruling was promulgated by reason of the Belridge decisions, 'which have made it necessary to devise a method by which the measure of

Page 5

the tax imposed upon persons who are engaged in certain taxable businesses both within and outside of the City of Los Angeles can be determined.' It is also explained that the formula prescribed in [480 P.2d 957] the Ruling was selected with a view toward providing a simple means of apportionment which would eliminate difficulties such as assigning weight to various factors and maintaining the kind of records necessary to the application of more complex formulae.

The keynote of the substantive portion of the Ruling is struck in the first paragraph of Part I: 'Whenever a person is engaged within the City of Los Angeles in a business subject to a tax under Sections 21.166 or 21.167, L.A.M.C., only those gross receipts which are Directly attributable to the business engaged in within the City of Los Angeles shall be included within the measure of the tax.' (Italics added.) The remainder of Part I goes on to describe what gross receipts should and should not be considered 'directly attributable' to local activities and to provide procedures and practices to be followed in making the determination. Two paragraphs are particularly relevant for our present purposes.

Paragraph 1(c) of the Ruling provides: '(c) If the person engaged in such business owns, leases, occupies or otherwise maintains within the City a place or premises upon which or from which he engages in such business, all receipts resulting from sales of goods, wares or merchandise which Are in any manner attributable to business functions carried on, at, or from that place of business, and which goods, wares or merchandise Are either sold for shipment into the City of Los Angeles to the purchaser or his agent or designee, or are shipped from a place within the City of Los Angeles to a place within the City, or from a place within the City to a place outside the City but within the State of California, shall be considered directly attributable to the business engaged in within the City.' (Italics added.)

Paragraph 1(d), on the other hand, provides in substance that if such a person having such a place of business within the City has receipts attributable 'both to business activities based upon that place of business and business activities carried on outside the City of Los Angeles' 25 [4 Cal.3d 116] percent of the receipts resulting from the sale of goods Which are not shipped from or into the City as provided in paragraph 1(c) shall be considered directly attributable if four or more of seven specifically listed elements of the selling process take place within the City, and 15 percent of the gross receipts so derived shall be considered directly attributable if less than four of the said elements take place within the City. The seven elements are, generally speaking: negotiating or soliciting, display of samples, processing of orders, acceptance of orders, arranging for delivery, billing and collection. [5]

Page 6

[480 P.2d 958] [4 Cal.3d 117] In the case of Carnation Co. v. City of Los Angeles (1966) 65 Cal.2d 36, 52 Cal.Rptr. 225, 416 P.2d 129, we considered one specific application of Ruling 14 in the light of the Belridge decisions. In that case, 'administrative and manufacturing, processing or handling facilities for all products' whose gross receipts were in issue were located on the taxpayer Carnation's Los Angeles premises, [6] and 'sales (of such products) at wholesale and retail (were) made both within and without the city limits.' (65 Cal.2d at p. 38, 52 Cal.Rptr. at p. 226, 416 P.2d at p. 130.) The City, relying on Ruling 14 (Part I, par. 1(c)), sought to base its business tax on 'gross receipts from the sale of such products without regard to the place of sale if within the State of California.' (65 Cal.2d at p. 38, 52 Cal.Rptr. at p. 226, 416 P.2d at p. 130.) Carnation contended that this was forbidden by the Belridge cases and that the tax could be based only on sales to in-city customers; the trial court agreed.

We reversed the judgment. We noted first 'that it is constitutional for a city to tax the privilege of manufacturing, processing or handling goods within its boundaries, and to determine the amount of the tax on the gross receipts from sales of the goods, regardless of whether the sales are made within or without the boundaries. (American Mfg. Co. v. St. Louis, 250 U.S. 459, 39 S.Ct. 522, 63 L.Ed. 1084.)' (65 Cal.2d at p. 38, 52 Cal.Rptr. at p. 226, 416 P.2d at p. 130.) Then, stating that the question at issue was whether the tax sought to be levied in the case before us was of this nature (i.e., a tax upon 'the privilege of manufacturing, processing or handling goods'), we proceeded to explain why the

Page 7

[480 P.2d 959] Belridge cases did not compel a negative answer to that question. Belridge, we pointed out, did not involve goods manufactured in Los Angeles--and in fact none of the goods there in question ever entered the City. Thus, we reasoned, the basis for the tax upon Belridge's business privilege was constitutionally limited to the extent of its Selling activities within the City, whereas in Carnation the activity of Manufacturing provided contact with all subsequent sales, wherever made within the state, and provided adequate constitutional[4 Cal.3d 118] support for the measurement of the privilege tax on the basis of All gross receipts derived from such sales. (65 Cal.2d at pp. 39--40, 52 Cal.Rptr. 225, 416 P.2d 129.)

II

It is manifest that the roots of our Belridge decisions can be traced to the numerous and varied cases wherein the United States Supreme Court has insisted--on various doctrinal bases--that state taxes on interstate enterprises be fairly apportioned in order to prevent multiple tax burdens on such enterprises. Thus in cases involving state net income taxes on interstate businesses the high court, grounding its decision upon the due process clause, has struck down taxes which seek to 'reach profits which are in no just sense attributable to transactions within (the taxing) jurisdiction' and therefore operate 'unreasonably and arbitrarily, in attributing to (the taxing jurisdiction) a percentage of income out of all appropriate proportion to the business transacted' in that jurisdiction. (Hans Rees' Sons v. North Carolina (1931) 283 U.S. 123, 134, 135, 51 S.Ct. 385, 389, 75 L.Ed. 879; see also, e.g., Butler Bros. v. McColgan (1942) 315 U.S. 501, 506--507, 62 S.Ct. 701, 86 L.Ed. 991.)

Similarly in cases involving state ad valorem property taxes on instrumentalities used in interstate commerce the court has required, on grounds of the due process and commerce clauses, that the tax be apportioned as to property which may be similarly taxed in other states. 'Otherwise there would be multiple taxation of interstate operations and the tax would have no relation to the opportunities, benefits, or protection which the taxing state gives those operations.' (Standard Oil Co. v. Peck (1952) 342 U.S. 382, 385, 72 S.Ct. 309, 310, 96 L.Ed. 427; see also and compare Central Railroad Co. of Pennsylvania v. Pennsylvania (1962) 370 U.S. 607, 82 S.Ct. 1297, 8 L.Ed.2d 720.)

Again, in cases involving gross receipts taxes on interstate enterprises, the court has held that the commerce clause requires apportionment of the tax if the activities giving rise to the gross receipts occurred in more than one state. 'The vice characteristic of those (gross receipts taxes) which have been held invalid is that they have placed on the commerce burdens of such a nature as to be capable in point of substance, of being imposed * * * or added to * * * with equal right by every state which the commerce touches, merely because interstate commerce is being done, so that without the protection of the commerce clause it would bear cumulative burdens not imposed on local commerce.' (Western Live Stock v. Bureau of Revenue (1938) 303 U.S. 250, 255--256, 58 S.Ct. 546, 548--549, 82 L.Ed. 823; see also, e.g., gwin, White & Prince, Inc. v. Henneford (1939) 305 U.S. 434, 59 S.Ct. 325, 83 L.Ed. 272; J.D. Adams [4 Cal.3d 119] Mfg. Co. v. Storen (1938) 304 U.S. 307, 58 S.Ct. 913, 82 L.Ed. 1365; but see General Motors v. Washington (1964) 377 U.S. 436, 84 S.Ct. 1564, 12 L.Ed.2d 430.)

Although the Constitution of this state, unlike that of the United States, contains no provision specifically preventing its constituent political subdivisions from enacting laws affecting commerce among them, there is no doubt that many of the considerations relevant to problems of interstate commerce apply in miscrocosm to the problems of intrastate or intercity commerce in a heavily populated state such as our own. In the words of one perceptive commentator: 'The basic policy underlying the commerce clause of the Federal Constitution (art. 1, § 8, par. 3)--to preserve the free flow of commerce among the states

Page 8

[480 P.2d 960] to optimize economic benefits--is equally applicable to intercity commerce within the state. If fifty independent economic units within the United States are undesirable, 387 economic enclaves within California would be intolerable. A tax burden which places intercity commerce at a disadvantage in comparison to a wholly intracity business may have such an effect.' (Sato, Municipal Occupation Taxes in California: The Authority to Levy Taxes and The Burden on Intrastate Commerce (1965) 53 Cal.L.Rev. 801, 818, fn. omitted.)

The decisions of this court in City of Los Angeles v. Belridge Oil Co., Supra--as well as a number of other decisions to which we shall presently advert--represent a recognition of these manifest realities and a determination that, in spite of the absence of a specific 'commerce clause' in the state Constitution, certain other provisions of the state and federal Constitutions forbid municipal taxation which, by encouraging multiple burdens through the levy of unapportioned or improperly apportioned taxes on intercity business, operates to place such businesses at a competitive disadvantage.

One of the first cases to articulate this doctrine was Ferran v. City of Palo Alto (1942) 50 Cal.App.2d 374, 122 P.2d 965, a case upon which we relied in Belridge. There the city imposed a license tax on the business of laundering and taking orders for laundering--the tax being measured by 'the number of employees at the plant or place of laundering.' Plaintiff laundry maintained its plant, where 35 persons were employed, in San Francisco but had customers throughout the bay area, including Palo Alto, who were serviced by truck on a pick-up and delivery basis. Of a gross annual income amounting to approximately $60,000 only about $900 was derived from Palo Alto business, and plaintiff contended that the application of the license tax to it on the basis of its total number of employees was unconstitutional.

[4 Cal.3d 120] The Court of Appeal agreed. Nothing that a license tax computed by The amount of business done within the city would be free from constitutional infirmity, and granting that the assessment of that amount might properly proceed by an indirect means looking to numbers of employees rather than dollar volume, the court nevertheless went on to hold the Palo Alto tax invalid as applied to plaintiff. Two separate constitutional grounds were stated. First, the court held that the tax had an improper extraterritorial application. [7]

'Since the number of employees is in a general way proportionate to the amount of business done, and since in this case the total amount of business done is about $60,000 per annum, of which only about $900 per annum comes from within Palo Alto, it follows that the license tax is nonlocal and operates upon business outside of Palo Alto in proportion to the difference in amounts. It is an invalid attempt by the city to make its ordinance extraterritorial in scope and application. If the method were upheld, it would be possible to subvert the entire principle of local application of municipal revenue measures.' (50 Cal.App.2d at pp. 382--383, 122 P.2d at p. 970.) Second, the court held that the tax resulted in a denial of equal protection of the laws. [8] 'We also hold that the case

Page 9

[480 P.2d 961] is governed by the principles laid down in Buen(e)man v. Santa Barbara, Supra (1937) 8 Cal.2d 405, 65 P.2d 884, [9] and related cases, and that * * * the ordinance is void as an unlawful and unreasonable discrimination against and denial of the equal protection of the law to laundries doing their laundering and having their plants outside of Palo [4 Cal.3d 121] Alto, but deriving some of their business from within said city. It also unlawfully discriminates against those engaged in Palo Alto in the business of taking orders for laundering or washing to be done by laundries maintaining their washing plants and doing their business outside the city. The business of such solicitors may be an independent calling having no logical connection whatsoever with the number of employees at the plant where the washing is done.' (50 Cal.App.2d at p. 383, 122 P.2d at p. 970.)

In Security Truck Line v. City of Monterey (1953) 117 Cal.App.2d 441, 256 P.2d 366, 257 P.2d 755, the principles announced in Ferran were clarified. [10] There the city sought to levy a business license tax upon highway carriers who hauled fish during canning season from points outside the city to canneries within the city--the tax being measured by the unladen weight of each vehicle used for this purpose. Plaintiff carrier had its principal place of business outside the city and had neither place of business nor agents nor terminus in the city, but during the autumn and winter canning season it engaged in the hauling of sardines from points in southern California to canneries within the city. Of plaintiff's sixty trucks no more than four were involved in fish hauls at any one time during the season, but its other commitments made it necessary to rotate the use of its trucks so that most of them were used for fish hauling at one time or another during the season; moreover, sometimes it was necessary for plaintiff to augment its own fleet of trucks by subcontracting with independent haulers who would haul fish only occasionally and sometimes only once a season. Prorated on a tonnage mile basis plaintiff's fish deliveries constituted only 1 percent of its total business, but during the season it derived 20 percent of its income from fish hauling.

The plaintiff carrier brought an action to have the tax declared unconstitutional and its enforcement enjoined. It urged that under the ordinance as applied it was required to pay a license fee as to each one of its vehicles used for fish hauling even if that particular vehicle hauled only one load of fish into the city during the season, and that, considering its necessary rotation of trucks, the ordinance would require it to license a substantial portion of its fleet plus the trucks of subcontracted haulers. Such a tax, plaintiff complained, was not reflected in the rate structure governing its compensation, and it urged that the ordinance was unconstitutional on several grounds--among them that of unlawful discrimination in violation of state and federal Constitutions. The trial court held that the ordinance was 'unconstitutional in its application and wording' (117 Cal.App.2d at p.

Page 10

[480 P.2d 962] 449, 256 P.2d at p. 372) and issued the injunction.

[4 Cal.3d 122] The Court of Appeal affirming the judgment, stated its approach to the problem in these terms: 'If the tax here involved is imposed upon a taxable local event that is, if the carrier is doing business in Monterey and if the measure of the tax is not discriminatory, then, in our opinion, the tax is valid. But if the tax is basically upon an event occurring outside the city, or, if the tax is discriminatory as to plaintiff, then it is invalid.' (117 Cal.App.2d at p. 451, 256 P.2d at p. 373.) [11]

Proceeding to apply this two-step standard the court first concluded that the plaintiff's activities in Monterey were sufficient from a due process standpoint to permit a tax upon them. '(S)uch activities constitute the doing of business in Monterey, a taxable event occurred there, and that city is empowered to tax such event by a proper nondiscriminatory ordinance.' (117 Cal.App.2d at p. 452, 256 P.2d at p. 374.) In reaching this conclusion the court rejected an argument of the plaintiff to the effect that Any taxation of intercity carriers by particular municipalities was 'unfair and unsound' on the basis that if each community served by a carrier could tax it an unfair burden on the carrier and on intercity business would result. This argument--which apparently sought to draw an analogy to those cases decided under the federal commerce clause which forbid a tax on the privilege of engaging in interstate commerce itself (see Spector Motor Service v. O'Connor (1951) 340 U.S. 602, 71 S.Ct. 508, 95 L.Ed. 573; Puget Sound Stevedoring Co. v. Tax Commission (1937) 302 U.S. 90, 58 S.Ct. 72, 82 L.Ed. 68; Robbins v. Shelby Taxing District (1887) 120 U.S. 489, 7 S.Ct. 592, 30 L.Ed. 694)--was held to lack any basis in state constitutional provisions.

However, when the court turned its attention to the validity of the particular tax at bench it recognized that the argument of multiple burdens, 'while it does not result in a holding of lack of power to tax, does suggest that such tax ordinances must be scrutinized carefully to see that a city measures its tax by the taxable event that occurs in the city, and does not measure in such a manner that an unfair or discriminatory burden is imposed on such carriers.' (117 Cal.App.2d at p. 453, 256 P.2d at p. 374.) The tax before it, the court concluded, was measured in an invalid manner because the amount of tax was governed by a factor which had no relationship to the actual amount of business done in the taxing city. 'The tax is imposed upon each truck making a delivery or deliveries during the fish hauling season. If that truck makes one hundred deliveries during the season, the maximum tax is but $13.50 for that truck. But if the carrier uses one hundred different trucks to make the one hundred deliveries, it must pay [4 Cal.3d 123] $13.50 for each truck, or a total of $1,350. * * * The taxable event in both cases is the same--the delivery of one hundred loads of fish in Monterey--yet one company would pay one hundred times what the other had to pay. It seems clear that the measure of the tax set forth in the ordinance has no reasonable connection with that taxable event. * * * (The tax) is based upon an arbitrary standard and a purely extraneous event.' (117 Cal.App.2d at pp. 453--454, 256 P.2d at p. 374.)

Finally, the court pointed out that the tax struck down in the Ferran case shared the constitutional defect which rendered the Monterey tax invalid. 'In the Ferran case the tax was measured by a purely extraneous event (i.e., the number of employees at the San Francisco plant) that had no relation to the quantum or nature of the business done in Palo Alto. That is equally true in the instant case. Here, the standard selected, the number of individual trucks making deliveries, rather than the number

Page 11

[480 P.2d 963] of such deliveries or the tonnage carried into the city is a purely accidental and extraneous event that has no relation to the taxable event occurring in Monterey or the quantum of business there carried on. For these reasons, it is our opinion that the measure * * * is capricious, arbitrary and discriminatory.' (117 Cal.App.2d at p. 454, 256 P.2d at p. 375.)

In City of Los Angeles v. Carson (1960) 181 Cal.App.2d 540, 5 Cal.Rptr. 356; City of Los Angeles v. Drake (1961) 195 Cal.App.2d 744, 16 Cal.Rptr. 103, and City of Los Angeles v. California Motor Transport Co. (1961) 195 Cal.App.2d 759, 15 Cal.Rptr. 917, the Security Truck Line case was relied upon to hold invalid business license taxes on charter bus and motor transport businesses based upon the number of vehicles utilized. To be contrasted with these cases is Willingham Bus Lines, Inc. v. Municipal Court (1967) 66 Cal.2d 893, 59 Cal.Rptr. 618, 428 P.2d 602, where the city imposed a business license tax amounting to "2% Of the gross receipts attributable to the portion of the trip traveled within the city limits * * * by charter vehicles." We there said that 'This method of allocation obviously works to confine the tax to that part of a licensee's revenue which is derived from intracity business' (66 Cal.2d at p. 896, 59 Cal.Rptr. at p. 621, 428 P.2d at p. 605), to which we added in a footnote: 'In so doing it avoids discrimination against multi-city enterprise since it minimizes the risk of multiple taxation. (Cf., e.g., City of Los Angeles v. Belridge Oil Co. (1954) 42 Cal.2d 823, 832, 271 P.2d 5, app. dism. (1955) 348 U.S. 907, 75 S.Ct. 292, 99 L.Ed. 711; Security Truck Line v. City of Monterey (1953) 117 Cal.App.2d 441, 451--454, 256 P.2d 366, 257 P.2d 755, and cases there discussed.)' (66 Cal.2d at p. 869, fn. 6, 59 Cal.Rptr. at p. 621, 428 P.2d at p. 605.)

The foregoing review of the constellation of cases to which the Belridge decisions belong enables us to state with some confidence the [4 Cal.3d 124] principles which support and inform those decisions. In the first place, it is clear that in spite of the absence of a specific 'commerce clause' in our state Constitution, other provisions in that Constitution--notably those provisions forbidding extraterritorial application of laws and guaranteeing equal protection of the laws (see fns. 7 and 8, Ante)--combine with the equal protection clause of the federal Constitution to proscribe local taxes which operate to unfairly discriminate against intercity businesses by subjecting such businesses to a measure of taxation which is not fairly apportioned to the quantum of business actually done in the taxing jurisdiction. On the other hand, those constitutional principles do not Prohibit local license taxes upon businesses 'doing business' both within and outside the taxing jurisdiction; as long as such taxes are apportioned in a manner by which the measure of tax fairly reflects that proportion of the taxed activity which is actually carried on within the taxing jurisdiction, no constitutional objection appears. However, and conversely, no measure of apportionment can satisfy the constitutional standard if the measure of tax is made to depend upon a factor which bears no fair relationship to the proportion of the taxed activity actually taking place within the taxing jurisdiction.

We proceed to apply these principles to the case now before us.

III

The taxpayer Shell concedes that it is engaged in the business of 'selling * * * godds * * * at wholesale' in the City of Los Angeles within the meaning of L.A.M.C. section 21.166--and that it is therefore subject to a business tax under the provisions of L.A.M.C. section 21.03. [12] The tax sought to be imposed on Shell pursuant to these sections is resisted in only one respect: Shell contends that the tax exceeds the City's constitutional powers and is in violation of the taxpayer's constitutional

Page 12

[480 P.2d 964] rights insofar as it is based upon the Total gross receipts derived by Shell from wholesale sales of gasoline delivered from a point within the City to retailers located outside the City. We agree with this contention.

Ruling 14, upon which the City bases its attempt to include all of the questioned gross receipts in the measure of Shell's tax, essentially sets up a rigid distinction between, on the one hand, receipts derived from sales of goods which Are shipped from or into the City, and on the other hand, receipts derived from sales of goods which Are not shipped from or into the City. [13] Paragraph 1(c) of the Ruling, which deals with receipts in the [4 Cal.3d 125] former category, provides that All receipts from sales of goods 'which are In any manner attributable' (italics added) to in-city business functions and which Are shipped from or into the City 'shall be considered directly attributable to the business engaged in within the City'--and therefore shall be included in the measure of the tax. [14] In contrast, paragraph 1(d) of the Ruling provides that if a taxpayer has receipts attributable to both in-city and out-of-city activities, and those receipts result from the sale of goods which Are not shipped from or into the City, either 15 or 25 percent--according to the presence or absence in the City of certain specified elements of the selling process (see fn. 5, Ante)--of those gross receipts shall be considered 'directly attributable' and therefore properly included in the measure of the tax. [15] Thus, under the Ruling a taxpayer who has receipts 'which are in any manner attributable' to in-city selling activities but which are also to some degree attributable to out-of-city selling activities will be taxed on 100 percent of those receipts if the goods whose sale produces them Are shipped from or into the City, whereas he will be taxed on a maximum of 25 percent of those receipts if the goods Are not shipped from or into the City.

Most significantly, the aforesaid results will flow from the Ruling Regardless of the proportion of selling activity which takes place within the City. If a particular receipt is 'in any manner attributable' to incity selling activities and if the goods are shipped from or into the City, the fact that a substantial portion of--or even the greater portion of--the selling activities which produced that receipt took place outside the City is of no moment: the entire receipt is included. On the other hand, If the goods are not shipped from or into the City, no more than 25 percent of the receipt is included in the tax base even if all but a small fraction of the selling activity which produced it takes place within the City.

We think it manifest that the apportionment formula set forth in Ruling 14 is capable of being applied in violation of the constitutional principles set forth in Belridge and the other cases we have discussed. That formula, to the extent that it places decisive importance upon the situs of the goods at the time of shipment or delivery, rests upon a 'purely accidental and extraneous event that has no relation to the taxable event occurring in (the City) or the quantum of business there carried on.' (Security Truck Line v. City of Monterey, Supra, 117 Cal.App.2d 441, 454, 256 P.2d 366, 375.) The 'taxable event' here is the conduct of selling activities in the [4 Cal.3d 126] City by a business subject to taxation, and the formula of Ruling 14 depends on a factor which bears no rational relationship to the Proportion of those activities which actually takes place within the City. To the extent that the Ruling can be applied to include within the tax base the Total gross receipts arising from sales which have resulted in part from any substantial out-of-city sales

Page 13

[480 P.2d 965] activity, it purports to reach gross receipts other than those 'directly attributable to * * * selling activities carried on in the city' (City of Los Angeles v. Belridge Oil Co., Supra, 48 Cal.2d 320, 324, 309 P.2d 417, 419) and is in violation of constitutional provisions forbidding extraterritorial application of local taxes and insuring equal protection under the law. (See fns. 7, 8, Ante.)

It is clear, however, that a taxpayer who challenges an apportionment formula on constitutional grounds must show more than the possibility of erratic or unconstitutional application. 'One who attacks a formula of apportionment carries a distinct burden of showing by 'clear and cogent evidence' that It results in extraterritorial values being taxed.' (Butler Bros. v. McColgan, Supra, 315 U.S. 501, 507, 62 S.Ct. 701, 704, 86 L.Ed. 991, italics added; see also City of Los Angeles v. Moore Business Forms, Inc. (1966) 247 Cal.App.2d 353, 362, 55 Cal.Rptr. 820.) In the context of this case the taxpayer Shell has the burden of showing by 'clear and cogent evidence' that the City's application of Ruling 14 to its business actually operates to include within its tax base total and undivided gross receipts from sales resulting in part from substantial out-of-city sales activity.

Shell has sustained its burden. At trial it presented substantial amounts of evidence detailing the functions of the out-of-city district offices contributing to the wholesale sale of gasoline to out-of-city dealers. [16] This evidence showed in essence that the district offices have primary responsibility for obtaining station sites (subject to approval by division, regional, or headquarters offices), constructing stations on approved sites, locating dealers to operate the stations, and 'servicing' dealers within the district. While we think that the functions of the district office relating to the location and construction of new service stations are only indirectly related to the selling process, it is clear that certain functions performed in relation to setting up new dealers and 'servicing' both new and old dealers are directly involved in that process. Thus, for example, the district office is responsible for binding dealers to purchase quotas through written sales agreements. Additionally, when a new dealership is created it is [4 Cal.3d 127] the district office which makes arrangements with the bulk terminal for the initial delivery and future supply of gasoline to the station. Payment problems concerning out-of-city dealers are also the responsibility of the district office.

In addition to the functions of the district offices which are directly involved in the sales process, certain other aspects of that process take place outside the city. The actual delivery of the product of course occurs at the out-of-city station. Billing also occurs at this point, the driver of the delivery truck preparing an invoice according to the metered volume of gasoline actually delivered and handing it to the dealer. Furthermore, in certain circumstances--i.e., when a dealer because of a poor payment record or credit rating is on a 'currency' rather than remittance basis--actual collection is made on a C.O.D. basis at the time of delivery.

It is clear from the foregoing that substantial elements of Shell's overall sales process relating to out-of-city dealers take place outside the City. [17] However, the

Page 14

[480 P.2d 966] City, applying its Ruling 14, refuses to take cognizance of those out-of-city elements in the measure of its tax--and accordingly purports to tax the total gross receipts derived from the sales in question--solely because the goods are shipped from the City. Such an application of the Ruling is violative of the constitutional principles we have discussed because it renders the measure of tax dependent on a factor (i.e., the situs of the goods upon shipment) which bears no relationship to the proportion of the taxed activity (i.e., the business of selling) which actually takes place within the taxing jurisdiction and, under the facts of this case, operates to reach gross receipts other than those which are 'directly attributable to * * * selling activities carried on in the City.' (City of Los Angeles v. Belridge Oil Co., Supra, 48 Cal.2d 320, 324, 309 P.2d 417, 419.)

Finally, we note our conclusion that the case of Carnation Co. v. City of Los Angeles, Supra, 65 Cal.2d 36, 52 Cal.Rptr. 225, 416 P.2d 129, whose legal effect in the instant context has been a subject to considerable argument among the parties, is, as Shell has maintained, not controlling in the determination of the instant case. Carnation holds that a business privilege tax levied on the [4 Cal.3d 128] business of 'manufacturing and selling' (as opposed to merely 'selling') under the provisions of L.A.M.C. sections 21.166 and 21.167 is fundamentally a tax upon the privilege of manufacturing and that such a tax may constitutionally be based upon total gross receipts from sales, wherever made, of products wholly manufactured within the taxing jurisdiction. [18]

The judgment is reversed and the cause is remanded to the trial court with directions to set aside the findings of fact and conclusions of law; to determine a proper apportionment of defendant's gross receipts in conformity with the views herein expressed and, to that end, to receive such additional evidence as it may deem necessary or advisable; thereafter, having reexamined and redetermined all issues, to make and file findings of fact and conclusions of law in conformity with the views herein expressed; and to enter judgment accordingly.

TOBRINER, Acting C.J., and PETERS and MOSK, JJ., concur.

BURKE, Justice (concurring).

The holding of the opinion in this case, as I read it, is that insofar as concerns the gross receipts from sales of gasoline delivered from Shell's in-city bulk terminal to locations outside the city, the city may not constitutionally assign as the controlling factor in fixing the measure of its tax on the business of 'selling,' the element of delivery from in the city to out of the city when substantial elements of the sales process to the out-of-city customers actually take place outside the city. Instead, a fair apportionment must be made as between in-city and out-of-city activities contributive to those gross receipts.

Although I agree with that ruling, it also seems to me that storage in the bulk plant in the city and delivery from that plaint to out-of-city points are plainly factors to be taken into account and accorded their fair weight in making the apportionment. Based on my understanding that nothing in the opinion precludes considering the storage and delivery factors, I concur.

It aslo appears appropriate to note that if the city's code provisions undertook to cover businesses engaged in 'handling and selling'; 'storage, handling and selling'; 'assembling and selling'; or 'processing and selling,' as well as (insofar as concerns Shell) merely 'selling,' then [4 Cal.3d 129] we would have a case more closely analogous to Carnation (Carnation Co. v. City of Los

Page 15

[480 P.2d 967] Angeles (1966) 65 Cal.2d 36, 52 Cal.Rptr. 225, 416 P.2d 129), in which the tax was levied on the business of 'manufacturing and selling.'

McCOMB and WOOD, * JJ., concur.

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1 A description of the function of the district office in the sales operation will be set forth Infra.

2 Apparently section 21.166 is a 'catch-all' provision. Other sections of the article are directed to specific kinds of businesses. (See City of Los Angeles v. Belridge Oil Co. (1954) 42 Cal.2d 823, 828, 271 P.2d 5.)

3 The adverb 'directly' was added to the standard in the second Belridge decision.

4 L.A.M.C. section 21.15, subdivision (h), provides in relevant part: 'When, by reason of the provisions of the Constitution of the United States or the Constitution of California, the business tax imposed by this Article cannot be enforced without there being an Apportionment according to the amount of business done in the City of Los Angeles, or in the State of California, as the case may be, the City Clerk may make such rules and regulations for the Apportionment of the tax as are necessary or desirable to overcome the constitutional objections.' (Italics added.)

5 Paragraph 1(d) provides in full as follows:

'(d) If the person engaged in such business owns, leases, occupies or otherwise maintains within the City of Los Angeles a place or premises upon which or from which he engages in business and has receipts which are attributable both to business activities based upon that place of business and business activities carried on outside the City of Los Angeles, 25 percent of the receipts resulting from the sale of goods, wares or merchandise manufactured and sold or sold by the person which are not shipped from or into the City of Los Angeles as provided in paragraph (c) above, shall be considered directly attributable if four or more of the elements of the selling process listed below take place within the City of Los Angeles with respect to the sales of goods, wares or merchandise which produce those receipts; if less than four of the listed elements of the selling process take place within the City, 15 percent of the gross receipts so derived shall be considered directly attributable.

'For the purpose of determining the amount of attributable gross receipts which shall be considered directly attributable for the purposes of this paragraph (d), the following elements of the selling process shall be considered:

'1. Negotiating sales of, or soliciting, receiving or taking orders for the sale of goods, wares or merchandise, and/or carrying on activities by an employee, agent, or otherwise, designed to promote, stimulate or otherwise encourage the sale of goods, wares or merchandise.

'2. Display of articles or samples of goods, wares or merchandise of like or similar kind to those offered for sale where the actual articles sold or to be sold will be delivered from a place of storage or manufacture located outside the City of Los Angeles but within the State of California.

'3. Processing of orders received or taken preparatory to their being accepted, where the actual acceptance occurs elsewhere.

'4. Approval or acceptance of orders received or taken.

'5. Giving an order for or arranging for delivery or shipment of articles sold or to be sold from a place of storage or manufacture located outside the City of Los Angeles but within the State of California.

'6. Billing for goods, wares or merchandise sold.

'7. Receiving or collecting receipts (as defined in subparagraph (a) in Section 21.00) resulting from sales of goods, wares or merchandise.

'It is recognized that many persons carrying on the business of selling goods, wares or merchandise will not have their functions so organized that all of the elements of the selling process listed will be present; it is further recognized that certain of the elements listed may occur simultaneously, or nearly so, with other elements in all or a portion of the transacactions of sale handled by a particular person. Notwithstanding, each of the elements present shall be considered as a separate element for the purposes of the regulation.

'It shall be recognized that certain businesses are subdivided into divisions or organized along functional lines for the convenience of administration and management and that it is to be expected in some cases that the operations of a particular division or functional unit of a taxpayer may call for the application of the 25 percent rate, and the operations of another may call for the application of the 15 percent rate. Due regard for such divisional or functional organization shall be made in administering the business tax ordinance under the provisions of this ruling.'

6 The City refers us to the record and briefs in Carnation and invites us to conclude therefrom that in fact a number of the products there involved were not manufactured within the City but were only 'processed and handled' there prior to sale. On this basis the City urges that our Carnation decision is of broader application than our opinion indicates. We decline this invitation to reexamine the record in Carnation and alter the scope of our holding therein. Although such a procedure does not lack weighty precedent (see Bingham v. United States (1935) 296 U.S. 211, 218--219, 56 S.Ct. 180, 80 L.Ed. 160), we believe that the interests of sound judicial administration counsel against the alteration of a final opinion of this court by such a means.

7 Article XI, section 11, of the California Constitution provides: 'Any county, city, town, or township may make and enforce Within its limits all such * * * regulations as are not in conflict with general laws.' (Italics added.) This provision has been held to forbid extraterritorial application of local ordinances. (South Pasadena v. Terminal Ry. Co. (1895) 109 Cal. 315, 321, 41 P. 1093.)

8 The Fourteenth Amendment to the United States Constitution provides that 'No State shall * * * deny to any person within its jurisdiction the equal protection of the laws.' The California Constitution contains no specific equal protection provision but it contains a number of provisions requiring the uniform application of laws. Article I, section 21, upon which the Ferran court appears to have placed reliance, in pertinent part provides: '* * * nor shall any citizen, or class of citizens, be granted privileges or immunities which, upon the same terms, shall not be granted to all other citizens.' Article IV, section 16 provides: 'A local or special statute is invalid in any case if a general statute can be made applicable.' The test for determining the validity of a statute or ordinance against a claim of unlawful discrimination is substantially the same under these state prohibitions as it is under the equal protection clause. (Whittaker v. Superior Court (1968) 68 Cal.2d 357, 367, fn. 16, 66 Cal.Rptr. 710, 438 P.2d 358; County of Los Angeles v. Southern Cal. Tel. Co. (1948) 32 Cal.2d 378, 389, 196 P.2d 773.)

9 The Bueneman case involved a flat rate license fee upon businesses which solicited orders for laundry and maintained a pickup and delivery system within the taxing city but had their plant located outside the city. Persons operating a similar business but having their plant within the city were not subject to the tax. This court held that the tax resulted in an invalid discrimination in favor of in-city laundries and was in violation of constitutional protections insuring equal protection of the laws.

10 The Security Truck Line case was not cited in either of our Belridge opinions. Ferran, as we have indicated above, was cited and relied upon in both Belridge opinions.

11 Illustrating the application of this test by reference to previous cases, the court stated that the tax in Ferran 'was void as a denial of equal protection and because of discrimination against the outside business for failure of apportionment.' (117 Cal.App.2d at p. 451, 256 P.2d at p. 373.)

12 The cited sections of L.A.M.C. are set forth in the text accompanying and immediately preceding footnote 2, Ante.

13 Ruling 14 is discussed and set forth in relevant part in the text following footnote 4, Ante.

14 As we have explained above, our Belridge decisions held that receipts 'directly attributable' to in-city activities were properly included within the measure of the tax.

15 In City of Los Angeles v. Moore Business Forms, Inc. (1966) 247 Cal.App.2d 353, 55 Cal.Rptr. 820, an application of paragraph 1(d) was upheld against constitutional attack.

16 The trial court found as a fact that 'the major part of the sales activity (relating to wholesale sales to out-of-city dealers) takes place in the City. * * *' The evidence which we now summarize is not inconsistent with this finding.

17 We do not suggest that the out-of-city sales activities which we have mentioned are the only such activities which should be considered directly contributive to Shell's gross receipts. Nor do we evaluate the relative significance of the various factors. Such matters will be the proper concern of the trial court upon remand. We here determine only that if there are substantial out-of-city sales activities which directly contribute to the gross receipts sought to be made a basis of the tax, the measure of tax must apportion those gross receipts in a manner which fairly reflects the proportion of incity to out-of-city activities. We express no present opinion as to which specific activities of Shell are to be considered sales activities for this purpose.

18 Because the issue is not now before us we express no present opinion whether an apportionment of gross receipts is required in the case of products not Wholly manufactured within the taxing jurisdiction.

* Assigned by the Acting Chairman of the Judicial Council.

Page 590

80 Wn.2d 590
496 P.2d 504
DRAVO CORPORATION, a Pennsylvania corporation, and Al Johnson Construction Co., a Delaware corporation,
Joint Venturers, d/b/a Dravo-Johnson, Appellants/Cross-Respondents,
v.
CITY OF TACOMA, a municipal corporation, Respondent/Cross-Appellant.
No. 41906.
Supreme Court of Washington, En Banc.
May 4, 1972.

Page 591

[496 P.2d 505] DeGarmo, Leedy, Oles & Morrison, Richard M. Stanislaw, Seattle, for appellant.

Robert R. Hamilton, F. H. Chapin, Jr., Tacoma, John R. Kramer, for respondents.

STAFFORD, Associate Justice.

This is an appeal from a judgment of the superior court declaring a portion of Tacoma's business and occupation tax unconstitutional. The challenged provision imposed a tax on the gross receipts of contracts made with the city, whether performed within or without its boundaries.

In 1964, pursuant to the authority of RCW 35.92.050, Tacoma issued an invitation for bids to build the Mossyrock dam, powerhouse and appurtenances on property it had acquired for that purpose in Lewis County. Section 1.08 of the Instructions to Bidders gave notice that Tacoma's business[496 P.2d 506] and occupation tax (hereinafter called a B&O tax) would apply to the prospective contract.

Page 592

Dravo-Johnson is a joint venture formed for the specific purpose of bidding on and constructing the Mossyrock Project. It is composed of two corporations: the Dravo Corporation, a Pennsylvania corporation with its principal place of business in Pittsburgh, and the Al Johnson Construction Company, a Delaware corporation with its principal place of business in Minneapolis, Minnesota. Both corporations were qualified to do business in the state of Washington. The Dravo Corporation maintained its principal Washington office in Bellevue. Neither at the time of contracting nor thereafter did the Dravo Corporation, the Al Johnson Construction Company, or their joint venture have an office or place of business in Tacoma. The office and principal place of business of the joint venture (hereinafter called Dravo) was located at the dam site.

Having been informed of the B&O tax by the Instructions to Bidders, Dravo included within its bid an amount to cover such expenditure based on the applicable tax rate. Dravo's representative personally delivered its bid to the city clerk In Tacoma.

Dravo's low bid was accepted by the city In Tacoma. The formal contract was drawn on a form provided by the city. It was signed by representatives of the two jointly participating corporations at their respective home offices and submitted to Tacoma by mail on January 21, 1965. The following day, the contract document was finalized In Tacoma upon being signed by representatives of the city.

Tacoma collected a B&O tax of $40,184.38 on the contract. It was paid quarterly throughout the four year construction period, being based on and paid from the gross quarterly amounts advanced by Tacoma to Dravo under the contract. In addition to the amount paid by Tacoma, under the basic contract, the city also contracted to have Dravo perform extra work on the Mossyrock Project. On the subsequent contracts, Dravo paid the city.$3,418.36 in B&O taxes. There is no evidence that Dravo paid B&O taxes other than those in issue.

In September 1967, Dravo filed a claim for refund of the

Page 593

B&O tax paid from October 15, 1965 to July 15, 1967. In June 1969, it filed a claim for refund of a like tax paid from October 15, 1967 to March 27, 1969. The total refund claimed was $40,184.38. The record does not indicate that a claim for refund was made for the.$3,418.36 paid in B&O taxes based upon the extra work contracts. The claims were denied.

This action was brought to have the questioned provision of Tacoma's B&O tax ordinance declared unconstitutional and to obtain a refund of the amounts paid thereunder. In the alternative, Dravo requested an apportionment of said taxes upon their activities in the city. The city's answer pleaded as a bar, the statute of limitations, unjust enrichment and estoppel. Both parties moved for summary judgment.

At the hearing for summary judgment, the trial court ruled that, as applied to this case, the section of the ordinance imposing a B&O tax on persons contracting with the city was unconstitutional, and that the statute of limitations did not bar Dravo from recovering a tax refund. It left for trial Tacoma's affirmative defenses of unjust enrichment and estoppel.

At trial the court decreed that Dravo was entitled to recover the taxes paid on the extra work contracts (I.e.,.$3,418.36), but denied recovery as to the tax paid under the terms of the basic contract (I.e., $40,184.38) on the ground of unjust enrichment. Both parties have appealed.

It is well settled that the cities of this state have authority to levy B&O taxes. State ex rel. Pac. Telephone & Telegraph Co. v. Department of Pub. Serv., 19 Wash.2d 200, 272, 142 P.2d 498 (1943); Pacific Telephone & Telegraph Co. v. City of Seattle, 172 Wash. 649, 652, 21 P.2d 721 (1933).

[496 P.2d 507] Pursuant to that authority, Tacoma enacted a B&O tax ordinance which reads in pertinent part as follows:

6.68.225 Transactions subject to tax. Except where such a tax is otherwise levied and collected by the City from such person, there is hereby Levied upon and there shall be Collected from every person as set forth and

Page 594

provided in Section 6.68.220 of this chapter, A tax on the act or privilege of engaging in business activities and transactions with the City involving the purchase of materials, supplies, equipment, Improvements, and other contractual services. Such tax shall be Levied on the privilege of accepting and executing the contract, and shall be Collected whether such business activities or transactions occur or take place Within or without the City and whether or not such person has his office or place of business within or without the City.

Any person engaging in such business activities and/or transactions with the City shall be taxed on the contractual transactions in the same manner and form and under the same rules and regulations and at the same rates of tax as if they were doing business within the City of Tacoma.

(Italics ours.) It is this section which the trial court held unconstitutional, as applied to Dravo.

Initially, we note that a taxing authority has no power to levy a tax upon activities which occur outside its territorial limits. Connecticut Gen. Life Ins. Co. v. Johnson, 303 U.S. 77, 80, 58 S.Ct. 436, 82 L.Ed. 673 (1938); James v. Dravo Contracting Co., 302 U.S. 134, 58 S.Ct. 208, 82 L.Ed. 155 (1937). As we said in Lone Star Cement Corp. v. City of Seattle, 71 Wash.2d 564, 572, 429 P.2d 909, 913 (1967):

The phrase, 'the privilege of doing business,' used in section 3 of Seattle's ordinance, is all-inclusive; but taxation of that privilege must be confined to a standard within the territorial limits of Seattle, for the city has no power either to authorize, license, or tax activities beyond its territorial limits.

In Lone Star, Seattle sought to impose a tax for the 'privilege of engaging in business activities' upon persons doing business within the city as manufacturers or sellers at wholesale or retail. The measure of the tax was the value of the products manufactured or the gross proceeds of such sales. Where the activity taxed occurred partially within and partially outside of the city, provision was made for apportionment.

Lone Star manufactured cement in two plants, one in

Page 595

Seattle, the other in Concrete, Washington. Over 88 per cent of the cement products manufactured and sold at the Concrete plant were delivered to destinations outside of Seattle. The Seattle office took no part therein other than to receive information thereon at the end of each day. Seattle sought to tax the entire gross proceeds of sales from the Concrete plant.

Lone Star paid the tax on the gross proceeds from sales of all cement products (manufactured at its Concrete plant) which entered Seattle and were subsequently sold in or outside the city. We held that Seattle could not constitutionally tax the remaining 88 per cent of sales made from the city of Concrete.

In Lone Star the taxable events were sales made Outside the city. We held the city could impose a B&O tax only if the taxable event occurred Within its territorial limits.

In the case at bar, we must first determine the taxable events upon which Tacoma levied its B&O tax. In this regard § 6.68.225 provides:

Such tax shall be levied on the privilege of accepting and executing the contract . . .

Thus, 'accepting and executing the contract' is the taxable event.

Next, to decide where the taxable event occurred, we must determine the meaning of the phrase 'accepting and executing[496 P.2d 508] the contract'. A basic rule for construing revenue measures provides that if there is any doubt as to the meaning of a taxing statute or ordinance, it must be construed most strongly against the taxing power in favor of the citizen. Foremost Dairies, Inc. v. State Tax Comm., 75 Wash.2d 758, 763, 453 P.2d 870 (1969); Buffelen Lbr. & Mfg. Co. v. State, 32 Wash.2d 40, 43, 200 P.2d 509 (1948). However, there is a corollary which provides that the foregoing rule is inapplicable unless it can be automatically assumed, or proved, that the statute in question is ambiguous or its meaning is doubtful. Guinness v. State, 40 Wash.2d 677, 685, 246 P.2d 433 (1952).

Interpreted in light of the whole ordinance, the

Page 596

phrase 'accepting and executing the contract' is not ambiguous. It refers to the taxpayer's activity of Entering into a contract with Tacoma under which there will be a 'purchase of materials, supplies, equipment, improvements, and other contractual services.' It does not refer to the taxpayer's activity of Performing the contract. Here, the contract Entered into was for the purchase, by Tacoma, of an improvement (I.e., a dam) to be built by Dravo.

As provided in ordinance § 6.68.225, the capacity in which Dravo was taxed and its rate of taxation were determined by § 6.68.220. Under § 6.68.220(d) it was taxed as one engaged in the business of making sales at retail. A sale at retail, as defined in § 6.68.055, includes

the sale of or charge made for tangible personal property consumed and/or for labor and services rendered in respect to the following: . . . (b) the Constructing, repairing . . . or Improving or new or existing buildings or Other structures under, Upon, or above Real property of or for Consumers, including the installing or attaching of any article of tangible personal property . . . whether or not such personal property becomes a part of the realty . . . and shall also include the sale of services or charges made for the clearing of land and the moving of earth to the extent necessary for such constructing or improving . . .

(Italics ours.) The taxable event was the activity of Dravo in Entering into a contract to construct the Mossyrock dam for Tacoma.

In determining where this taxable event occurred we must look to the indicia of contract making. The invitation for bids was issued In Tacoma. Dravo submitted its bid by having a personal representative deliver it to the city clerk In Tacoma. Although the formal memorandum of contract was signed by representatives of Dravo outside of Tacoma, it was prepared on a form provided by the city and signed by the city's representatives In Tacoma. The totality of the foregoing indicia leads to the conclusion that the incidents had their locus in Tacoma, and were sufficient

Page 597

to establish that, for the purpose of taxation, the basic contract's place of making was in Tacoma. See American Oil Co. v. Neill, 380 U.S. 451, 458, 85 S.Ct. 1130, 14 L.Ed.2d 1 (1965).

Dravo argues, however, that Tacoma seeks to do indirectly what it cannot do directly. In effect, it contends the taxable event which Tacoma seeks to reach is not the activity of Entering into a contract, but Dravo's Performance thereof. Dravo directs our attention to the fact that the tax was collected quarterly throughout the course of the four year period it took to build the dam.

The mere schedule of tax collection, however, does not support the conclusion that the activity taxed was the Performance of the contract. Section 6.68.220 provides that there shall be levied upon and collected, on a quarterly basis, a B&O tax based upon the gross proceeds from 'sales at retail' which is defined in § 6.68.055(b) as including the construction or improving of structures on the real property of consumers. The taxable event is the Contract. The gross proceeds from the construction or improving of structures on [496 P.2d 509] the city's property is merely the Measure of the tax. Since Tacoma made quarterly progress payments to Dravo, the tax could only be measured by those payments as they were made. The quarterly collection was the fairest method of exacting the tax.

Having decided that the taxable event occurred within the territorial limits of the city, we must determine whether that taxable incident forms a sufficient contact, or nexus, with Tacoma to give, as a matter of due process, jurisdiction to impose the tax. [1]

A taxing authority is empowered to tax activity within its jurisdiction because it provides an environment of services and protection, which enable the taxpayer to

Page 598

engage in the activity that is the subject of the tax. To sustain the tax against a due process challenge, there must be a reasonable relationship between the event taxed and the benefit conferred. We referred to this rationale in State ex rel. Stiner v. Yelle, 174 Wash. 402, 408, 25 P.2d 91 (1933); and the United States Supreme Court articulated it in Wisconsin v. J. C. Penney Co., 311 U.S. 435, 444, 61 S.Ct. 246, 249, 85 L.Ed. 267 (1940).

A state is free to pursue its own fiscal policies, unembarrassed by the Constitution, if by the practical operation of a tax the state has exerted its power in relation to opportunities which it has given, to protection which it has afforded, to benefits which it has conferred by the fact of being an orderly, civilized society.

. . . The simple but controlling question is whether the state has given anything for which it can ask return.

Dravo contends that Tacoma has conferred no benefit upon which it may reasonably base the tax. It argues that construction of the dam took place in Lewis County, and that there is no evidence to indicate that Tacoma provided services or protection to Dravo at the dam site. On the other hand, Tacoma asserts that the benefit conferred was award of the $40,000,000 contract to Dravo.

Both contentions are incorrect. Dravo was not taxed on its activity in Lewis County. The tax was levied on the act of Entering into the contract in the city of Tacoma. On the other hand, although the award of a $40,000,000 contract might be considered a benefit, the city received a reciprocal benefit, I.e., a $40,000,000 dam. The benefit conferred, for which Dravo could be taxed, was the environment of an 'orderly, civilized society', maintained by Tacoma within its borders, that enabled Dravo to there engage in a business transaction with the city (I.e., entering into the contract with the city).

Due process requires 'some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax.' Miller Bros. Co. v. Maryland, 347 U.S. 340, 344, 74 S.Ct. 535, 539, 98 L.Ed. 744 (1954).

Page 599

Accord American Oil Co. v. Neill, 380 U.S. 451, 458, 85 S.Ct. 1130, 14 L.Ed.2d 1 (1965); General Motors Corp. v. Washington, 377 U.S. 436, 84 S.Ct. 1564, 12 L.Ed.2d 430 (1964); Northwestern States Portland Cement Co. v. Minnesota, 358 U.S. 450, 465, 79 S.Ct. 357, 3 L.Ed.2d 421 (1959). The crux of this appeal is whether there is a definite link or minimum connection between the city and the transaction it seeks to tax, I.e., the making of a contract with the city.

In reaching our determination we must bear in mind that when the constitutionality of a tax statute or ordinance is challenged, our concern must be with the practical operation of the tax. Wisconsin v. J. C. Penney Co., 311 U.S. 435, 444, 61 S.Ct. 246, 85 L.Ed. 267 (1940). Since it is the measure of a tax that determines its [496 P.2d 510] economic effect, the measure must reasonably relate to the activity taxed.

In the case at bar the measure of the tax is set forth in § 6.68.220(d) of Tacoma's B&O tax ordinance. The measure of the tax is a percentage of the gross proceeds from the construction contract. The question is whether such measure is fairly related to the activity of making the contract to construct the dam. General Motors Corp. v. Washington, 377 U.S. 436, 441, 84 S.Ct. 1564, 12 L.Ed.2d 430 (1964).

The fact that the value which the gross receipts measure is, in large part, the result of activity Outside the territorial limits of the taxing jurisdiction does not mean the gross receipts are not fairly related to the activity Within the jurisdiction. There is no constitutional objection to resorting to extra-territorial elements in determining the Measure of a tax. General Motors Corp. v. State, 60 Wash.2d 862, 874, 376 P.2d 843 (1962), aff'd in General Motors Corp. v. Washington, supra; Wisconsin v. J. C. Penney Co., supra, 311 U.S. at 445, 61 S.Ct. 246, rehearing denied, 312 U.S. 712, 61 S.Ct. 444, 85 L.Ed. 1143 (1941); Great Atl. & Pac. Tea Co. v. Grosjean, 301 U.S. 412, 425, 57 S.Ct. 772, 81 L.Ed. 1193 (1937).

In General Motors, we sustained a state tax imposed

Page 600

upon the privilege of engaging in business activities within the state, measured by General Motors' gross receipts from wholesale sales of motor vehicles, parts and accessories delivered in Washington. The fact that the gross receipts in large part represented extensive out-of-state manufacturing and operational activities did not mean that the gross receipts were not fairly related to the act of selling. As stated by the United States Supreme Court in the J. C. Penney Co. case 311 U.S. at 445, 61 S.Ct. at 250:

The fact that a tax is contingent upon events brought to pass without a state does not destroy the nexus between such a tax and transactions within a state for which the tax is an exaction.

In General Motors the local taxable incidents, the wholesale sales, were of sufficient substance that the sales price substantially reflected the value of the activities carried on within the state.

Dravo's transaction of making the contract with Tacoma, in the city, was a substantial income producing activity fairly related to the gross proceeds that accrued therefrom. Where the activity taxed is 'selling at retail', as defined by ordinance § 6.68.055(b), a city can tax the gross proceeds from sales made within the city even though the subject of the sale is without the city. Los Angeles v. Belridge Oil Co., 42 Cal.2d 823, 271 P.2d 5 (1954), appeal dismissed, 348 U.S. 907, 75 S.Ct. 292, 99 L.Ed. 711 (1955); Keystone Metal Co. v. City of Pittsburgh, 374 Pa. 323, 97 A.2d 797 (1953), cert. denied, 346 U.S. 887, 74 S.Ct. 139, 98 L.Ed. 391 (1953), rehearing denied, 346 U.S. 917, 74 S.Ct. 273, 98 L.Ed. 413 (1953). Thus, the fact that the dam was constructed in Lewis County is not determinative. Further, although Dravo maintained no office in Tacoma, that, in-and-of itself, is not controlling. General Motors Corp. v. State, 60 Wash.2d 862, 874, 376 P.2d 843 (1962).

As to the basic contract, the locus of the activity taxed (I.e., the making of the contract) occurred within the city, and provided a sufficient nexus upon which the city could

Page 601

base its B&O tax. [2] The B&O tax on the basic contract was constitutional. The record, however, is barren of evidence to indicate the locus of the place of making of the extra work contracts. Thus, as to the tax on the latter, we are unable to determine whether a constitutional nexus has been established.

Dravo's activity in contracting for and constructing the Mossyrock Project was wholly intrastate. Although the parties composing the joint venture are foreign corporations, the joint venture was formed for purely local purposes. Its entire operation took place within the borders of this [496 P.2d 511] state. No violation of the federal commerce clause is alleged and none can be asserted. State Tax Comm. v. Howard P. Foley Co., 13 Ariz.App. 85, 474 P.2d 444 (1970). It is, therefore, unnecessary to consider whether § 6.68.225 of the Tacoma B&O tax ordinance violates the federal commerce clause.

Dravo has, however, pleaded alternatively for an apportionment of the tax on the basic contract should we find the ordinance constitutional. Section 6.68.250 of the Tacoma B&O tax ordinance provides for apportionment as follows:

6.68.250 Business within and without city--Apportionment. Any person rendering services and maintaining places of business both within and without this city shall, for the purpose of computing tax liability under this section, apportion to this city that portion of his gross income which is derived from services rendered within this city. Where such apportionment cannot be accurately made by separate accounting methods, the taxpayer shall apportion to this city that proportion of his total income which the cost of doing business within the city bears to the total cost of doing business both within and without the city.

The question is whether the foregoing section requires apportionment in this case.

The state B&O tax statute contains an identical provision. RCW 82.04.460. Although we have not expressly construed

Page 602

the application of that section, we did consider it in Crown Zellerbach Corp. v. State, 45 Wash.2d 749, 278 P.2d 305 (1954). In that case Crown Zellerbach was taxed on its activity of extracting and manufacturing within the state. The measure of the tax was the value of the manufactured products which in turn was measured by the gross proceeds from their sales both within and without the state. Crown Zellerbach made no claim for apportionment, asserting instead a claim for total exemption. It contended the statutory scheme of the B&O tax assured that the local incidence of manufacture was not all that was taxed. Thus, it argued that its activity of selling interstate was indirectly subjected to an unconstitutional law. In referring to RCW 82.04.460, the apportionment provision, we point out that, contrary to Crown Zellerbach's argument, the statutory scheme assured that only the local incidence of manufacturing was being taxed.

In a second case, Crown Zellerbach Corp. v. State, 53 Wash.2d 813, 328 P.2d 884 (1958), Crown Zellerbach contended that since its sales promotion activities, carried on outside the state, were reflected in the gross sales price of products sold within the state, the first Crown Zellerbach case required an apportionment of the tax on wholesale sales within this state. We responded at 819, 328 P.2d at 888:

We do not agree that the cited case so holds because . . .. (2) the apportionment referred to therein concerns activities which are substantially a part of the taxable incident, rather than those activities which enhance only the measure of the tax.

Thus, under the statutory provision, apportionment is not applicable if the taxable incident or activity occurs entirely within the taxing jurisdiction. See also Fibreboard Paper Products Corp. v. State, 66 Wash.2d 87, 93, 401 P.2d 623 (1965); General Motors Corp. v. State, 60 Wash.2d 862, 878, 376 P.2d 843 (1962); United States Steel Corp. v. State, 51 Wash.2d 224, 226, 316 P.2d 1099 (1957).

Section 6.68.250 of the ordinance should be interpreted similarly. Only when the activity that is the incidence of

Page 603

the tax takes place both within and without the city does § 6.68.250 require an apportionment of the gross proceeds.

In the case before us the taxable activity was the making of the contract. It took place entirely within the city limits. Thus, § 6.68.250 does not apply.

We do not reach the question of whether due process may require an apportionment when two different taxing jurisdictions taxing separate activities, but both using gross proceeds as the measure of [496 P.2d 512] their taxes, [3] impose a multiple burden on a taxpayer. In such a case the burden would be on the taxpayer to establish the multiple tax burden. See General Motors Corp. v. Washington, 377 U.S. 436, 441, 84 S.Ct. 1564, 12 L.Ed.2d 430 (1964); Norton Co. v. Department of Revenue, 340 U.S. 534, 537, 71 S.Ct. 377, 95 L.Ed. 517 (1951). Dravo has made no such showing. The record indicates that the joint venture was subjected only to the Tacoma B&O tax.

The decision of the trial court is reversed insofar as it holds that § 6.68.225 is unconstitutional. However, it is affirmed insofar as it upholds Tacoma's entitlement to retain the $40,184.38. The case is remanded for a determination, in light of this opinion, as to whether there is a sufficient constitutional due process nexus for Tacoma to impose its B&O tax on Dravo's gross proceeds from the extra work contracts.

HAMILTON, C.J., FINLEY, ROSELLINI, HUNTER, HALE, and NEILL, JJ., and RYAN, J. pro tem., concur.

UTTER and WRIGHT, JJ., not participating.

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1 For discussion of the due process nexus requirements see Barnes, State Taxation of Interstate Commerce: Chaos and New Hope, 16 W.Res.L.Rev. 859, 864--871 (1965); Barnes, State Taxation of Interstate Commerce: Nexus and Apportionment, 48 Marq.L.Rev. 218 (1964); Federal Limitations on State Taxation of Interstate Business, 76 Harv.L.Rev. 953, 960--962 (1962); Annot., 67 A.L.R.2d 1322, 1329--1332 (1959).

2 See American Oil Co. v. Neill, 380 U.S. 451, 458, 85 S.Ct. 1130, 14 L.Ed.2d 1 (1965) and the discussion in the body of the instant opinion.

3 For a discussion of the problem raised when more than one municipality imposes taxes on intrastate commerce, See Sato, Municipal Occupation Taxes in California: The Authority to Levy Taxes and the Burden on Intrastate Commerce, 53 Cal.L.Rev. 801 (1965). California requires apportionment. See Los Angeles v. Shell Oil Co., 4 Cal.3d 108, 93 Cal.Rptr. 1, 480 P.2d 953 (1971); Los Angeles v. Belridge Oil Co., 48 Cal.2d 320, 309 P.2d 417 (1957); Los Angeles v. Belridge Oil Co., 42 Cal.2d 823, 271 P.2d 5 (1954), appeal dismissed, 348 U.S. 907, 75 S.Ct. 292, 99 L.Ed. 711 (1955).

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September 19, 2017

Rules Office
Hawaii Department of Taxation
830 Punchbowl Street, Room 221
Honolulu, HI 96813

Re: **Comments on Proposed Rules Relating to County Surcharge**

Ladies and Gentlemen:

The Notice of Public Hearing relating to these proposed rules states that the Department's intent is to simplify the county surcharge rules by deleting the requirement that the taxpayer have nexus with the county imposing the surcharge. The proposed rules as presented go far beyond that topic and raise several issues and concerns, discussed below.

A. Nexus with the County Imposing the Surcharge.

In state tax parlance, "nexus" usually refers to the requirement under the Commerce Clause of the U.S. Constitution that a person or entity have a presence in the jurisdiction that is trying to tax it. *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992). Here, it must be kept in mind that the county surcharge *is not* a state tax. Although the Hawaii Legislature has delegated the power to enact a surcharge on the GET and has prescribed standards and parameters for doing so, the surcharge is imposed by county ordinance. *See* HRS § 248-2.6; Rev. Ord. of Honolulu §§ 6-60.1 to 6-60.3. Thus, some demonstrable connection between the surcharging county and the prospective taxpayer may be necessary to satisfy constitutional requirements. Just as it would be unusual and unfair for Kauai County to impose its vehicular weight tax against a Nissan Sentra that is garaged in Pukalani and never strays from Maui County, it would seem odd for Honolulu to impose its county surcharge against a Lanai City bakery that occasionally accepts phone orders and ships a few loaves of sweet bread to Kaneohe.

B. Deletion of Sourcing Rule Relating to Commissions.

The proposed rules delete the entire section relating to sourcing of commissions, namely HAR § 18-237-8.6-04, and leave nothing in its place. This move has the potential to plunge the law in this area into chaos, with some taxpayers likely to interpret the deletion of the rule as a non-event and others likely to think that the services rules are now to apply to commissions. If the Department's intent is not to change the existing law, there should be no reason to delete the existing rule. If the Department does wish to change the law, we feel that the subject is significant enough so that the Department's intent needs to be made known in the notice of public hearing to comply with HRS § 91-3(a)(1).

C. Adoption of "Benefit to the District" Test.

In several of the existing rules, the Department allowed for the use of "any reasonable allocation method that clearly, fairly, and properly reflects the gross income to the appropriate taxation district; provided that the allocation method is documented." The proposed rules replace every occurrence of that standard with a standard like this:

> (b) If services are used or consumed in more than one taxation district, gross income shall be allocated using any reasonable method; provided that the method is consistently used by the taxpayer and supported by verifiable data that reasonably quantifies the proportionate benefit received by each taxation district.

Proposed § 18-237-8.6-03(b). We respectfully suggest that the new standard is a major change, is not an improvement over the old one, and has the potential to cause widespread confusion. Private parties have no idea how to measure the benefit received by a taxation district from a private business transaction (which transaction was never intended to benefit a taxation district in the first place). If the Department's aim is to require the "reasonable allocation method" to have an economic basis, then it could instead fashion a standard similar to that in the reimbursement rules, for example the standard in HAR § 18-237-20-06(e).

In any event, the change to the standard is significant. We do not believe that the existing Notice of Public Hearing apprises the public of the depth of the proposed change, and for that reason the validity of the rule may be called into question under HRS § 91-3(a)(1).

Thank you for the opportunity to submit comments.

Very truly yours,

Thomas Yamachika
President