



THE ATTORNEY GENERAL OF TEXAS

AUSTIN 11, TEXAS

GERALD C. MANN
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ATTORNEY GENERAL

Honorable George H. Sheppard
Comptroller of Public Accounts
Austin, Texas

Overruled in part
by 0-4392

Dear Sir:

Opinion No. 0-2317

Re: Is a Post Exchange, operated and maintained for the convenience of officers and enlisted men of the Army engaged in war games in East Texas and Louisiana, such an instrumentality or agency of the Federal government as to confer immunity from the cigarette stamp tax (Article 7047c-1, Vernon's Annotated Civil Statutes) upon either the sale in Texas of unstamped cigarettes to the Exchange by licensed distributors in the State, or the importation of unstamped cigarettes from other states by said Post Exchange and the sale of such cigarettes to Army personnel?

We have for attention and answer your letter of May 2, 1940, wherein you submit for the opinion of this Department the two following questions and factual statement, which we quote:

"We have been asked by several qualified cigarette distributors whether or not they would be liable for the tax on cigarettes if sold unstamped and delivered in their own trucks to a post exchange, or one of its branches, which is being operated in connection with the regular United States Army maneuvers now taking place in the vicinity of San Augustine, Texas. The cigarette tax above referred to is levied under Chapter 241, Regular Session of the Forty-fourth Legislature and amended by Senate Bill 247, Regular Session of the Forty-fifth Legislature.

"The facts pertaining to the prospective purchasers of unstamped cigarettes from the qualified cigarette distributors are as follows:

"1. All troops taking part in the maneuvers are members of the regular U. S. Army and not National Guard or State Militia troops.

"2. The Post Exchange and its branches, which operate exclusively for the benefit of the Regular U. S. Army troops, are not located on property over which jurisdiction has been ceded to the United States government by the State of Texas.

"3. The buildings used by the Post Exchange for warehouses, storeroom and office are rented from local interest and not owned or constructed by the United States government. The rent for all such buildings is paid out of Post Exchange funds.

"4. The capital for stocking and paying the expenses of operation of the Post Exchange and its branches is raised by the sale of shares to various companies for which it is operated. The companies pay for these shares out of surplus funds accumulated from unused appropriations by Congress for company mess purposes.

"5. The Post Exchange and its branches are operated by Army personnel and supervised by officers of the Regular Army.

"6. All books and records, pertaining to the receipts and disbursements and general operations of the Post Exchange, are audited by Army auditors.

"7. All bills for merchandise, purchased by either the Post Exchange or its branches, must be submitted to the officer in charge of the Post Exchange for payment.

"8. Any profit made from the operation of the Post Exchange is divided among the companies according to the number of shares held by each company.

This profit is deposited to the Company fund and may be expended for entertainment or other things beneficial which may be thought advisable by the Company Commander.

"9. The Post Exchange does not sell cigarettes to the general public.

"Will you please advise me of your opinion in regard to the following questions:

"(a) Would a Texas cigarette 'distributor' be liable for the tax on unstamped cigarettes sold and delivered by him to a Regular Army Post Exchange or its branches, when operated in the manner and under the conditions as above described?

"(b) Is a Post Exchange, when operated in the manner above described, a cigarette distributor, as defined by Subsection 'm' of Section 1 of Article 7047c-1, Vernon's Annotated Civil Statutes, and liable for the tax on the 'first sale' in this State of cigarettes imported from other States, as levied by Section 2 of the above mentioned Article?"

Under the authorities, as we read them, the right of a state to levy and collect various excise taxes upon the sale or use of commodities by and through Post Exchanges operated in connection with the Army of the United States, turns upon either of two grounds or theories: (1) the absence of constitutional and legislative jurisdiction over the territory within which the sale or use of the commodity sought to be taxed is consummated or occurs, and (2) the immunity, under the Constitution of the United States, of the Federal government, or any of its departments, agents, or instrumentalities, created to discharge the constitutional functions of government, from taxation at the hands of the State under its revenue powers.

The first theory of tax immunity is removed from this case, because it is made to appear from your letter that the Post Exchanges involved are not located within the confines of a military reservation or other territory over which exclusive constitutional and legislative jurisdiction has been ceded by the Chief Executive of Texas to the United States, so as to remove sales consummated within such territory from the State's taxing power, under the authority of *Standard Oil Co. of California vs. California*, 291 U. S. 242; 54 Sup. Ct. 381; 78 Ed. 775.

The single issue for our determination in the instant case, and the one upon which turns the answer to both questions submitted by you, is whether or not Post Exchanges, organized, maintained and operated, under the facts and circumstances outlined, at various points in Texas subject to the political and legislative jurisdiction of the State, are departments, agencies or instrumentalities of the Federal government, so as to allow the purchase by them tax free, of cigarettes from licensed dealers in Texas, or the importation of such unstamped cigarettes from outside the State, and the sale or use of such cigarettes without the affixing of the State revenue stamps.

For the historical background and development of a Post Exchange as constituted under modern conditions, the language of the court in the case of Keane vs. United States, 272 Fed. 577, is enlightening:

"We have no definite information at hand as to how or when the first post exchange known in modern parlance was established; but it can safely be said that such a post exchange as we are now discussing is a descendant of the old sutler's camp. The dictionary tells us that a sutler was or is a small trader, who follows an army, and who is licensed to sell goods, especially edibles, to the soldiers. In other words, the post exchange is nothing more nor less than a stationary soldiers' co-operative sutler's camp or store. When troops are in active warfare and constantly on the march, manifestly a post exchange could not be maintained, and under such circumstances the sutler plies his trade, being authorized to do so by the commanding officer; but where soldiers are stationed for considerable periods of time at a post, then it becomes feasible for them to do away with the inconvenience of trading with a poorly equipped sutler, and with the necessity of paying him profits on his sales, and, instead, to establish for their own convenience and pleasure the soldiers' modern private store or exchange."

That Post Exchanges are a convenient and useful part of Army life, in ministering to such daily requirements of Army personnel as the Government has not deemed necessary to provide, cannot be gainsaid, and this fact finds recognition in the special Post Exchange regulations issued by the War Department, and by appropriations by Congress for the construction and equipment of suitable buildings for the purpose. But the authorities, although taking cognizance of these facts, have, with the exception of one hereinafter discussed, uniformly held that Post Exchanges were not thereby made agencies or instrumentalities of the Federal government.

Although not involving a tax question, but rather a question of whether or not funds realized from a Post Exchange belonged to the United States so that an indictment would lie for defrauding in connection therewith, we consider the case of Keane vs. United States, supra, to be highly persuasive, in holding that the prosecution would fail because a Post Exchange was not a department of the government and the United States was not responsible for its contracts and obligations and had no interest in its funds, although its business was

conducted by an officer detailed for the purpose. We quote copiously from this opinion because the modus operandi of the Post Exchange involved therein closely parallels the ones in the instant case:

"Nowhere in this pamphlet of special regulations is it required or commanded that post exchanges shall be established. Indeed, it is expressly stated in these Special Regulations that these exchanges are voluntary organizations among the soldiers themselves. As best we can gather from these regulations, a post exchange is a voluntary, unincorporated co-operative store at, near, or on a military post; the Secretary of War giving the soldiers at such post a license or privilege to form such a co-operative store. The Secretary of War, in effect, says, in these regulations, to the soldiers, that while they are not required to establish post exchanges, yet, if they do establish them, that they should have for their purpose the supplying to the troops at reasonable prices of the articles of ordinary use, wear, and consumption, not supplied by the government, and to afford them means of rational recreation and amusement, and through exchange profits to provide, when necessary, the means for improving the messes. The regulations suggest that an assessment should be made upon the several organizations contributing to the exchange for the purpose of procuring necessary articles, and that all articles thus procured must be paid for by the first profits of the institution; it being distinctly understood that the officers incurring debts on behalf of the exchange, and not the government, are responsible for the payment thereof.

"Members of the exchange must be organizations, companies, detachments, and individual enlisted men cannot become members, unless three or more of them are associated in a mess. The special management of the exchange is conducted by an officer designated and detailed by the commanding officer, and this officer is responsible for the management of the exchange, and is regarded as the custodian of the funds belonging to it. When the exchange is free from debt, at the end of each quarter, a sum sufficient to cover anticipated debts is set aside as a reserve fund, and a percentage of the remainder is distributed among the members, and other parts thereof are set aside for specific purposes, and the

remainder may be divided among the organizations contributing to the exchange on an equitable basis; and a division of the cash resources of the exchange is made whenever the troops belonging to the exchange, or any part of them, change their station, and when all the units composing membership in an exchange have gone away or removed from the post, the exchange stock must be reduced to the lowest extent possible and converted into cash; and prior to the departure of the troops the property of the exchange is sold and the proceeds, together with the cash, are distributed among the organizations according to the number of shares held by each. Post exchange funds, when deposited in a bank, must be placed under their official designations, and not to the credit of the officer who is their custodian, and such funds of a post exchange are especially declared to be not public moneys within the meaning of sections 5488, 5499, and 5492 of the Revised Statutes (Comp. St. ¶ 10255, 10302, 10259), and misapplication of such funds by an officer having their custody is punishable, not under the general law, but under the Articles of War. Nowhere in these regulations do we find a rule or even a suggestion that under any possible contingency does or would the government ever receive or come into possession of any of the funds or assets of the exchange."

Bearing more specifically upon the taxability by a state of a commodity sold to a post exchange of a United States Army, we cite the case of *People vs. Standard Oil Co. of California*, 22 Pac. (2d) 2, and quote therefrom the following conclusive language:

"It is next urged that a sale to the army post exchange is a sale to a department of the government of the United States for official use of said government. Manifestly these sales are neither to a 'department' of the government nor for official use. The gasoline was sold to the exchange for resale to certain classes of persons for their private consumption. We have no hesitation in concluding that the legislative intent was to include the sales in question in computing the tax. But these observations do not determine the cause.

"We are pointed to the decision of the Supreme Court of the United States in the case of *Panhandle Oil Co. v. Mississippi*, 277 U. S. 218, 48 S. Ct. 451,

452, 72 L. Ed. 857, 56 A. L. R. 583, where the court used language showing that an important question is here involved. There, as here, the state of Mississippi imposed an excise tax upon distributors of gasoline measured by sales within that state. The state sued the oil company to recover balances represented by sales to the United States for use of its Coast Guard service operating in the Gulf of Mexico and for its veterans' hospital at Gulfport. The sales were made directly to the government, and the court held that said statute was inoperative as to them, using language in part as follows: 'The states may not burden or interfere with the exertion of national power or make it a source of revenue or take the funds raised or tax the means used for the performance of federal functions. * * * The amount of money claimed by the State rises and falls precisely as does the quantity of gasoline so secured by the government. It depends immediately upon the number of gallons. The necessary operation of these enactments when so construed is directly to retard, impede, and burden the exertion by the United States of its constitutional powers to operate the fleet and hospital. * * *' This was a five-four decision of the court; Justices Holmes, Brandeis, McReynolds, and Stone dissented, Justices Holmes and McReynolds writing opinions.

"But it seems to us that a well-founded distinction may be found between the sales there involved and sales to an army post exchange. The commanding officer of an army post is not required to organize the post exchange unless there is need for it or unless the units present desire to participate therein or unless the personnel is sufficient to profitably maintain and support such an institution. In other words, a post exchange is at most but a government agency, designed to operate for the welfare of the troops such activities as a general store, meat or vegetable market or gasoline station, or a restaurant, gymnasium, recreation room, library, or theater. Thus it is not properly described by the word 'department' of the government in its activities. It is largely a co-operative institution, intended to supply the needs and promote the moral and civic betterment of the troops at the post.

"It is supervised by an exchange council, com-

posed of the commanding officers of the respective units represented in the organization. The funds of the exchange are not public moneys within the meaning of the Revised Statutes of the United States (Rev. Stats. ¶ 5488, 5490, 5492 (18 USCA ¶ 173, 175, 177)). The exchange is not instituted by the aid of funds from the United States nor are its avails paid into the treasury. It is a voluntary, unincorporated, co-operative association in which all units share the benefits and all assume a position analogous to that of partners. In the event of the inability of the post exchange to pay its debts, the organizations which participate in it are supposed themselves to pay off all such obligations in proportion to their respective interests in the exchange. Neither the government nor the officers of the post wherein the exchange is located are liable for its debts. The property of the post exchange is not to be treated as property belonging to the United States. The exchange itself is liable for certain federal taxes, such as the stamp tax imposed by the Internal Revenue Act, the freight tax imposed by the War Revenue Act of 1917 (40 Stat. 300), a floor tax on tobacco under the Revenue Act of 1918, ¶ 702 (40 Stat. 1118); sales of ice cream and soft drinks by a post exchange are subject to tax under the same act. From these and other observations that might be made, touching the nature of the organization of an army post exchange, we are of the opinion that it is an organization largely engaged in business of a private nature and that sales to it should not be beyond the reach of the taxing power of the state wherein it is located and that it is not one of those agencies through which the federal government directly exercises its constitutional or sovereign power."

Although the judgment of the Supreme Court of California in the above case was reversed by the Supreme Court of the United States in the case of Standard Oil Co. of California vs. California, cited at the outset of this opinion, such reversal was not upon the point of law now under discussion, but rather upon a question of territorial jurisdiction. Consequently, the discussion of the court, above quoted, is not in anywise discounted thereby.

The case of Pan-American Petroleum Corp. vs. State of Alabama, 67 Fed. (2d) 590, likewise upholds the right of a state to tax the sale of a commodity, even though the tax is passed on to the Post Exchange of the regular Army, as the

purchaser thereof. In this connection, the court said:

"....Furthermore, a post exchange is, of course, not the government; nor is it a department or instrumentality thereof. On the contrary, a post exchange is a voluntary, unincorporated, co-operative association of army organizations in which all share as partners in the profits and losses. The government has no share in the profits, and is not bound by the losses. We are therefore of the opinion that sales made by appellant to the post exchanges at Camp McClellan and Maxwell Field are not exempt from the state excise taxes. *People v. Standard Oil Co.* (Cal. Sup.) 22 P. (2d) 2."

The case of *United States vs. Query et al.*, 21 Fed. Sup. 784, stands alone in opposition to the principle of law announced in the above discussed cases. On an injunction brought by the United States to enjoin the South Carolina Tax Commission from enforcing certain provisions of its revenue statutes, the court held that a Civilian Conservation Corps Post Exchange, established pursuant to statutory authority and operated for the welfare of the camp's enrollees, is a Federal instrumentality not subject to the license tax imposed by State statute on the privilege of selling certain articles, and not subject to the supervisory authority of the State Tax Commission. Title 16, USCA, Section 584p, appropriates money out of the Federal Treasury "to pay any expense in connection with the conduct, operation or management of any camp exchange" established and operated in accordance with regulations prescribed by the Director. The court, in its opinion, seizes upon this recognition by Congress and the utilization of Federal funds to pay current operating expenses of the camp exchange, as stamping such exchanges with the character of Federal agencies or instrumentalities, protected, under general principles of constitutional law, from State taxation. Under the facts before us, it does not appear that funds from the Federal Treasury are used to defray operating expenses, nor have we found an act of Congress authorizing any appropriation except for the construction of the buildings which house such exchanges. This point of difference may serve to reconcile the apparent conflict between these authorities, but if not, we are not inclined to follow this decision of a Federal district court against the three well considered decisions of appellate courts, both State and Federal, which, to our mind, have announced the better rule of law.

But even conceding that we have incorrectly interpreted

the decisions of our courts to hold that a Post Exchange, organized and maintained in connection with the regular Army, is not an agency or instrumentality of the Federal government in the constitutional sense, it would nevertheless be our opinion that the excise stamp tax levied upon the sale of cigarettes to or by a Post Exchange for the personal use of officers and men of the regular Army, would not be a burden upon a Federal function, obnoxious to the Federal Constitution.

Prior to our examination of the recent trend of decisions of the Supreme Court of the United States, and inferior Federal and State tribunals, we would have said that this question was conclusively foreclosed by the decision of the Supreme Court of the United States in the case of *Panhandle Oil Co. vs. State of Mississippi*, 277 U. S. 218; 48 Sup. Ct. 451; 72 L. Ed. 857. This case involved the constitutionality of an attempted levy and collection by a state of an excise tax from a local distributor of motor fuel, upon motor fuels sold by such distributor directly to the Navy for use in certain boats belonging to the United States Navy. The contention was made in this case that the tax was levied as an occupation tax upon the local dealer or distributor, measured by the gallonage sold, and the mere fact that such dealer or distributor, as a business practice, passed such tax on to the consumer, who in this instance chanced to be the United States government, would not render such tax unconstitutional as a direct burden upon a Federal instrumentality. Although this contention was rejected by the Supreme Court, a vigorous dissent was entered by Mr. Justice Holmes, who pointed out that, carried to its ultimate conclusion, such principle of law would result in employees of the various departments and bureaus of the Federal government being allowed to purchase clothes and various other articles and commodities upon which the various states had levied sales taxes, merely by virtue of the fact that such tax was passed on to the consumer as part of the cost of the product.

This dissenting opinion of Mr. Justice Holmes was vindicated when the Supreme Court, in the case of *James vs. Dravo Contracting Co.*, 302 U. S. 134; 82 L. Ed. 155, limited its own decision in the *Panhandle* case discussed above, by holding that an occupation tax measured by gross income is not invalid when imposed by a State upon a contractor with the United States as laying a direct burden on the Federal government, even though the imposition of the tax may increase the cost to the government of the work contracted to be done. Although not expressly overruled, the Supreme Court in this case expressly mentioned the decision in the case of *Panhandle Oil Co. vs. Mississippi*, supra, and stated that it and similar

cases had been distinguished and limited to their particular facts.

Federal Land Bank of St. Paul vs. D. E. Ochford, 287 N.W. 522, cites and follows the authority of James vs. Dravo Contracting Co., supra, and numerous other decisions of the Supreme Court of the United States, modifying the principle of Federal immunity established in the Panhandle case, and holds that a Federal Land Bank, although admittedly an instrument or agency of the Federal government, was yet subject to an excise tax levied by a state upon the sale to it of motor fuel.

Like the motor fuel tax in the case last cited and the occupation tax measured by gross income upon the contractor in the leading case of James vs. Dravo Contracting Co., supra, the cigarette tax levy involved in the instant question is an excise tax levied upon the sale or use of cigarettes by licensed distributors in Texas. This tax is not levied upon Post Exchanges of the Army, as such, and the fact that such tax is passed on to such Post Exchanges by licensed distributors in Texas as part of the purchase price, constitutes too remote a burden to render such a tax unconstitutional as a tax upon an agency or an instrumentality of the Federal government, under the recent trend of authorities modifying if not indirectly overruling the much-discussed and much-criticised principle of Federal tax immunity announced in the case of Panhandle Oil Co. vs. State of Mississippi, supra.

Even agencies and instrumentalities of the Federal government may engage in practices and functions outside the protection of the Constitution and thereby become subject to the laws of a state regulating or taxing such extragovernmental function. The sale of cigarettes for the personal use and convenience of officers and men of the Army falls within this classification and should be subject to the excise tax levied thereon by the State of Texas. The point we stress is that for a Federal agency or instrumentality to be immune from State taxation, its activities and functions must be in furtherance of the constitutional powers of the Federal government. We can find no rational relationship between smoking cigarettes by officers and men, insofar as the constitutional functions and purposes of the government is concerned, and the proper functioning of the Army. To hold otherwise would be to extend the tax immunity to smokers of cigarettes in the postal service and in the various other departments of the Federal government. Authorities supporting our position here, that Federal agencies or instrumentalities which also engage in extragovernmental functions may not invoke Federal immunity from taxation unless the Federal functions are un-

duly burdened, are Educational Films Corporation of America vs. Ward, 51 Sup. Ct. 170; 282 U. S. 379; Santa Clara Co. vs. Southern Pacific Ry., 18 Fed. 385, aff. 118 U. S. 394; Alward vs. Johnson, 282 U. S. 509; 51 Sup. Ct. 273; 75 L. Ed. 496; Willcuts vs. Bunn, 282 U. S. 216; 51 Sup. Ct. 125; 75 L. Ed. 304; Tirrell vs. Johnston, 171 Atl. 641.

We answer both questions submitted in the affirmative. Licensed cigarette distributors in Texas may not lawfully sell unstamped cigarettes to regular Army Post Exchanges or branches, operated in the mode and manner outlined, nor may such exchanges resort to the expediency of importing cigarettes to escape the tax collectible on intra-state sales, because they in turn would become "distributors" and liable for the tax accruing on a "first sale" as defined by the Cigarette Tax Law of Texas.

Yours very truly

ATTORNEY GENERAL OF TEXAS

By s/Pat M. Neff, Jr.
Pat M. Neff, Jr.
Assistant

PMN/oe/wc

APPROVED MAY 7, 1940
s/Gerald C. Mann
ATTORNEY GENERAL OF TEXAS

Approved Opinion Committee By s/BWB Chairman