

RESTRICTING THE SCOPE OF STATE TAXATION UPON AIRLINES: *ALOHA AIRLINES, INC. v.* *DIRECTOR OF TAXATION*

In seeking to increase state revenues without hurting domestic business operations, state governments have refrained from raising tax rates and, instead, have pursued the taxation of foreign business activities occurring within their borders.¹ Although the taxation power is regarded as essential to a state's existence,² federal law often regulates an area previously subject to state taxation and preempts the state from taxation of the regulated activity.³ This occurred when Congress passed section 7(a) of the Airport Development Acceleration Act of 1973 (ADAA).⁴ The ADAA denied states the right to raise revenues through the direct or indirect taxation of airline passengers,⁵ yet permitted states to levy airline taxes for general revenue-raising purposes. Consequently, numerous states continued to levy taxes under this general revenue-raising exception.⁶ In *Aloha Airlines, Inc. v. Director of Taxation*,⁷ the United States Supreme Court dealt a blow to these general revenue-raising rights by holding that the ADAA preempted a Hawaii general revenue-raising tax⁸ upon an

1. See generally L.K. HUBBELL, *FISCAL CRISIS IN AMERICAN CITIES: THE FEDERAL RESPONSE* 3-24 (1979).

2. Chief Justice John Marshall stated in *Gibbons v. Ogden*, 22 U.S. (9 Wheat.) 1 (1824): "The power of taxation is indispensable to their [the states'] existence, and is a power which, in its own nature, is capable of residing in, and being exercised by different authorities at the same time." *Id.* at 199.

3. For an explanation of the methods of federal preemption, see *infra* notes 29-32 and accompanying text.

4. Pub. L. No. 93-44, § 7(a), 87 Stat. 88, 90 (1973) (codified as amended at 49 U.S.C. § 1513 (1982)) [hereinafter referred to as the ADAA or the Act]. For the effect of the 1982 amendment upon § 1513, see *infra* note 44.

5. For relevant text of 49 U.S.C. §§ 1513(a), (b) (1982), see *infra* note 44.

6. 49 U.S.C. § 1513(b) allows general revenue-raising taxes such as personal property taxes, franchise taxes, net income taxes, and sales and use taxes. For relevant text of the statute, see *infra* note 44.

7. 104 S. Ct. 291 (1983).

8. For the text of the Hawaii taxing statute, see *infra* note 11.

airline's gross receipts.

Aloha Airlines, Inc. is a Hawaii corporation engaged in the interisland air transportation of persons, property, and mail within Hawaii.⁹ Hawaii law classified Aloha Airlines as a "Public Service Company"¹⁰ and subjected it to a Public Service Tax of four percent upon its gross receipts.¹¹ Aloha Airlines challenged the constitutionality of the tax in light of the ADAA¹² and filed its tax returns showing no liability.¹³ The Hawaii Director of Taxation (Director) then made assessments consistent with the unpaid tax.¹⁴ Aloha Airlines appealed to the Hawaii Tax Appeal Court which concluded that the Director had made proper assessments and that the Public Service Tax was both a "property tax and a general tax."¹⁵ On appeal, the Hawaii Supreme Court affirmed,¹⁶ holding that the tax violated neither the commerce clause¹⁷ nor the supremacy clause¹⁸ of the Fed-

9. 104 S. Ct. 291, 293 (1983).

10. Hawaii law includes all public utilities within the definition of Public Service Companies. HAWAII REV. STAT. § 239-2 (1976). Prior to 1981, a public utility included "any person, insofar as such person owns or operates an aerial transportation enterprise as a common carrier." HAWAII REV. STAT. § 269-1 (1976). In 1981, the state legislature amended § 269-1 to remove air common carriers from the definition of public utilities. HAWAII REV. STAT. § 269-1 (Supp. 1983). Aloha Airlines and other air common carriers remain liable for the tax levied by HAWAII REV. STAT. § 239-6 (1976). For the text of § 239-6, see *infra* note 11.

11. The statute reads, in pertinent part:

§ 239-6 *Airlines, certain carriers.* There shall be levied and assessed upon each airline a tax of four percent of its gross income each year from the airline business; . . . The tax imposed by this section is a means of taxing the personal property of the airline or other carrier, tangible and intangible, including going concern value, and is in lieu of the tax imposed by chapter 237, but not in lieu of any other tax.

HAWAII REV. STAT. § 239-6 (1976) (emphasis in original).

12. See *infra* note 44.

13. Aloha Airlines filed amended returns for 1973, 1974, 1975, and 1976 and its initial 1977 return showing no tax liability. *In re Aloha Airlines, Inc.*, 65 Hawaii 1, 5, 647 P.2d 263, 267 (1982), *rev'd sub nom.* Aloha Airlines, Inc. v. Director of Taxation, 104 S. Ct. 291 (1983).

14. 65 Hawaii at 5, 647 P.2d at 267. Also, the claims for refund on Aloha's amended returns were denied. *Id.*

15. *In re Aloha Airlines, Inc.* ST. TAX REP. [Hawaii] (CCH) ¶ 200-118 (Hawaii Tax App. Ct. June 6, 1978).

16. 65 Hawaii 1, 647 P.2d 263 (1982).

17. The commerce clause provides: "The Congress shall have Power . . . To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes." U.S. CONST. art. I, § 8, cl. 3.

18. Article VI of the United States Constitution provides in pertinent part:

eral Constitution.¹⁹ The United States Supreme Court reversed, declaring that the ADAA preempted the tax.²⁰

The traditional constitutional attack upon state taxation of interstate commerce arises from the commerce clause.²¹ Prior to 1977, courts treated state taxation of interstate commerce as regulatory in nature and in conflict with Congress' power to regulate commerce.²² Courts held that taxes on the privilege of doing business in interstate

This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.

U.S. CONST. art. VI, cl. 2.

19. 65 Hawaii 1, 13, 19, 647 P.2d 263, 271, 275 (1982), *rev'd sub nom.* Aloha Airlines, Inc. v. Director of Taxation, 104 S. Ct. 291 (1983).

20. 104 S. Ct. 291, 295 (1983).

21. For text of the commerce clause, see *supra* note 17. Congress has the sole power to regulate interstate commerce, and any state tax upon interstate commerce regulates interstate commerce. See *infra* notes 22-24 and accompanying text (discussing the development of judicial commerce clause analysis of state taxation). Several approaches have been taken by the Supreme Court. The state tax might discriminate against interstate or foreign commerce and thus be invalid. See *Boston Stock Exch. v. State Tax Comm'n*, 429 U.S. 318, 328-32 (1977). Similarly, the risk of multiple taxation might not be borne by similar local commerce. See *Evco v. Jones*, 409 U.S. 91, 93-94 (1972). The state tax could apportion unfairly income or property to more than one state. See *Norfolk & W. Ry. Co. v. Tax Comm'n*, 390 U.S. 317, 329 (1968). Finally, a tax is invalid if there is an absence of due process jurisdiction to tax. See *McLeod v. J.E. Dilworth Co.*, 322 U.S. 327, 328-30 (1944); Lockhart, *Revolution in State Taxation of Commerce?*, 65 MINN. L. REV. 1025, 1029 (1981).

22. Prior to the drafting of the commerce clause, the framers of the Constitution suggested that interstate commerce should be immune from state taxation. See generally Hellerstein, *State Taxation of Interstate Business and the Supreme Court, 1974 Term: Standard Pressed Steel and Colonial Pipeline*, 62 VA. L. REV. 149 (1976). On various occasions the Supreme Court expressed its desire to insulate interstate commerce from state taxation. To the Court, state taxation usurped Congress' exclusive commerce regulatory power. See *Leloup v. Port of Mobile*, 127 U.S. 640 (1888); *Reading R.R. Co. v. Pennsylvania*, 82 U.S. (15 Wall.) 284 (1872); *Reading R.R. Co. v. Pennsylvania*, 82 U.S. (15 Wall.) 232 (1872).

Although other bases existed for striking down state taxes, see *supra* note 21 and accompanying text, this viewpoint survived for more than a century until *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977). See *infra* notes 25-28 and accompanying text. Immunity from state taxation served as the basis for disallowing many types of state taxes. See, e.g., *Spector Motor Serv., Inc. v. O'Connor*, 340 U.S. 602 (1951) (excise tax on the privilege of doing business); *Freeman v. Hewit*, 329 U.S. 249 (1946) (gross receipts tax on interstate sales); *McLeod v. J.E. Dilworth Co.*, 322 U.S. 327 (1944) (retail sales tax applied to interstate sales in the buyer's state).

commerce were unconstitutional per se,²³ and sustained only privilege taxes upon doing business within a state.²⁴ This strict view of state taxation was reversed in 1977 when the United States Supreme Court decided *Complete Auto Transit, Inc. v. Brady*²⁵ and held that the validity of a state tax depends upon its "practical effect."²⁶ In *Complete Auto* the Supreme Court held that a state may require interstate commerce to pay its fair share of the cost of state government.²⁷ The Court determined that a state tax does not violate the commerce clause when it is applied to an interstate activity 1) with a substantial nexus within the taxing state; 2) that is fairly apportioned; 3) that does not discriminate against interstate commerce; and 4) that is fairly related to services provided by the state.²⁸

When Congress enacts legislation that regulates interstate commerce, state taxation must not only survive commerce clause chal-

23. See, e.g., *Spector Motor Serv., Inc. v. O'Connor*, 340 U.S. 602, 608-10 (1951).

24. The courts sustained numerous taxes on the premise that interstate business had to pay its share of local government expenses. Only taxes found as sufficiently remote from interstate commerce, however, proved valid. See, e.g., *Exxon Corp. v. Wisconsin Dep't of Revenue*, 447 U.S. 207, 219-30 (1980) (gross receipts tax); *Braniff Airways, Inc. v. Nebraska State Bd. of Equalization & Assessment*, 347 U.S. 590, 601-02 (1954) (property taxes); *McGoldrick v. Berwind-White Coal Mining Co.*, 309 U.S. 33, 48-59 (1940) (retail sales tax); *Western Live Stock v. Bureau of Revenue*, 303 U.S. 250, 254 (1938) (privilege taxes on intrastate activities); *Henneford v. Silas Mason Co., Inc.* 300 U.S. 577, 582 (1937) (compensatory use tax on goods acquired through an interstate transaction).

25. 430 U.S. 274 (1977).

26. *Id.* at 278.

27. *Id.* at 287-89.

28. *Id.* at 287.

As stated by Lockhart, this four-part test represents a consolidation of previously used tests, each of which contains a complex set of factors. They are as follows: 1) "Substantial Nexus," see, e.g., *Braniff Airways, Inc. v. Nebraska State Bd. of Equalization & Assessment*, 347 U.S. 590 (1954); 2) "Fairly Apportioned," see, e.g., *Norfolk & W. Ry. Co. v. Missouri State Tax Comm'n*, 390 U.S. 317 (1968); 3) "Discrimination," see, e.g., *Boston Stock Exch. v. State Tax Comm'n*, 429 U.S. 318 (1977); and 4) "Related to Services," see, e.g., *Standard Pressed Steel Co. v. Department of Revenue*, 419 U.S. 560 (1975). LOCKHART, *supra* note 21, at 1037.

The Supreme Court clarified the test's fourth prong in *Commonwealth Edison Co. v. Montana*, 453 U.S. 609 (1981). The Court held that there is no due process clause requirement that the amount of general revenue taxes collected from an activity must be reasonably related to that activity. Consequently, states have latitude in levying general revenue taxes. *Id.* at 622. The framers did not intend the commerce clause to relieve those engaged in interstate commerce from their just share of state tax burdens even though it increases the cost of doing business. *Western Live Stock v. Bureau of Revenue*, 303 U.S. 250, 254 (1938).

lenges, but also supremacy clause challenges.²⁹ If the federal legislation does not expressly preempt the state taxation power, the courts must look to other factors that demonstrate congressional intent.³⁰ There is no formalized test similar to the commerce clause analysis in *Complete Auto* to determine whether a state provision is preempted by reason of the supremacy clause. Instead, as stated in *Rice v. Santa Fe Elevator Corp.*,³¹ courts must probe the nature of the federal enactment as well as the area sought to be regulated before declaring the state's action preempted under the supremacy clause.³²

Congress passed the Airport and Airway Development Act of 1970³³ to provide for the expansion and improvement³⁴ of the nation's airways and airports.³⁵ Funding for the Act's programs originated from federal taxes upon airline passenger tickets.³⁶ Prior

29. See *Hines v. Davidowitz*, 312 U.S. 52, 62-74 (1941).

30. See *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 236 (1947).

31. 331 U.S. 218 (1947).

32. Federal regulation may be so pervasive that a "reasonable inference" might exist to conclude that Congress left no room for states to supplement it. See *Cloverleaf Butter Co. v. Patterson*, 315 U.S. 148, 167-69 (1942); *Pennsylvania R.R. Co. v. Public Serv. Comm'n*, 250 U.S. 566, 569 (1919). The congressional enactment may touch a field that the federal system predominates so as to preclude enforcement of state laws on the same subject. See *Hines v. Davidowitz*, 312 U.S. 52, 62-74 (1941). In addition, the objective of the federal legislation and the character of obligations imposed by it may indicate the same legislative purpose. See *Napier v. Atlantic Coast Line R.R. Co.*, 272 U.S. 605, 608-13 (1926); *New York Cent. R.R. Co. v. Winfield*, 244 U.S. 147, 148-54 (1917); *Charleston & W.C. Ry. Co. v. Varnville Furniture Co.*, 237 U.S. 597, 603-04 (1915); *Southern Ry. Co. v. Railroad Comm'n*, 236 U.S. 439, 445-48 (1915). Finally, the state policy may produce a result that is inconsistent with the federal statute. *Hill v. Florida ex rel. Watson*, 325 U.S. 538, 541-43 (1945).

33. Pub. L. No. 91-258, 84 Stat. 219 (1970), codified at 49 U.S.C. § 1701 (1976), repealed by Pub. L. 97-248, Title V, § 523(a), 96 Stat. 671 (1982) (current version at 49 U.S.C. § 2201 (1982)).

34. 49 U.S.C. § 1701 (1970).

35. Congress had found that the nation's airways and airports were inadequate to deal with current and potential aviation growth:

Over the past 5 years, the certified air carrier fleet has increased from a substantially piston fleet of 2,079 aircraft to an almost completely jet fleet of 2,586 aircraft. In terms of capacity, the seat miles flown have increased from 94.8 billion seat miles to 210 billion. By 1980 it is estimated that the domestic certified airlines will enplane 420 million passengers, almost tripling the 1969 figure.

H.R. REP. NO. 601, 91st Cong., 1st Sess. 5 (1970), reprinted in 1970 U.S. CODE CONG. & AD. NEWS 3047, 3051.

36. The Airport and Airway Revenue Act of 1970, Pub. L. 91-258, § 208, 84 Stat. 236, 250-52 (1970), established a trust fund for the ADAA's expenditures. The fund received revenues from an 8% tax on domestic airline tickets, a \$3.00 charge upon

to the 1970 enactment, some states had attempted to levy head taxes³⁷ on enplaning passengers in order to fund their own airport improvement programs.³⁸ The passage of the Act threatened federal preemption of these head taxes. In *Evansville-Vanderburgh Airport Authority District v. Delta Airlines, Inc.*³⁹ the United States Supreme Court ended the confusion temporarily when it declared constitutional a one-dollar state head tax on enplaning passengers.⁴⁰

The decision in *Evansville Airport* sparked an increase in the number of new airport head taxes.⁴¹ Congress, which had not ex-

international flight tickets, and a 5% tax on air freight. Pub. L. 91-258, §§ 4261, 4271, 84 Stat. 236, 238-40 (codified as amended at 26 U.S.C. §§ 4261, 4271 (1982)).

37. "Head Money" is defined as "[a] sum of money reckoned at a fixed amount for each head (person) in a designated class." BLACK'S LAW DICTIONARY 648 (5th ed. 1979).

38. See, e.g., N.H. REV. STAT. ANN. § 422.43 (1983).

Even after enactment of the ADAA of 1970, the United States' share of the costs of an airport or airway improvement program could not exceed 50% of the allowable project costs. 49 U.S.C. § 1717 (1970). Two years later this section was amended to increase the allowable United States' share of costs to 75%. 49 U.S.C. § 1717 (Supp. III 1973), repealed by Pub. L. 97-248, Title V, § 523(a), 96 Stat. 695 (1982). Presently, fund apportionment is based upon the number of enplaning passengers at a local airport. 49 U.S.C. § 2206 (1982).

39. 405 U.S. 707 (1972). The Supreme Court upheld the constitutionality of the tax based upon its practical effect and not upon its computation formula. *Id.* at 716. In doing so, the Supreme Court held that states may constitutionally charge interstate and domestic users of state-provided facilities a reasonable fee to defray the costs of the facilities' maintenance. *Id.* at 714.

In addition, the Supreme Court distinguished *Crandall v. Nevada*, 73 U.S. (6 Wall.) 35 (1867), an earlier case that had disallowed a head tax on passengers riding private railroads that passed through Utah. The Supreme Court noted that in *Crandall* the head tax was imposed upon private railroads and their passengers, and not related to state-provided facilities. 405 U.S. at 712. This tax deprived passengers of the benefits of the State tax. *Id.* In *Evansville Airport*, the local government administered a head tax in a public airport upon passengers who enjoyed the benefits of the airport maintenance paid for by such funds. *Id.* at 709. A facility provided at public expense aids, rather than hinders, travel. *Id.* at 714.

40. For state court decisions prior to *Evansville Airport* holding head taxes unconstitutional, see, e.g., *Northwest Airlines, Inc. v. Joint City-County Airport Bd.*, 154 Mont. 352, 463 P.2d 470 (1970) (one dollar enplaning charge held unconstitutional); *Allegheny Airlines, Inc. v. Sills*, 110 N.J. Super. 54, 264 A.2d 268 (N.J. Super. Ct. Ch. Div. 1970) (service charge on enplaning passengers held unconstitutional).

41. As of 1972, several jurisdictions either had head taxes ranging from \$.50 to \$3.00 or were considering legislation to establish similar changes. See H.R. REP. NO. 1279, 92d Cong., 2d Sess. 3-4 (1972).

pected the Supreme Court to rule the head tax constitutional,⁴² rected by passing the Airport Development Acceleration Act of 1973,⁴³ which included a prohibition against airport head taxes. The statute explicitly prohibited state taxation of persons traveling by air transportation.⁴⁴ In addition, it proscribed taxation of the "carriage" of air travelers, the sale of such transportation, and the resulting gross receipts.⁴⁵ Congress left intact a state's right to levy other taxes for

42. See S. REP. NO. 12, 93d Cong., 1st Sess. 21 (1973). The Senate Report reads, in pertinent part:

[The Senate Commerce] Committee never intended that air travelers would be subject to state and local head taxes as well as to national user charges. The Committee believed there was no danger of this because the basic constitutional guarantee of a citizen's right to unhindered interstate travel, and a U.S. Supreme Court decision which had prevailed since 1867, indicated such taxes could not be constitutionally imposed. It is unfair that this is happening now since state and local head taxes constitute an inequitable, double burden of taxation on air passengers.

Id. at 21 (referring to *Crandall v. Nebraska*, 73 U.S. (6 Wall.) 35 (1867)).

Congress also voiced a concern over the inflexibility of the head tax. First, the head tax would penalize those passengers in smaller cities that would have to use connecting flights and enplane more than once. *Hearings on S. 2397, S. 3611, and S. 3755 Before the Subcomm. on Aviation of the Senate Comm. on Commerce*, 92d Cong., 2d Sess. 137 (1972). (comment of W. Gilliland, Vice-Chairman, Civil Aeronautics Board). Second, the fixed fee, when applied to small fares, would constitute a substantial increase in the fare as opposed to the increase to a higher-priced ticket. *Id.* at 175. (statement of R. Sorlien, Vice-President of Altair Airlines, Inc.).

43. Pub. L. No. 93-44, § 7(a), 87 Stat. 88, 90 (1973) (codified as amended at 49 U.S.C. § 1513 (1982)).

44. 49 U.S.C. § 1513 (1976). In 1982, Congress amended § 1513 to address local property taxes that unreasonably burden and discriminate against interstate commerce. Although the amendment has no bearing upon the proceedings in *Aloha Airlines*, it still provides valuable insight into congressional intent as to the types of permissible taxes upon air commerce.

The amendment, in relevant part, prohibits a state from levying property taxes that:

1)(A) assess air carrier transportation at a value that has a higher ratio to the true market value of air carrier transportation property than the ratio that the assessed value of other commercial and industrial property of the same type in the same assessment jurisdiction has to the true market value of the other commercial and industrial property. . . .

(C) levy or collect an ad valorem property tax on air carrier transportation property at a tax rate that exceeds the tax rate applicable to commercial and industrial property in the same assessment jurisdiction.

3) This subsection shall not apply to any in lieu tax which is wholly utilized for airport and aeronautical purposes.

49 U.S.C. § 1513(d) (1982).

45. *Id.*

general revenue-raising purposes.⁴⁶ As a result of this enactment, the ADAA preempted numerous state head tax schemes.⁴⁷

Although the Hawaii statute⁴⁸ designates the airline tax as a "personal property tax,"⁴⁹ it is computed upon the gross receipts of an airline⁵⁰ and is in lieu of an excise tax.⁵¹ The valuation of property by a gross receipts method has been successful in the valuation of

46. *Id.* § 1513(b).

47. *See, e.g.,* Allegheny Airlines, Inc. v. City of Philadelphia, 453 Pa. 181, 309 A.2d 157 (1973) (head tax on deplaning and enplaning passengers held unconstitutional).

48. *See supra* note 11 for the text of HAWAII REV. STAT. § 239-6.

49. Beginning in 1933, Hawaii classified airlines as public utilities and subjected them to a Public Utility Tax upon their gross receipts. 1927 Hawaii Sess. Laws Act 100. Twenty years later, the Hawaii legislature removed airlines from the Public Utility Tax but subjected them to the General Excise Tax Law. 1953 Hawaii Sess. Laws Act 279. (The General Excise Tax is discussed *infra* at note 51.). Finally, in 1963, airlines were reclassified as Public Service Companies along with public utilities and subjected to the redesignated Public Service Tax. 1963 Hawaii Sess. Laws Act 147, § 2(a). As of 1982, airlines are no longer classified as Public Service Companies but are still subject to the tax. *See supra* note 10. Presently, airlines are subject to a flat tax rate applied against their "gross income" under HAWAII REV. STAT. § 239-6.

"Gross Income" means gross income derived from public service business defined as follows: "(B) [g]ross income from the transportation of passengers or freight . . . by land or water or air . . . [o]riginating and terminating within this State." *Id.* The statute has been amended by HAWAII REV. STAT. § 239-2(6) (Supp. 1977).

50. *See supra* note 11 for text of HAWAII REV. STAT. § 239-6. Hawaii has not had a personal property tax since 1947. A personal property tax that existed prior to 1932 did include the following provision: "In estimating the aggregate value of each such enterprise for profit, there shall be taken into consideration the net profits made by the same, also the gross receipts . . . as well as all other facts and considerations which reasonably . . . bear on such valuation." 1921 Hawaii Sess. Law Act 250, codified at REV. LAW HAWAII § 1320 (1925) (now HAWAII REV. STAT.) (repealed 1932).

51. The exact language of HAWAII REV. STAT. § 239-6 is "in lieu of the tax imposed by Chapter 237." *See supra* note 11 for the text of § 239-6.

Chapter 237 is the General Excise Tax Law, HAWAII REV. STAT. § 237 (1976 & Supp. 1983). The chapter levies "privilege taxes against persons on account of their business and other activities in the State measured by the application of rates against values of products, gross proceeds of sales, or gross income, whichever is specified. . . ." HAWAII REV. STAT. § 237-13 (Supp. 1983).

Although there is a conflict in terms between the chapter's title "General Excise Tax Laws" and the assessing section's labeling of the tax as a "privilege tax," the operation of the tax and not the description will control its meaning. *See Herman v. City of Baltimore*, 189 Md. 191, 198, 55 A.2d 491, 495 (1947). Excise taxes are imposed upon manufacture, sale, or consumption of commodities, upon licenses to pursue certain occupations, and upon corporate privileges. *See Flint v. Stone Tracy Co.*, 220 U.S. 107 (1911); *Blaustein v. Levin*, 176 Md. 423, 4 A.2d 861 (1939).

public utilities.⁵² Yet, labeling of a tax as a personal property tax does not determine its true character.⁵³ Although some weight is given to a tax's title,⁵⁴ courts look to the operation of the statute in order to determine a tax's character.⁵⁵

The Hawaii Supreme Court utilized the four-part commerce clause test as described in *Complete Auto*.⁵⁶ Aloha Airlines protested that the state tax did not meet the fourth prong of the test, asserting that "the tax was not fairly related to the services provided by the

52. The United States Supreme Court has allowed the gross receipts method for property valuation. *See, e.g.*, *Cudahy Packing Co. v. Minnesota*, 246 U.S. 450 (1918); *United States Express Co. v. Minnesota*, 223 U.S. 335 (1912).

Hawaii courts followed these holdings and determined that the Hawaii Public Utility Tax imposed a tax similar to the *ad valorem* real and personal property taxes otherwise imposed. *Hawaii Consol. Ry. v. Borthwick*, 34 Hawaii 269, 281 (1937), *aff'd*, 105 F.2d 286 (9th Cir. 1939) (public utility found subject to the gross receipts tax). In *Consolidated Railway*, however, the Hawaii Supreme Court noted that the tax's similarity to an "ad valorem tax" originated from its computation based on the ratio obtained between the net and gross income of the utility business and not based on a flat rate. *Id.* Contrary to this rationale, the present Hawaii Public Service Tax on airlines does not use a variable rate, but a flat one. HAWAII REV. STAT. § 239-6 (1976 & Supp. 1983). *See supra* note 11.

Some courts have held that excise taxes passed on to consumers "may or may not have an ad valorem factor therein." *Powell v. Gleason*, 50 Ariz. 542, 548, 74 P.2d 47, 50 (1937). *But see Herman v. City of Baltimore*, 189 Md. 191, 197, 55 A.2d 491, 495 (1947) (excise taxes never can be property taxes because the latter are based on ownership alone).

Public utility property traditionally is difficult to value because the majority of the property is capitalized in stock and bonds with variable market values. Luce, *Assessment of Real Property for Taxation*, 35 MICH. L. REV. 1217, 1233 (1937). Yet, the gross income method of valuation (similar to HAWAII REV. STAT. § 239-6) has resulted in a reasonable and efficient method of valuing public utility property. *See Ravage, Valuation of Public Utilities for Ad Valorem Taxation*, 41 YALE L.J. 487, 514-17 (1932).

53. *See, e.g.*, *Storoasli v. Minnesota*, 283 U.S. 57, 62-63 (1931).

54. In determining the nature of a tax, the statute's labeling of the tax's character is a relevant factor. *See, e.g.*, *Lutz v. Arnold*, 208 Ind. 480, 491, 193 N.E. 840, 844 (1955). Some courts have held the effect should be (at least) persuasive. *See, e.g.*, *George E. Breece Lumber Co. v. Mirabal*, 34 N.M. 643, 647, 287 P. 699, 700 (1930), *aff'd per curiam*, 283 U.S. 788 (1931). Also, the opinion of a state court of the tax's nature is given due weight, but is not conclusive. *See, e.g.*, *Society for Savings in the City of Cleveland v. Bowers*, 349 U.S. 143, 151-54 (1955).

55. *See, e.g.*, *Educational Films Corp. of Am. v. Ward*, 282 U.S. 379, 387 (1931).

56. *In re Aloha Airlines, Inc.*, 65 Hawaii 1, 12, 647 P.2d 263, 271 (1982) (citing *Complete Auto Transit*, 430 U.S. 274 (1977)), *rev'd sub nom.* *Aloha Airlines, Inc. v. Director of Taxation*, 104 S. Ct. 291 (1983). *See also* text accompanying notes 25-28 (four-part *Complete Auto* test).

State."⁵⁷ The court rejected Aloha Airline's contention, noting that the revenue collected from the tax on airline activity helped to create a trained work force and a civilized society.⁵⁸ These benefits relate to the state tax that the Hawaii statute imposed.⁵⁹

The Hawaii Supreme Court also held that the Hawaii tax did not conflict with the ADAA's prohibition against gross receipts taxes.⁶⁰ The court noted that the ADAA prohibited state and local charges on air commerce but allowed a wide variety of other state and local taxes.⁶¹ The court labeled this process as a paradox in the statute which reflected congressional intent not to prohibit all state taxation of air transportation.⁶² Noting the federal preemption rules used in *Rice*,⁶³ the court found determinative the fact that the ADAA did

57. 65 Hawaii at 12, 647 P.2d at 271. Aloha Airlines asserted that the tax receipts derived from HAWAII REV. STAT. § 239-6 did not directly fund airport and airline activities but, instead, funded general government costs. *Id.*

58. *Id.* The Hawaii Supreme Court noted that in *Commonwealth Edison Co. v. Montana*, 453 U.S. 609 (1981), the United States Supreme Court held that there is no requirement for the state taxes derived from a particular activity to reasonably relate to the value of services provided to that activity. 65 Hawaii at 12, 647 P.2d at 271 (quoting *Commonwealth Edison*, 453 U.S. 609, 622 (1981)). Thus, Aloha Airlines must pay its fair share of the costs to provide "a trained work force and the advantages of a civilized society." 65 Hawaii at 13, 647 P.2d at 271 (quoting *Japan Line, Ltd. v. County of Los Angeles*, 441 U.S. 434, 445 (1979)).

59. 65 Hawaii at 13, 647 P.2d at 271.

60. *Id.* at 13-19, 647 P.2d at 271-75.

61. *Id.* at 16, 647 P.2d at 273.

62. *Id.* at 16-17, 647 P.2d at 273-74. The Hawaii Supreme Court noted that the "paradox" of the ADAA's allowance of general revenue taxes in § 1513(b), see *supra* text accompanying note 48, and its disallowance of other direct taxes in § 1513(a), see *supra* text accompanying note 44, necessitated a deeper analysis of the statute's purpose. *Id.*

63. See *supra* notes 31-32 and accompanying text.

The Hawaii Supreme Court began with an analysis similar to that used by the United States Supreme Court in *Rice* when it first noted that a state's taxation power is essential to its existence. *Id.* at 14, 647 P.2d at 272 (quoting *Gibbins v. Ogden*, 22 U.S. (9 Wheat.) 1, 199 (1824)). See *supra* note 2. Thus, when a federal statute does not expressly preempt a state taxation power, the courts must presume that the statute did not intend to supersede the state tax. *Aloha Airlines*, 65 Hawaii at 15, 647 P.2d at 273.

In addition, the Court noted that the purpose of § 1513 was to protect the primary source of revenue for the Airport and Airway Revenue Act of 1970. *Id.* at 17, 647 P.2d at 274. The legislative history of § 1513, see *supra* notes 41-43 and accompanying text, indicated congressional annoyance with head taxes that appeared to burden interstate commerce. 65 Hawaii at 17, 647 P.2d at 274. The Hawaii Supreme Court did reason, however, that § 1513's prohibition of head taxes attempted to prevent state encroachment upon Congress' source of revenue. *Id.*

allow for general revenue-raising taxes,⁶⁴ and that the tax levied by the Hawaii statute had some attributes similar to a property tax.⁶⁵ The court sustained the tax, holding that the Hawaii airline tax did not attempt to regulate airlines⁶⁶ and did not frustrate the purpose of the ADAA.⁶⁷

The dissent in *Aloha Airlines* focused on the majority's cursory treatment of the literal conflict of the Hawaii statute's tax upon gross receipts with the ADAA's prohibition of state taxes upon airline gross receipts.⁶⁸ The dissent stated that conflict in itself should render the Hawaii tax unconstitutional by means of preemption.⁶⁹ Furthermore, the dissent noted that the Hawaii tax had none of the attributes of any past Hawaii property taxes and implied that the characterization of the tax in this manner merely served as a legislative means to avoid federal preemption.⁷⁰

In a unanimous decision, the United States Supreme Court overturned the Hawaii Supreme Court's ruling and held that the ADAA expressly preempted the Hawaii tax.⁷¹ The Court held that the ADAA unambiguously disallowed state taxes upon the gross receipts of airlines and that the Hawaii Supreme Court had erred in looking beyond the plain language of the statute to determine Congress' purpose.⁷² Furthermore, the Court held that nothing in the legislative history of the ADAA implied a congressional purpose to limit the

64. *Id.* at 17, 647 P.2d at 273. *See supra* text accompanying note 48.

65. *Id.* at 17, 647 P.2d at 274. The Hawaii Supreme Court noted that in *Hawaii Consol. Ry. v. Borthwick*, 34 Hawaii 269 (1937), *aff'd*, 105 F.2d 286 (9th Cir. 1939), its territorial predecessor had held that the Public Utility Tax based upon gross receipts was a fair and reasonable method of computing property value. 65 Hawaii at 17, 647 P.2d at 268 (quoting *Hawaii Consol. Ry. v. Borthwick*, 34 Hawaii 269, 280, 281 (1937), *aff'd*, 105 F.2d 286 (9th Cir. 1939)). *See supra* notes 50-55 and accompanying text.

66. 65 Hawaii at 18, 647 P.2d at 275.

67. *Id.* at 18, 647 P.2d at 275.

68. *Id.* at 20, 647 P.2d at 275-76.

69. *Id.* at 20, 647 P.2d at 275.

70. *Id.* at 20, 647 P.2d at 275-76.

71. 104 S. Ct. 291 (1983).

72. *Id.* at 294. The Court did not find, as did the Hawaii Supreme Court, a "paradox" in § 1513. The Court stated that § 1513(a) preempted specifically some state airline taxes, including gross receipts taxes, while § 1513(b) allowed some general revenue taxes which were not preempted expressly in § 1513(a). *Id.* at 294 n.6. The Court did not explain the distinction between gross receipts taxes and those taxes described in § 1513(b).

preemptive effect of the Act to airline passenger taxes.⁷³ Finally, the Court disagreed with Hawaii's claim that the Hawaii tax should escape preemption because of its characterization as a personal property tax.⁷⁴ The Court noted that the Hawaii Legislature's description of the tax was not unclear in its purpose and intended effect of levying a tax upon the gross receipts of airlines.⁷⁵

As the Court stated correctly,⁷⁶ and the Hawaii Supreme Court attempted to avoid,⁷⁷ the method of computing the Hawaii tax⁷⁸ conflicted directly with the ADAA's prohibition against gross receipt taxes.⁷⁹ Although Congress did provide for the continuance of some general revenue-raising taxes upon airlines,⁸⁰ it clearly prohibited any gross receipts tax.⁸¹ Although no legislative history exists that

73. *Id.* at 294-95. The Court also noted that during the House hearings on the ADAA, an Ohio congressman suggested expanding § 1513(b) to allow "gross receipts taxes fairly apportioned to a State." *Id.* at 294 n.7 (quoting *Hearings on H.R. 4082 before the Subcomm. on Transportation and Aeronautics of the House Comm. on Interstate and Foreign Commerce*, 93d Cong., 1st Sess., 246-53 (1973)). Subsequently, when Congress passed § 1513(b) without the change, the Ohio Attorney General concluded that this preempted Ohio's gross receipts tax. *Id.* (citing Ohio Op. Atty. Gen. 73-117 (Nov. 20, 1973)).

74. 104 S. Ct. at 295.

75. *Id.*

76. *See supra* notes 71-75 and accompanying text.

77. *See supra* notes 56-67 and accompanying text. Although the Hawaii Supreme Court cited authority holding that the Public Utility Tax was similar to a personal property tax, the court did not address the issue whether an airline is properly classified as a "public utility." *See supra* note 65 and accompanying text. Public utilities, unlike airlines, have a substantial amount of their assets in bonds. *See supra* note 52. This sometimes necessitates the use of a gross receipts valuation method. *See generally* Ravage, *Valuation of Public Utilities for Ad Valorem Taxation*, 41 YALE L.J. 487 (1932).

In addition, the § 239-6 tax is "in lieu of the taxes imposed by Chapter 237" which are general excise taxes and not property taxes. *See supra* notes 50-54. Although excise taxes are permissible under § 1513(b), § 1513(a) still prohibits any tax computed upon an airline's gross receipts. *See supra* text accompanying note 45. *But see infra* note 81.

78. *See supra* notes 11, 48-50 and accompanying text.

79. *See supra* note 45 and accompanying text.

80. *See supra* note 44 and accompanying text.

81. *See supra* note 45 and accompanying text. The Supreme Court stated that the express prohibition of gross receipts taxes in § 1513 precluded any further preemption tests. 104 S. Ct. at 295 n.10. Also problematic is that § 1513(b) permits sales and use taxes on the sale of goods or services, yet § 1513(a) prevents gross receipt taxes. The Court's interpretation of Congress' blanket intention to disallow all taxes based upon

manifests Congress' intention of prohibiting gross receipts taxes,⁸² Congress made the choice to disallow such taxes and congressional intent must be followed.⁸³ Thus, general revenue-raising taxes based upon an airline's gross receipts are unconstitutional in light of the ADAA.⁸⁴

After *Aloha Airlines*, all state taxes computed upon the gross receipts of airlines are subject to preemption by the ADAA.⁸⁵ Even if the tax more closely resembles a permissible general revenue-raising tax that other interstate businesses bear equally,⁸⁶ as opposed to a head tax upon airlines and their passengers,⁸⁷ the Court's holding in *Aloha Airlines* declares these taxes preempted and invalid.⁸⁸ It will take congressional action to clarify the prohibition upon gross receipts taxes before states may raise additional revenue utilizing a

gross receipts falters in the attempt to characterize a sales or use tax that is not normally computed upon gross receipts.

82. Both the United States Supreme Court and the Hawaii Supreme Court agreed that Congress enacted the ADAA in response to *Evansville Airport*. See 104 S. Ct. at 292-93; 65 Hawaii at 9, 647 P.2d at 274. In *Evansville Airport*, the Supreme Court held state airport head taxes permissible under the ADAA. See *supra* text accompanying notes 39-43. Yet, neither court could explain Congress' reason for differentiating between gross receipts taxes and the permissible general revenue-raising taxes of § 1513(b). See 104 S. Ct. at 294; 65 Hawaii at 9, 647 P.2d at 273-74.

Additional insight as to why Congress chose the § 1513 language "direct or indirect . . . and upon gross income" is taken from *Evansville Airport*. The Supreme Court stated the following as to the manner of levying the head tax:

[W]e do not think it particularly important whether the [h]ead charge is imposed on the passenger himself, to be collected by the airline, or on the airline to be passed on to the passenger if it chooses. In either case, it is the act of enplanement and the consequent use of runways and other airport facilities that give rise to the obligation.

405 U.S. 707, 714 (emphasis added).

Evansville Airport ignited congressional action. It follows that Congress utilized the above language from *Evansville Airport* to ensure that states would not apply any type of head tax upon airlines or their passengers. See *supra* note 42.

83. See 104 S. Ct. at 295 n.10. The Supreme Court noted that Congress may amend § 1513 if it believes its preemptive effect on state taxes is too broad. *Id.*

84. The Supreme Court did not analyze the Hawaii Supreme Court's commerce clause arguments, but dealt only with the federal preemption issue. See 104 S. Ct. at 294. In light of *Complete Auto* and *Commonwealth Edison*, interstate commerce must pay its fair share of the state costs in the forum of its business activities. See *supra* notes 21-28 and accompanying text.

85. See *supra* notes 73-84 and accompanying text.

86. See *supra* notes 21-28 and accompanying text.

87. See *supra* notes 33-46 and accompanying text.

88. See *supra* notes 71-84 and accompanying text.

gross receipts tax upon airlines.⁸⁹

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89. *See supra* notes 76-84 and accompanying text.