HB

222

Representative Jay Ramras
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Alaska State Legislature

While in Session
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House District 10

House of Representatives

Memo

To: Representative Gabrielle LeDoux
Co-Chair House Community & Regional Affairs
Representative Anna Fairclough
Co-Chair House Community & Regional Affairs

From: Representative Jay Ramras

Date: March 31, 2007

Re: Hearing Request for HB222 – Passenger Vessel Tax Credit

Please accept this memo as a request for the House Community and Regional Affairs Committee to hear HB222.

Please find attached to this memo the following documents:

- Sponsor Statement for HB222
- CSHB222 (25-LS0782\E)
- Explanation of changes version \C to version \E
- Original version of the Bill (25-LS0782\C)
- Legal opinions

Representative_Jay_Ramras@legis.state.ak.us

Alaska State Legislature

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Representative Jay Ramras
House District 10

Chair, House Judiciary Committee • Member, House Labor & Commerce Committee • Member, House Oil & Gas Committee • Member, House Military & Veteran Affairs Committee

Sponsor Statement HB222

"An Act providing a credit for a municipal tax imposed on certain passengers traveling on commercial passenger vessels that provide overnight accommodations; and providing for an effective date."

The revenue anticipated from the passenger excise tax in 2007 is $41 million. The *Primary* Election Voter Pamphlet of 2006 stated that $14 million would go to municipalities that have ports of call and another $10 million will go to a "Regional Cruise Ship Impact Fund" for other municipalities at which cruise ships do not stop.

These taxes cannot possibly be described as covering the costs of servicing the vessels, as required under Federal law, 33 U.S.C. § 5(b)(2).

House Bill 222 addresses how the $46.00 passenger excise tax should be distributed as a tax credit to municipalities with ports of call. HB 222 would ensure that a municipality that is one of the first five ports of call for the vessel would be entitled to a credit against the tax equal to the lesser of $10 or the actual amount of a passenger tax paid to each municipality.

House Bill 222 allows a municipality that is a port of call to have a guaranteed income source, which bond buyers, in turn, would see as stable and trustful. Through the provisions of HB222 municipalities could bond permanent port facilities, which in turn would ensure a healthy cruise industry and income stream for the State of Alaska.

E-Mail Representative_Jay_Ramras@legis.state.ak.us

25-LS0782\E
Bullock
3/28/07

CS FOR HOUSE BILL NO. 222( )

IN THE LEGISLATURE OF THE STATE OF ALASKA

TWENTY-FIFTH LEGISLATURE - FIRST SESSION

BY

Offered:
Referred:

Sponsor(s): REPRESENTATIVE RAMRAS

A BILL

FOR AN ACT ENTITLED

"An Act providing a credit for the payment of certain municipal passenger taxes or fees against the excise tax on travel aboard commercial passenger vessels; and providing for an effective date."

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

*** Section 1.** AS 43.52 is amended by adding a new section to read:

Sec. 43.52.225. Tax credit for local levy. A passenger liable for the tax under AS 43.52.220 is entitled to credit against the tax equal to the lesser of $10 or the actual amount of a passenger tax paid to each municipality that is one of the first five municipalities that is a port of call for the vessel on which the passenger is traveling and that imposes a passenger tax. The total amount of the credits may not exceed the amount of the tax levy in AS 43.52.210. In this section, "passenger tax" means a municipal tax or fee that is imposed on the passenger, the commercial passenger vessel, or the operator of the vessel, and is calculated by reference to the number of passengers or berths on the vessel.

* **Sec. 2.** The uncodified law of the State of Alaska is amended by adding a new section to read:

RETROACTIVITY. Section 1 of this Act is retroactive to December 17, 2006.

* **Sec. 3.** This Act takes effect immediately under AS 01.10.070(c).

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House District 10

House of Representatives

Memo

To: Representative Jay Ramras

From: Jane Pierson

Date: April 1, 2007

Re: HB 222 Explanation of Changes versi \C to version \E

P. 1, L. 7 Caps the amount that can be collected to $10.00

P. 1, L.12 Adds the word fee after tax in the definition of "passenger tax".

Representative_Jay_Ramras@legis.state.ak.us

Legal Opinions Relating to the Cruiseship Head Tax Initiative

A compilation of legal opinions relating to components of the Head Taxes authorized in the cruiseship ballot initiative approved by Alaska voters in August, 2006.

MEMORANDUM

TO: North West Cruiseship Association

DATE: January 18, 2007

RE: ***Analysis of Constitutional Issues Arising from Passenger Head Tax***

I. OVERVIEW

The Initiative's $46.00 passenger head tax violates federal law in at least three ways:

First, it violates 33 U.S.C. § 5, which prohibits taxes or fees on vessels operating in navigable waters, or their passengers, except for narrowly tailored, fairly allocated user fees that enhance the "safety and efficiency" of interstate commerce. The passenger tax imposed by the Initiative does not come close to satisfying the test for a proper fee under 33 U.S.C. § 5.

Second, it violates the Tonnage Clause of the United States Constitution, which the Supreme Court has read to prohibit any taxes or fees on vessels in interstate commerce except those directly related to services provided to those vessels. Here, the tax operates not as a user fee but as a revenue generating device, which the Tonnage Clause squarely prohibits.

Third, it violates the Commerce Clause of the United States Constitution. The sponsors of the Initiative designed the passenger tax to discriminate against interstate commerce, which the Commerce Clause prohibits. Further, the tax fails the "internal consistency" test, which asks whether interstate commerce would be unduly burdened if every state imposed a similar tax, as well as the requirement that the tax be fairly related to the services provided by the state.

II. 33 U.S.C. § 5

In 2002, Congress amended the Rivers and Harbors Act of 1884 to prohibit state and local governments from levying or collecting *any* "taxes, tolls, operating charges, fees, or any other impositions whatever ...from any vessel or other water craft [operating in navigable waters], or from its passengers or crew." 33 U.S.C. §5(b). This law preempts any state taxes enacted in violation of its terms. *See also Aloha Airlines, Inc. v. Dir. of Taxation of Hawaii*, 464 U.S. 7, 12 n.5 (1983) (addressing similar federal statute governing airline taxes and fees).

Congress excepted narrowly-tailored user fees from this broad prohibition. Thus, a state may levy "*reasonable* fees *charged on a fair and equitable basis* that (A) are used *solely* to pay the cost of a service to the vessel or water craft; (B) enhance the safety and efficiency of interstate and foreign commerce; *and* (C) do not impose more than a small burden on interstate or foreign commerce." 33 U.S.C. § 5(b)(2) (emphasis added). (Congress also excepted some types of "property taxes" from the prohibition. *See* 33 U.S.C. §5(B)(3).) Congress meant this exception to be narrow. As Representative Young stated, "non-Federal interests[] may impose taxes or fees only . . . *under extremely limited circumstances* in which reasonable fees can be charged on a fair and equitable basis for the cost of service actually rendered to the vessel." Cong. Record (Nov. 22, 2002), at E2143-44 (emphasis added). Any such "fees must *also* enhance the safety and efficiency of interstate and foreign commerce *and* represent at most a 'small burden' on interstate and foreign commerce." *Id.* at E2144 (emphasis added). "Generally, taxes will *not* be allowed under this section." *Id.* (emphasis added).

Notably, as Representative Young pointed out, Subsection 5(b)(2) sets forth *conjunctive* requirements for a permissible fee, not a disjunctive test, so a fee must satisfy all three statutory criteria. Thus, a charge imposed to cover something other than the cost of servicing a vessel would be improper *even if* it enhanced the safety and efficiency of commerce. Similarly, a charge that is not imposed on "a fair and equitable basis" – for example, a fee imposed on some vessels that receive services but not others – would violate the statute *even if* it defrayed the cost of services and enhanced the safety and efficiency of commerce. At bottom, the statute makes clear that a state's fees must be tethered to the impact of having *that* vessel in its waters, and it must apply fairly across the board.

Bearing these conjunctive requirements in mind, the passenger tax violates Section 5(b) for at least four reasons:

First, it is a "tax," not a "fee," and the federal statute allows only "fees." Congress distinguished between taxes and fees, as illustrated by the exceptions to the prohibition, which are separately addressed to "fees" (in Sections 5(b)(1) and (2)) and "taxes" (in Section 5(b)(3)), and by the comments of Representative Young in the legislative history quoted above. Aside from the fact that the Initiative calls it a "tax," the passenger levy *functions* as a "tax," in part because the Initiative allocates some revenues to municipalities and then leaves the balance as unearmarked revenue. *See Qwest Corp. v. City of Surprise*, 434 F.3d 1176, 1183 (9th Cir. 2006); *Hexom v. Oregon Dept. of Transportation*, 177 F.2d 1134, 1135-36 (9th Cir. 1999).

Second, even if a court evaluates the tax as a "fee" under Section 5(b)(2), it is not charged "on a fair and equitable basis." Passengers taking similar voyages on vessels with 249 or fewer sleeping berths can avoid the tax entirely, even if the state provides similar services to those vessels. Further, the tax bears no relationship to the time spent by passengers in Alaska waters or their impact on Alaska ports. Under the Initiative, passengers on large vessels would pay for services that smaller vessels use as well, such as the construction, maintenance and operation of docks. There is nothing "fair and equitable" about one segment of an industry subsidizing services used by another. *See Northwest Airlines, Inc. v. County of Kent, Mich.*, 955 F.2d 1054, 1062-63 (6th Cir. 1992) (airport could not impose cost of maintaining fire rescue solely on airlines where concessionaires also benefited from those services).

Third, the revenue generated from the passenger tax is not used "*solely* to pay the cost of a service to the vessel." To the contrary, the Legislature "may" use money generated by the taxes for general improvement of port and harbor facilities, services to provide for vessel visits, enhancing the safety and efficiency of interstate commerce, and "*such other lawful purposes as determined by the legislature.*" AS 43.52.040(a) (emphasis added). Even if the Legislature were to accommodate the Initiative's suggested uses of the funds collected, passengers on vessels calling in one port would wind up paying to improve facilities in other ports, where the vessel may not call and the passenger may never visit. This violates the law. *See City and County of Denver v. Continental Air Lines, Inc.*, 712 F. Supp. 834, 840 (D. Colo. 1989) (airport could not charge passengers a fee to build new facility they might never use).

Fourth, the Initiative virtually ensures that this tax will generate millions of dollars to be spent for something other than vessel services. The revenue anticipated from the passenger excise tax in 2007 is $41 million, of which $14 million will be shared with municipalities where the cruise ships call. *See* Primary Election Voter Pamphlet 2006, at 13. Another $10 million will go into a "Regional Cruise Ship Impact Fund" for other municipalities at which cruise ships *do not stop*. *Id.* These funds cannot *possibly* be described as covering the cost of servicing these vessels; indeed, they will be given to the very jurisdictions whose potential actions so concerned Representative Young. *See* Cong. Record (Nov. 22, 2002), at E2143 (referring to "local jurisdictions seeking to impose taxes and fees on vessels merely transiting or making innocent passage through navigable waters . . . adjacent to the taxing community . . . even where the vessel is not calling on, or landing, in the local community"). Further, the Initiative allows tax revenues to be used to "enhance the safety and efficiency of interstate and foreign commerce" or for "other lawful purposes," provisions so amorphous that they transform the Alaskan passenger tax into a general revenue measure in clear violation of federal law.

III. THE TONNAGE CLAUSE

Article I, Section 10 of the United States Constitution provides that "[n]o State shall, without the Consent of Congress, lay any Duty of Tonnage." U.S. CONST. art. I, § 10, cl. 3. Courts have construed the Tonnage Clause expansively to forbid a variety of taxes based on measures other than tonnage. Thus, in *Clyde Mallory Lines v. Alabama*, 296 U.S. 261, 265-66 (1935), the Court construed the Tonnage Clause to apply to "all taxes and duties regardless of their name or form . . . which operate to impose a charge for the privilege of entering, trading in, or lying in a port," without regard to any reference to "[t]onnage."

The Tonnage Clause does *not* forbid the collection of "fees or charges by authority of a state for *services* facilitating commerce, such as pilotage, towage, charges for loading and unloading cargoes, wharfage, storage, and the like." *Clyde Mallory*, 296 U.S. at 265; *see also id.* at 265-66 (Tonnage Clause does not prohibit charges "for services rendered to and enjoyed by the vessel"). Thus, a charge will satisfy the Tonnage Clause if it defrays the cost of services provided directly to the vessel at issue; it will fail, however, if it merely operates as "a revenue device." *New Orleans Steamship Ass'n v. Plaquemines Port, Harbor & Terminal Dist.*, 874 F.2d 1018, 1023 (5th Cir. 1989).

The passenger tax violates the Tonnage Clause for essentially the same reasons that it violates 33 U.S.C. § 5(b). The flat head tax applies to all covered vessels that enter Alaska

marine waters, without regard to the number of ports at which they call or the facilities they use; its proceeds are not dedicated entirely to legitimate port-related services (and, indeed, the tax will generate more money than the state could expect to use for port-related services); and even the possible port-related uses of funds collected from a particular vessel will not necessarily go to facilities (or even ports) used by that vessel or its passengers. Accordingly, the tax has been assessed for the mere "privilege of access by vessels or goods to the ports or to the territorial limits of a state," in violation of the Tonnage Clause. *Clyde Mallory*, 296 U.S. at 265.

IV. THE COMMERCE CLAUSE

Article I, Section 8 of the United States Constitution provides that "Congress shall have Power . . . [t]o regulate Commerce with foreign Nations, and among the several States." U.S. CONST. art. I, § 8, cl. 3. Although this provision makes only an affirmative grant of power to Congress, it also prevents states from unduly interfering with interstate commerce – a doctrine known as the "dormant" or "negative" Commerce Clause. Under the dormant Commerce Clause, a State's "power to lay and collect taxes, comprehensive and necessary as that power is, cannot be exerted in a way which involves a discrimination against [interstate] commerce." *Pennsylvania v. West Virginia*, 262 U.S. 553, 596 (1923). The point is to combat local favoritism and economic isolationism by individual states, and to foster a single, unified national identity and market. *See, e.g., Am. Trucking Ass'ns v. Mich. Pub. Serv. Comm'n*, 125 S. Ct. 2419, 2423 (2005).

The U.S. Supreme Court has developed and applied several tests to determine whether a state tax unconstitutionally discriminates against, or otherwise unduly burdens and interferes with, interstate commerce. The passenger tax fails at least three of these tests:

First, the dormant Commerce Clause bars any form of discrimination against interstate commerce, unless the State offers a compelling justification for that discrimination. *S. Cent. Bell Tel. Co. v. Alabama*, 526 U.S. 160, 169 (1999). This prohibition against discrimination applies not only to facially discriminatory state taxes, but also to state taxes that have either the *purpose* or the *effect* of burdening out-of-state interests to the advantage of in-state interests. *See Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263, 270 (1984); *S.C. State Highway Dep't v. Barnwell Bros.*, 303 U.S. 177, 184 n.2 (1938).

The passenger tax is unlawful because it has a clear *purpose* of burdening persons from outside Alaska. In determining whether a state has enacted a law with a discriminatory purpose, courts often look to its legislative history or the statements of its sponsors. *See, e.g., S.D. Farm Bureau, Inc. v. Hazeltine*, 340 F.3d 583, 593 (8th Cir. 2003) (looking to "direct evidence that the drafters of Amendment E or the South Dakota populace that voted for Amendment E intended to discriminate against out-of-state businesses"); *SDDS, Inc. v. South Dakota*, 47 F.3d 263, 268 (8th Cir. 1995) (referring to "legislative history ... brimming with protectionist rhetoric"). Here, public statements show that the sponsors supported the Initiative *specifically* because it would disproportionately burden out-of-state tourists and out-of-state businesses – and they counted on fellow Alaskans to support the initiative for that very reason. *See, e.g.*, Paula Dobbyn, *Court to Rule on Tourist Tax Petition*, Anchorage Daily News, Oct. 11, 2005 at F1 ("'It's a tax on *people from outside* the state and it's specifically designed to build infrastructure so that when they come here, Alaskans don't have to subsidize them,' Geldhof said."); Joseph Ditzler, *Mat-Su CVB*

to Campaign Against Tax on Cruising, Anchorage Daily News, Dec. 17, 2005 at F1 ("Alaskans polled typically support the initiative, recognizing *it taxes Outsiders . . .*, Geldhof said."); Paula Dobbyn, *Judge OKs Cruise-Ship Initiative*, Anchorage Daily News, Feb. 9, 2006 at D1 ("'Even for a cynical political hack like me, it's a good day when the citizens get to win one against a multibillion-dollar industry *located in British Columbia and Outside*,' said Joe Geldhof."); Paula Dobbyn, *Cruise Industry Blitzing Voters*, Anchorage Daily News, May 19, 2006 at A1 ("'Alaskans are not stupid,' said Joe Geldhof, a Juneau lawyer. 'For the average person sitting in a bar, it takes five minutes to figure out *this is a tax on the guy from Ohio*.'").

Second, the U.S. Supreme Court has developed a test of "internal consistency" to detect and prevent multiple taxation of (and therefore discrimination against) interstate commerce. Courts apply the test by imagining what would happen if every state imposed precisely the same tax; the tax fails the internal consistency test if, as a result, interstate commerce would be burdened more heavily than intrastate commerce. "Internal consistency is preserved when the imposition of a tax identical to the one in question by every other State would add no burden to interstate commerce that intrastate commerce would not also bear." *Okla. Tax Comm'n v. Jefferson Lines, Inc.*, 514 U.S. 175, 185 (1995).

The passenger tax fails the internal consistency test. The Supreme Court long has expressed suspicion of state schemes that assess a flat tax simply because someone crosses the state's border in the course of commerce. "If each state imposed flat taxes for the privilege of making commercial entrances into its territory, there is no conceivable doubt that commerce among the states would be deterred." *Am. Trucking Ass'ns v. Scheiner*, 483 U.S. 266, 284 (1987). Here, the passenger tax assesses a flat tax on passengers solely for the privilege of allowing their cruises to enter Alaskan waters. Plainly, if every other state imposed an identical tax, the result would be a heavy burden on interstate commerce that intrastate commerce would not also bear – a burden that would increase depending on how many states' waters a cruise ship entered, without regard to the burdens imposed by the vessel on any given state. *See Jefferson Lines*, 514 U.S. at 185. The tax thus violates the fundamental principle of the internal consistency test, i.e., that "revenue measures [must] maintain state boundaries as a neutral factor in economic decisionmaking." *Scheiner*, 483 U.S. at 283.

Third, a state tax passes muster under the dormant Commerce Clause only if it "is fairly related to the services provided by the State." *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977). *See also Atlantic Richfield Co. v. Alaska*, 705 P.2d 418, 432 (Alaska 1985) (same). The Initiative violates this test.

"[W]hen the measure of a tax bears no relationship to the taxpayer's presence or activities in a State, a court may properly conclude under the ... *Complete Auto Transit* test that the State is imposing an undue burden on interstate commerce." *Commonwealth Edison*, 453 U.S. at 629. Here, the passenger tax does not fairly relate either to the services provided by the State to, or to the costs imposed on the State by, cruise ships. Instead, the Initiative imposes the same tax on cruise ship passengers, whether the vessel stays in Alaska 3 days or 10, whether it calls at one Alaska port or several, and whether it loads cargo and supplies on one occasion or many.

STATE OF ALASKA

Frank H. Murkowski, Governor

DEPARTMENT OF LAW

OFFICE OF THE ATTORNEY GENERAL

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May 16, 2003

The Honorable Cheryll Heinze
Alaska House of Representatives
State Capitol, Room 416
Juneau, AK 99801-1182

Dear Representative Heinze:

This is to respond to your request regarding HB 207 and the applicable federal law concerning taxes, fees, and other levies on vessels or their passengers or crew. Specifically, the Maritime Security Act of 2002, among other things, amended 33 U.S.C. sec. 5 to provide:

> (b) No taxes, tolls, operating charges, fees, or any other impositions whatever shall be levied upon or collected from any vessel or other water craft, or from its passengers or crew, by any non-Federal interest, if the vessel or water craft is operating on any navigable waters subject to the authority of the United States, or under the right to freedom of navigation on those waters, except for --
>
> (1) fees charged under section 208 of the Water Resources Development Act of 1986 (33 U.S.C. 2236); or
>
> (2) reasonable fees charged on a fair an equitable basis that --
>
> (A) are used solely to pay the cost of a service to the vessel or water craft;
>
> (B) enhance the safety and efficiency of interstate and foreign commerce; and
>
> (C) do not impose more than a small burden on interstate or foreign commerce.

John Corso, City & Borough of Juneau Attorney, recently examined the change in federal law. As you know, the CBJ has a port fee in place and is therefore very interested in this subject. I have reviewed Mr. Corso's opinion and I concur with his conclusions. I have attached a copy of his memorandum for your review.

The new statutory language basically restates the federal constitutional rule that a fee can be imposed on vessels or the passengers only to the extent the authority imposing such fee provides a service to the vessel. Article I, section 10, cl. 3 of the United States Constitution provides: "No State shall, without the Consent of Congress, lay any Duty of Tonnage...." *Clyde Mallory Lines v. State of Alabama*, 296 U.S. 261 (1935) (the prohibition against tonnage duties does not extend to charges made by state authority for services rendered to and enjoyed by the vessel). Additionally, there are several other constitutional provisions that are implicated by a fee or tax on cruiseships.

As Mr. Corso states in his memorandum, "the statute adds some new emphasis to the constitutional rule." The fees must be used "solely" to pay the cost of a service to the vessel, must "enhance the safety and efficiency of interstate and foreign commerce," and must not impose more than a "small" burden on that commerce.

I hope this information is of assistance and please let me know if you have further questions.

Sincerely,

Gregg D. Renkes
Attorney General

Enclosure

CBJ Law Department
MEMORANDUM

To: Assembly Finance Committee

From: John R. Corso, City & Borough Attorney

Subject: Port Fees; federal law

Date: April 21, 2003

I. Discussion

Last week, KTOO broadcast a story about the Murkowski administration reaction to recent changes in federal maritime law. The law in question is the Maritime Security Act of 2002, which, among other changes, amended 33 USC §5 to provide:

> (b) No taxes, tolls, operating charges, fees, or any other impositions whatever shall be levied upon or collected from any vessel or other water craft, or from its passengers or crew, by any non-Federal interest, if the vessel or water craft is operating on any navigable waters subject to the authority of the United States, or under the right to freedom of navigation on those waters, except for--
>
> (1) fees charged under section 208 of the Water Resources Development Act of 1986 (33 U.S.C. 2236), or
>
> (2) reasonable fees charged on a fair and equitable basis that--
>
> (A) are used solely to pay the cost of a service to the vessel or water craft,
>
> (B) enhance the safety and efficiency of interstate and foreign commerce; and
>
> (C) do not impose more than a small burden on interstate or foreign commerce.

The reference in (b)(1) is to a long-established program for harbor project fee review by the Federal Maritime Commission. The Port Director administers this program for CBJ. I have attached copies of the new language and the referenced FMC statute.

The new statutory language essentially restates the constitutional rule described in my July 22, 1999 memorandum to the Assembly on the passenger fee initiative. Briefly, the rule is that we can impose a fee on visitors only to the extent we provide a service to visitors. We cannot charge them a fee for services we provide to someone else, such as ourselves.

Some services, such as dock construction and maintenance, are clearly justifiable as a service to ships and passengers. Others are less defensible. The statute will prevent the most flagrant abuses, such as a fee imposed on ships that merely pass through local waters without stopping. So said Congressman Young in the November 22, 2001 *Congressional Record*, attached. However, it can be used in less egregious circumstances as well. Mr. Young speculated that "generally taxes will not be allowed under this section". *Id.*

Even though the statute does not break any new legal ground, it does provide a reasonably clear and concise statement of the law. In this respect, it is more usable, (both for us and for plaintiffs) than a fuzzy principle extracted from constitutional text and a few judicial cases; which is all we had to work with before the statute.

Also, the statute adds some new emphasis to the constitutional rule. The new language says that fees must be use "solely" to provide a service to the vessel, must "enhance the safety and efficiency" of interstate and foreign commerce, and must impose only a "small" burden on that commerce. We must await judicial interpretation to learn exactly what these qualifiers mean, but they certainly do not make things easier for local port fees.

According to the KTOO story, the Murkowski administration has concluded that the new law prohibits passenger fees. I'm not sure that the Attorney General shares this view: informal contact with his staff suggests that they see it pretty much as I do.

II. Conclusion:

For the most part, the new statute just restates existing constitutional law. It makes no fundamental changes and does not invalidate our port or passenger fees.

However, it will serve to focus attention on how we use the fee revenue. Also, the statutory language is slightly more stringent than the constitutional rule it supplements. As a result, we should take extra care to spend passenger fee revenues on programs (or parts of programs) that benefit only the people who pay the fee. We may not balance our budget by taxing people who cannot vote.

CBJ Law Department
MEMORANDUM

To: Mayor and Assembly

From: John W. Hartle, City Attorney JWH

Subject: Fees on Cruise Lines; Resolution 2294b.

Date: March 12, 2005

You have asked for an analysis of the objections raised by Jim Reeves of Dorsey and Whitney regarding the proposed increases in cruise line fees in Resolution 2294b. I have analyzed all the cases cited by Mr. Reeves, and the other major case law as well. The short answer is that, while there is always some risk regarding particular expenditures, and federal law does provide special protection to interstate and foreign shipping, it appears that the present proposal would pass muster under the U.S. Constitution because the proposal is a fee for services and facilities that benefit the cruise industry, rather than a tax to raise general revenues.

The Tonnage Clause.

The Tonnage Clause of the U.S. Constitution gives the shipping industry a measure of special protection from state and local taxation. The clause provides: "No State shall, without the Consent of Congress, lay any Duty of Tonnage." U.S. Const. Art. I, § 10, cl. 3. It was added to the Constitution on September 15, 1787, according to the notes of James Madison, essentially as a supplement to the Commerce Clause, which also serves to limit state and local regulation or taxation of interstate or foreign commerce.

Under the Tonnage Clause, a municipality cannot levy a general tax on ships for the privilege of entering port; fees for services and facilities, however, can be imposed. There are many cases that make this point. Closest to home is the July, 2004, Superior Court decision in *Polar Tankers, Inc. v. City of Valdez*. Case No. 3AN-00-9665CI. In that case, the court struck down the City of Valdez's Ordinance 99-17 which imposed the "Tanker Tax," a business personal property tax levied mainly on oil tankers. Because the tax was imposed for the admitted purpose of raising general revenues, not based on a particular service or facility for the tankers, the court struck it down.

The fee increase proposed in Resolution 2294b, by contrast, is not intended as a general revenue measure. The resolution would impose fees for the purpose of constructing facilities outlined in the Long-Range Waterfront Plan that benefit the cruise industry. *See* Resolution 2294b, Sec. 2(e), pg. 3, line 22. Courts have consistently found that state or local fees for services or facilities do not violate the Tonnage Clause. In 1877, the U.S. Supreme Court summarized the law as follows:

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> To determine whether the charge prescribed by the ordinance in question is a duty of tonnage, within the meaning of the Constitution, it is necessary to observe carefully its object and essence. If the charge is clearly a duty, a tax, or burden, which in its essence is a contribution claimed for the privilege of entering the port of Keokuk, or remaining in it, or departing from it, imposed, as it is, by authority of the State, and measured by the capacity of the vessel, it is doubtless embraced by the constitutional prohibition of such a duty. *But a charge for services rendered or for conveniences provided is in no sense a tax or a duty.* It is not a hindrance or impediment to free navigation. *The prohibition to the State against the imposition of a duty of tonnage was designed to guard against local hindrances to trade and carriage by vessels, not to relieve them from liability to claims for assistance rendered and facilities furnished for trade and commerce.*

Keokuk Northern Line Packet Co. v. City of Keokuk, 95 U.S. 80, 84 -85 (1877) (emphasis added).

125 years later, courts are still saying the same thing:

> "[A] charge for services rendered or for conveniences provided is in no sense a tax or a duty. It is not a hindrance or impediment to free navigation."); see also *Barber v. Hawai'i*, 42 F.3d 1185, 1196 (9th Cir.1994) ("[A] state is not prohibited from charging reasonable fees in return for services rendered.")...For example, a harbor fee charged for the use of restroom facilities, parking, trash disposal, and security is not a "duty of tonnage" because services are provided in exchange for the fee. See *Barber*, 42 F.3d at 1196. Similarly, if fees are for pilotage, wharfage, use of locks on a navigable river, or for medical inspection, those fees are not unconstitutional duties of tonnage. *See Clyde Mallory*, 296 U.S. at 266, 56 S.Ct. 194.

Captain Andy's Sailing, Inc. v. Johns, 195 F.Supp.2d 1157, 1172 (D.Hawai'i 2001).

> A fee charged to ensure that emergency services are available is also not a duty of tonnage, even if not every ship paying the fee needs the service.

New Orleans Steamship Ass'n v. Plaquemines Port, Harbor & Terminal Dist., 874 F.2d 1018, 1023 (5th Cir 1989), cert. denied, 495 U.S. 932 (1990).

The Commerce Clause.

The Commerce Clause of the U.S. Constitution provides: "The Congress shall have power . . . To regulate commerce with foreign nations, and among the several states . . .." Allocating this authority over foreign and interstate commerce to Congress means that such authority is *not* allocated to states or municipalities; the negative sweep of the Commerce Clause precludes state or local regulation. There are many cases interpreting the Commerce Clause from the earliest days of the federal courts. In the context of shipping, however, the Commerce Clause is not as restrictive as the Tonnage Clause. If a fee or practice is allowed under the Tonnage Clause, the Commerce Clause is not likely to prohibit it.

The Maritime Transportation Security Act of 2002.

As a fairly recent enactment of Congress, this act has no body of developed case law interpreting it. However, from its plain language, it can be seen as the most restrictive of the three main areas of federal law restricting municipal fees on shipping interests. Although not mentioned in Mr. Reeves' memo regarding Resolution 2294b, the Maritime Security Act of 2002 provides his best argument. It provides:

> (b) No taxes, tolls, operating charges, fees, or any other impositions whatever shall be levied upon or collected from any vessel or other water craft, or from its passengers or crew, by any non-Federal interest, if the vessel or water craft is operating on any navigable waters subject to the authority of the United States, or under the right to freedom of navigation on those waters, except for
>
> (1) fees charged under section 2236 of this title;
> (2) reasonable fees charged on a fair and equitable basis that--
> (A) are used solely to pay the cost of a service to the vessel or water craft;
> (B) enhance the safety and efficiency of interstate and foreign commerce; and
> (C) do not impose more than a small burden on interstate or foreign commerce; or
> (3) property taxes on vessels or watercraft, other than vessels or watercraft that are primarily engaged in foreign commerce if those taxes are permissible under the United States Constitution.

This federal statute, among others, in my view comprises "the Consent of Congress" contemplated by the Tonnage Clause. Accordingly, if a project fits its requirements, it will pass muster under the Tonnage Clause and the Commerce Clause as well. This is the statute CBJ has been acting under since its enactment. Sponsored by Rep. Don Young, it was intended to clarify the requirements of the Commerce Clause, according to his address to Congress upon its passage:

> Section 445 [the Act] addresses the current problem, and the potential for greater future problems, of local jurisdictions seeking to impose taxes and fees on vessels merely transiting or making innocent passage through navigable waters subject to the authority of the United States that are adjacent to the taxing community. We are seeing instances in which local communities are seeking to impose taxes or fees on vessels even where the vessel is not calling on, or landing, in the local community. These are cases where no passengers are disembarking, in case of passenger vessels, or no cargo is being unloaded in the case of cargo vessels and where the vessels are not stopping for the purpose of receiving any other service offered by the port. In most instances, these types of taxes would not be allowed under the Commerce Clause of the United States Constitution. Unfortunately, without a statutory clarification, the only means to determine whether the burden is an impermissible burden under the Constitution is to pursue years of litigation. . . .

Conference Report on S. 1214, Maritime Transportation Security Act of 2002; Speech of Hon. Don Young, of Alaska, in the House of Representatives, Thursday, November 14, 2002.

The requirements of this federal statute appear to be straight out of the case law, particularly, the Fifth Circuit's summary of the U.S. Supreme Court *Clyde Mallory* decision. *See Plaquimines*, 874 F.2d 1018, 1021(5th Cir. 1989). One additional issue raised is that of the requirement that any fee "not impose more than a small burden on interstate or foreign commerce . . .." All indications are that the cruise industry is financially healthy at this time, and that the proposed additional one dollar per passenger could be contractually passed on to the cruise consumer, and, therefore, would not impose more than a small burden on interstate or foreign commerce.

Conclusion.

Resolution 2294b would increase the Port Development Fee by one dollar per passenger. Because the resolution requires that all funds collected by the Port Development Fund be spent on projects outlined in the Long-Range Waterfront Plan that benefit the cruise industry, the fee increase would very likely survive a challenge based on the case law from the U.S. Supreme Court and the U.S. Court of Appeals for the Ninth Circuit. In my view, so long as CBJ continues its vigilance in following the requirements of federal law and close cooperation with the industry in making expenditures (as required by Resolution 2294b), a legal challenge would be unlikely to succeed.

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MEMORANDUM February 16, 2004

SUBJECT: HB 207 Legal Issues (Work Order No. 23-LS0850)

TO: Representative Carl Gatto
Attn: Cody Rice

FROM: Kathryn Kurtz
Legislative Counsel

You have asked several questions related to the legality of HB 207.

Do the numbers your staff provided from the administration relating to state costs incurred supporting the cruise industry make HB 207 more defensible in terms of the tonnage clause and the Maritime Transportation Security Act of 2002 (MTSA)? The list of costs potentially attributable to the cruise industry that you provided attached to the letter of January 27, 2004 may be sufficient to satisfy the requirements of the tonnage clause, if that provision is read broadly enough. However, they may not be sufficient to satisfy the Maritime Transportation Security Act of 2002 (MTSA) service-to-vessel requirement for a fee of $100 per passenger.

The tonnage clause prohibits charges "for the privilege of entering, trading in, or lying in a port," but permits charges "for services rendered to and enjoyed by the vessel, such as pilotage, wharfage, or charges for the use of locks on a navigable river, or fees for medical inspection." Clyde Mallory Lines v. Alabama ex. rel. State Docks Commission, 296 U.S. 261, 265-266 (1935) (citations omitted).

In addition, under the Clyde Mallory decision, the tonnage clause permits charges for general services that benefit all harbor users, such as the "policing of a harbor so as to insure the safety and facility of movement of vessels." *Id.* at 266-267. The court reasoned that such services benefit all who enter a harbor:

> It is not any the less a service beneficial to appellant because its vessels have not been given any special assistance. The benefits which flow from the enforcement of regulations, such as the present, to protect and facilitate traffic in a busy harbor inure to all who enter it.

Id. Similarly, a fee to ensure that emergency services will be available was upheld against a tonnage clause challenge, even if "not every ship paying the fee needs the service." New Orleans Steamship Association v. Plaquemines Port, Harbor and Terminal

District, 874 F.2d 1018, 1023 (5th Cir. 1989).

In Barber v. Hawaii, 42 F.3d 1185 (9th Cir. 1994), the plaintiffs acknowledged the ability of states to charge reasonable fees in return for services rendered under the Clyde Mallory case, and further acknowledged provision of rest room facilities, parking, trash disposal, and security would satisfy the Clyde Mallory test. Based on this, the court found that "Hawaii provides services in exchange for the mooring and anchorage fees. The fees are not a duty on tonnage." *Id.* at 1196.

The list of costs you provided includes several programs that relate to navigation in general, including cruise ships, among them harbor project debt service, the marine pilot licensing program, the Department of Labor's marine training program, and the Corps of Engineers harbor program that might conceivably fall within the broader class of services to vessels for which fees are permissible under the tonnage clause. Other services included on the list, such as state parks and the Alaska Railroad, appear to have a much more attenuated relationship to vessels that may not be sufficient to bring them under the rubric of "services to vessels" for purposes of the tonnage clause.

The next question is to what extent the requirements of the tonnage clause and the MTSA are the same. A strong argument can be made that the requirements of the MTSA are more stringent in this regard.

The starting point to answer this question is the language of the MTSA. According to the Ninth Circuit,

> Statutory interpretation begins with the language of the statute. *See United States v. Ron Enters., Inc.*, 489 U.S. 235, 241, 103 L. Ed. 2d 290, 109 S. Ct. 1026 (1989). When the plain meaning of a statutory provision is unambiguous, that meaning is controlling. *Id.* at 242. To determine the plain meaning of a statutory provision, we examine not only the specific provision at issue, but also the structure of the statute as a whole, including its object and policy. *See Green v. Commissioner*, 707 F.2d 404, 405 (9th Cir. 1983). If ambiguity exists, we may use legislative history as an aid to interpretation. *See Id.*; *Mt. Graham Red Squirrel v. Madigan*, 954 F.2d 1441, 1453 (9th Cir. 1992).

Children's Hospital and Health Center v. Belshe, 188 F.3d 1090, 1096 (9th Cir. 1999).

To pass muster under the MTSA, a fee must be used "solely to pay the cost of a service to the vessel or water craft." 33 U.S.C. 5(b)(2)(A). These words could be read to require that fee revenue must pay for services to the vessel carrying the passenger who paid the fee. The language refers to "the vessel," which implies a specific vessel, not "a vessel," which could be any vessel. This phrasing is not ambiguous. However, if the court does look to the legislative history of this provision for additional guidance, they will find Representative Young's comment that "reasonable fees can be charged on a fair and

equitable basis for the cost of service **actually rendered** to the vessel. . . . Generally, taxes will not be allowed under this section." Congressional Record, November 22, 2002, E2143 at E2144, Conference Report on S. 1214, Speech of Hon. Don Young, Nov. 14. 2002 (emphasis added). This indicates legislative intent that "service to the vessel" be construed narrowly for purposes of this statute, more narrowly than the service to vessel concept as it is interpreted in the tonnage clause context.

Looking at the context of the enactment, arguably, such a narrow construction might invalidate some existing passenger fees in place in other states, fees that were in place prior to passage of the MTSA. This may not reflect the intent of the Congress. Also, it is conceivable that the drafters of this provision were writing with the tonnage clause in mind. Most of the courts that have interpreted the tonnage clause have taken fairly liberal views on what constitutes a service to a vessel, permitting fees that provide services to harbor users in general, including emergency services that most individual vessels will not actually use. However, given the clarity of the language of the statute, the courts interpreting the language of the MTSA may not try to interpret it in light of the tonnage clause.

The list of budget components and portions potentially attributable to the cruise industry that you provided does not appear to include any items that would fit the "service actually rendered to the vessel" criteria as I understand it, except possibly the port security grant portion of the Homeland Security Grant Program. Harbor project debt service, the marine pilot licensing program, and the marine training program may benefit the cruise industry, but it would be difficult to argue that they constitute services actually rendered to particular vessels. A harbor is usually not built for a particular vessel, and a marine pilot is probably not trained to work with only a specific vessel. Similarly, the Corps of Engineers harbor program projects in St. Paul and Wrangell would probably not be considered "a service actually rendered" to a particular vessel; it may benefit vessels that actually use those harbors, but it might be difficult to argue that it benefited vessels that do not visit those harbors.

Do the services support a $100 fee?

Independent of the cost of service to vessels requirement discussed above, to qualify for an exception to the MTSA ban on head taxes, a "fee" must be "reasonable." "Reasonable" might be gauged partly by reference to fees charged by other ports. According to the data your staff supplied, cruise ship passenger fees in selected U.S. ports range from $1.30 to $9.35. Internationally, fees range from $1 in the Dominican Republic to $15 in the Bahamas, with Bermuda an outlier at $60. So, Bermuda charges four times as much as the next highest port, and the proposed tax is 40% more than Bermuda charges. The proposed tax to be imposed by HB 207 is more than ten times as much as the other U.S. fees listed.

Reasonable might also be evaluated with reference to the total cost of a cruise. The Royal Caribbean website today is offering "hot deals" on Alaska cruises starting at $999. http://www.royalcaribbean.com/gohome.do, accessed 2/8/04. A fee of $100 would be

about 10% of the whole cruise price for some travelers; that may not be "reasonable" in the sense of inexpensive. On the other hand, travelers may face excise taxes of more than 10% in other contexts, for example on car rentals. I know of no legal authority that says a $100 head tax is inherently unreasonable· however, the size of the tax compared to fees elsewhere and relative to the price of the cruise might be used to argue that the fee is not "reasonable" and therefore violates the MTSA.

In addition, the MTSA requires that a fee "not impose more than a small burden on interstate or foreign commerce." Your staff has provided me with a sheaf of FCC filings to support your position that the burden of a $100 fee on the industry is small, given the financial position of the companies involved. Whether a $100 fee poses more than a small burden in this context is a question of fact requiring the analysis of financial statements rather than legal expertise. I can not predict with any degree of accuracy how a court will answer this question. Again, the MTSA is so new that there is no case law available interpreting "small burden" in this particular context.

Please explain the distinction between the legal requirement to "use the funds solely for the costs of a service to a watercraft . . . " and an unconstitutional dedication of funds.

As discussed above, the MTSA requires that fees levied on passengers be used "solely to pay the cost of a service to the vessel or water craft." 33 U.S.C. 5(b)(2)(A).

Article IX, sec. 7, Constitution of the State of Alaska, generally prohibits the dedication of funds:

> **SECTION 7. Dedicated Funds.** The proceeds of any state tax or license shall not be dedicated to any special purpose, except as provided in section 15 of this article or when required by the federal government for state participation in federal programs. This provision shall not prohibit the continuance of any dedication for special purposes existing upon the date of ratification of this section by the people of Alaska.

The MTSA addresses the use of funds. It does not require a dedication of funds per se.

As long as revenue from a fee levied on cruise ship passengers were used solely to pay the cost of a service to the vessel, the MTSA would arguably be satisfied, regardless whether Alaska adopts a statutory provision requiring that the funds be spent on the cost of a service to the vessel. Adopting such a statute would likely violate the prohibition on dedicated funds. Spending the money as required by the MTSA without adopting a statute specifically dedicating the stream of fee revenue should not pose a dedicated fund problem, but would require institutional memory and discipline on the part of the legislature.

How would a packaged tour tax differ from a cruise ship head tax in terms of defensibility?

Under the MTSA, a packaged tour tax would not differ from a cruise ship head tax in terms of defensibility. The MTSA applies to all taxes, tolls, fees, and impositions on passengers, vessels, and so forth. The MTSA provides:

> No taxes, tolls, operating charges, fees, or any other impositions whatever shall be levied upon or collected from any vessel or other water craft, or from its passengers or crew, by any non-Federal interest, if the vessel or water craft is operating on any navigable waters subject to the authority of the United States, or under the right to freedom of navigation on those waters, except for--
>
> (1) fees charged under section 208 of the Water Resources Development Act of 1986 (33 U.S.C. 2236); or
>
> (2) reasonable fees charged on a fair and equitable basis that--
>
> (A) are used solely to pay the cost of a service to the vessel or water craft;
>
> (B) enhance the safety and efficiency of interstate and foreign commerce; and
>
> (C) do not impose more than a small burden on interstate or foreign commerce.

33 U.S.C. 5(b).

The tonnage clause is a slightly different animal. There is one case that could be used to argue that a broader packaged tour tax that was not limited to cruise ships or cruise ship passengers should pass muster under the tonnage clause. *See* Hartley Marine Corporation v. Mierke, 474 S.E.2d 599 (W.Va. 1996) and the discussion of that case in my memo to you of March 19, 2003 at page 3. That decision is from a state court, and not binding precedent in Alaska, although a court might find it to have some persuasive value. However, there have been no additional reported decisions since my prior memo citing that case, and none of the decisions citing that case make the same argument related to the tonnage clause (although some of them discuss tax issues relating to the commerce clause).

You also asked how the Hartley Marine case passed muster under the privileges and immunities clause. The answer is that the privileges and immunities clause was apparently not raised in that case; it is not mentioned in the decision.

Commerce Clause

Your staff requested inclusion in this memo of the material relating to the commerce clause in my memo to you of March 19, 2003. Your staff also requested an analysis of the fourth prong of the commerce clause test, whether the tax discriminates against interstate commerce, in relation to the cruise ship head tax, particularly whether exempting Alaska Marine Highway System vessels from the tax proposed in HB 207 would violate the commerce clause.

When the framers wrote the federal constitution, they were very concerned about removing barriers to free trade between the states. This concern was addressed in the Commerce Clause in Article I, section 8 of the Constitution of the United States. The commerce clause expressly permits Congress to regulate commerce among the several states. It has also been interpreted to include a "negative command, known as the dormant Commerce Clause, prohibiting certain state taxation even where Congress has failed to legislate on the subject." Oklahoma Tax Commission v. Jefferson Lines, Inc., 514 U.S. 175, 179 (1995).

The Supreme Court has developed a four-part test for determining the validity of a tax under the federal commerce clause:

(1) whether the activity taxed has a sufficient nexus with the taxing state;
(2) whether the tax is fairly related to benefits provided by the state to the taxpayer;
(3) whether the tax is fairly apportioned to local activities; and
(4) whether the tax discriminates against interstate commerce.

Siong v. State, Department of Revenue, 622 P.2d 967, 973 (Alaska 1981), *citing* Complete Auto Transit, Inc., v. Brady, 430 U.S. 274, 279 (1977).[1]

The first prong of the Complete Auto deals with "nexus," or the quantity and quality of connections between the taxing state and the activity being taxed. The many interactions between cruise ships and coastal communities in Alaska would be found sufficient to satisfy the first prong of the Complete Auto test. Cruise ships and ferries provide overnight accommodations in part to enable passengers to enjoy the goods, services, and attractions available on shore in Alaskan communities. Cruise ships and ferries dock in Alaska ports, purchase goods and services from local vendors, and cruise ships sell on-shore tours and other services to disembarking passengers. Other state taxes involving vessels have easily met this prong of the Complete Auto test by virtue of less extensive contacts with shore. *See* Siong v. State, Department of Revenue, 622 P.2d 967, 970-971 (Alaska 1981); Hartley Marine Corporation v. Mierke, 474 S.E.2d 599, 608-609 (W. Va. 1996).

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[1] / Although this is an older case, the four-part test it describes is still good law. *See for example* Oklahoma Tax Commission v. Jefferson Lines, Inc., 514 U.S. 175, 183 (1995). Sometimes courts first analyze whether a law treats in-state and out-of-state interest differently, and then move to the Complete Auto test. *See* Barber v. Hawaii, 42 F.3d 1185, 1194 (9th Cir. 1994); Hartley Marine Corporation v. Mierke, 474 S.E.2d 599, 607 (W.Va. 1996).

The second prong, requiring a fair relationship to benefits provided by the state to the taxpayer, is also easily met. This relationship need not be especially close. According to the United States Supreme Court,

> If the event is taxable, the proceeds from the tax may ordinarily be used for purposes unrelated to the taxable event. ... The bus terminal may not catch fire during the sale, and no robbery may be foiled while the buyer is getting his ticket, but police and fire protection, along with the usual and usually forgotten advantages conferred by the State's maintenance of a civilized society, are justifications enough for the imposition of a tax.

Oklahoma Tax Commission v. Jefferson Lines, 514 U.S. at 199-200 (upholding an Oklahoma sales tax on the full price of bus tickets, including tickets for travel between states).[2] *See also* Hartley Marine Corporation v. Mierke, 474 S.E.2d at 610 ("There simply is no requirement that the tax imposed result in a direct and attributable benefit to a taxpayer.") Cruise ships and disembarking ferry and cruise ship passengers use many services provided by state and local government. For purposes of the commerce clause, it is not necessary that each vessel or passenger actually need or use each service in order to justify the tax.

The apportionment prong of the Complete Auto test is intended to ensure that "each State taxes only its fair share of an interstate transaction." *Id.* at 184, *quoting* Goldberg v. Sweet, 488 U.S. 252 (1989). Although there may be some question about how to apportion nights spent in transit between Canada and Alaska, assuming there is an equivalent Canadian tax, there should be no apportionment problem if the tax is calculated based on nights spent on Alaska waters.

The final commerce clause test element is whether the tax discriminates against interstate commerce. This prong of the Complete Auto test, according to the Alaska Supreme Court, means that a state cannot impose a tax which discriminates against interstate commerce by providing a direct commercial advantage to local businesses relative to interstate business. Siong v. Department of Revenue, 622 P.2d 967, 973 (Alaska 1981).

Discrimination against interstate commerce and HB 207

You asked whether the provisions of HB 207, particularly the exclusion of vessels operated by the state (including the Alaska Marine Highway System vessels), could be found to discriminate against interstate commerce. The leading U.S. Supreme Court case on the discrimination prong of the commerce clause test is Camps Newfound/Owatonna v. Harrison, 520 U.S. 564 (1996). In that case, the court invalidated a property tax that

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[2] / Similarly, to satisfy the requirements of due process, the relationship does not have to be particularly close--"[a]s long as the services are available, the issue of usage by the taxpayers is irrelevant." Keane v. Local Boundary Commission, 893 P.2d 1239, 1248 (Alaska 1995).

exempted property of charitable organizations generally, but offered only a limited tax benefit to charitable organizations "conducted or operated principally for the benefit of persons who are not residents." *Id.* at 568, 595.

In that case, the court first established that the camp was engaged in commerce, comparing it to hotels that offer guests goods and services that are consumed locally, noting the provision of services to out of state campers. *Id.* at 574. The court explained that the purpose of the clause was to provide a 'barrier against protectionism," and that the "'paradigmatic . . . law discriminating against interstate commerce is the protective [import] tariff or customs duty, which taxes goods imported from other States, but does not tax similar products produced in State.'" *Id.* at 575, *quoting* West Lynn Creamery v. Healy, 512 U.S. 186 (1994).

The definition of "commercial passenger vessel" in the bill excludes certain types of vessels, but does not overtly discriminate against interstate commerce in a way that would be clearly prohibited under the interstate commerce clause. The exclusion for non-commercial and government vessels applies to *all* noncommercial and government vessels, not just those operated by the state of Alaska or businesses incorporated in Alaska or those serving primarily Alaskans.

Conclusion
A $100 tax on cruise ship passengers, as proposed in HB 207, would probably be held to violate the MTSA. A packaged tour tax that extended beyond the cruise ship industry would probably also violate the MTSA. However, as written HB 207 does not create a dedicated fund problem under the state constitution.

In order to withstand scrutiny under the MTSA, the tax would have to meet all of the requirements of the exception in 33 U.S.C. 5(b)(2)(A), including that requirement that the fee be used "solely to pay the cost of a service to the vessel or water craft." A smaller fee with a direct link to the provision of specific services to specific vessels would be easier to defend.

The tax in HB 207 might also be held to violate the federal tonnage clause, although what constitutes a "service to a vessel" has been interpreted broadly enough in the tonnage clause context to permit some types of taxes on vessels. The tax might well withstand scrutiny under the commerce clause.

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MEMORANDUM March 19, 2003

SUBJECT: Cruise Ship Head Tax (Work Order No. 23-LS0850\A)

TO: Representative Carl Gatto
Attn: Jennifer Yuhas

FROM: Kathryn L. Kurtz KK
Legislative Counsel

An excise tax on passengers traveling on commercial passenger vessels might encounter challenges based on the commerce and tonnage clauses of the Constitution of the United States.

Commerce Clause

When the framers wrote the federal constitution, they were very concerned about removing barriers to free trade between the states. This concern was addressed in the Commerce Clause in Article I, section 8 of the Constitution of the United States. The commerce clause expressly permits Congress to regulate commerce among the several states. It has also been interpreted to include a "negative command, known as the dormant Commerce Clause, prohibiting certain state taxation even where Congress has failed to legislate on the subject." Oklahoma Tax Commission v. Jefferson Lines, Inc., 514 U.S. 175, 179 (1995).

The Supreme Court has developed a four-part test for determining the validity of a tax under the federal commerce clause:

(1) whether the activity taxed has a sufficient nexus with the taxing state;
(2) whether the tax is fairly related to benefits provided by the state to the taxpayer;
(3) whether the tax is fairly apportioned to local activities; and
(4) whether the tax discriminates against interstate commerce.

Siong v. State, Department of Revenue, 622 P.2d 967, 973 (Alaska 1981), *citing* Complete Auto Transit, Inc., v. Brady, 430 U.S. 274, 279 (1977).[1]

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[1] / Although this is an older case, the four-part test it describes is still good law. *See for example* Oklahoma Tax Commission v. Jefferson Lines, Inc., 514 U.S. 175, 183 (1995). Sometimes courts first analyze whether a law treats in-state and out-of-state interest

The first prong of the Complete Auto deals with "nexus," or the quantity and quality of connections between the taxing state and the activity being taxed. The many interactions between cruise ships and coastal communities in Alaska would be found sufficient to satisfy the first prong of the Complete Auto test. Cruise ships and ferries provide overnight accommodations in part to enable passengers to enjoy the goods, services, and attractions available on shore in Alaskan communities. Cruise ships and ferries dock in Alaska ports, purchase goods and services from local vendors, and cruise ships sell on-shore tours and other services to disembarking passengers. Other state taxes involving vessels have easily met this prong of the Complete Auto test by virtue of less extensive contacts with shore. *See* Sjong v. State, Department of Revenue, 622 P.2d 967, 970-971 (Alaska 1981); Hartley Marine v. Mierke, 474 S.E.2d 599, 608-609 (W. Va. 1996).

The second prong, requiring a fair relationship to benefits provided by the state to the taxpayer, is also easily met. This relationship need not be especially close. According to the United States Supreme Court,

> If the event is taxable, the proceeds from the tax may ordinarily be used for purposes unrelated to the taxable event. ... The bus terminal may not catch fire during the sale, and no robbery may be foiled while the buyer is getting his ticket, but police and fire protection, along with the usual and usually forgotten advantages conferred by the State's maintenance of a civilized society, are justifications enough for the imposition of a tax.

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The apportionment prong of the Complete Auto test is intended to ensure that "each State taxes only its fair share of an interstate transaction." *Id.* at 184, *quoting* Goldberg v. Sweet, 488 U.S. 252 (1989). Although there may be some question about how to

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differently, and then move to the Complete Auto test. *See* Barber v. Hawaii, 42 F.3d 1185, 1194 (9th Cir. 1994); Hartley Marine Corporation v. Mierke, 474 S.E.2d 599, 607 (W.Va. 1996).

[2] / Similarly, to satisfy the requirements of due process, the relationship does not have to be particularly close--"[a]s long as the services are available, the issue of usage by the taxpayers is irrelevant." Keane v. Local Boundary Commission, 893 P.2d 1239, 1248 (Alaska 1995).

apportion nights spent in transit between Canada and Alaska, assuming there is an equivalent Canadian tax, there should be no apportionment problem if the tax is calculated based on nights spent on Alaska waters.

The final commerce clause test element is whether the tax discriminates against interstate commerce. This prong of the Complete Auto test, according to the Alaska Supreme Court, means that a state cannot impose a tax which discriminates against interstate commerce by providing a direct commercial advantage to local businesses relative to interstate business. Sjong v. Department of Revenue, 622 P.2d 967, 973 (Alaska 1981).

The Tonnage Clause

The tonnage clause is a relative of the commerce clause; it too is concerned with ensuring the free flow of commerce between states. It prohibits a state from laying "any Duty of Tonnage" without the consent of Congress. The term "tonnage" originally referred to the internal capacity of a vessel. Clyde Mallory Lines v. Alabama ex rel State Docks, 296 U.S. 261, 265 (1935). However, the clause has been interpreted more expansively to include "all taxes and duties regardless of their name or form, and even though not measured by the tonnage of the vessel, which operate to impose a charge for the privilege of entering, trading in, or lying in a port." *Id.* The clause prohibits "reliance on tonnage duties to raise general revenues, to regulate trade, or to charge for the privilege of entering, lying in, or trading in a port." New Orleans S.S. v. Plaquemines Port, Harbor and Terminal District, 874 F.2d 1018, 1023 (5th Cir. 1989).

The clause permits states to charge for services rendered to a vessel, such as pilotage, wharfage, use of locks on a navigable river, or policing of a harbor, Clyde Mallory Lines, 296 U.S. at 265, or for ensuring the availability of a service, such as fire fighting, even though not every vessel will actually need the service. Plaquemines, 874 F.2d at 1023.

The first question to ask in a tonnage clause analysis is whether the tax in question fits into the tonnage clause framework--whether it might reasonably be construed as a charge for the privilege of entering, trading in, or lying in a port.

West Virginia considered this issue in Hartley Marine Corporation v. Mierke, 474 S.E.2d 599 (W.Va. 1996). The statute challenged in that case taxed the use or consumption by "motor carriers"--including buses, trucks, and aircraft as well as barges and watercraft--of fuel purchased outside the state. Id. at 672. The court held:

> Appellants urge this Court to view the use tax at issue as a charge for navigation of the rivers in violation of the Duty of Tonnage Clause. If this use tax were solely imposed for fuel consumption on the waters of this state, Appellants' arguments would be more convincing. The use tax at issue, however, is not a prohibited toll on the use of this state's navigable waterways, but an excise tax on the use of fuel which is imposed on all motor carriers operating within this state, including, buses, trucks, trains, and aircraft.

Id. at 612. Because the tax did not fall exclusively on users of the state's waterways, the court did not see it as a tonnage tax.

The tax imposed in West Virginia affected vessels and buses and aircraft, as well as commercial passenger vessels. A tax dealing exclusively with commercial passenger vessels may be more vulnerable to a tonnage clause argument.

Hawaii imposes fees for anchoring and mooring in state harbors. In Barber v. Hawaii, 42 F.3d 1185 (9th Cir. 1994), the plaintiffs argued that mooring and anchorage fees collected by the state were a duty on tonnage that violated the federal tonnage clause. The plaintiffs conceded that under the Clyde Mallory case, a state was permitted to charge reasonable fees for services rendered. They apparently also conceded that provision of restroom facilities, parking, trash disposal and security services would be sufficient to satisfy the requirements of the Clyde Mallory case. The plaintiffs then tried to argue that because the services provided were open to the public and not provided specifically for those paying the fees, that the state was effectively not providing those services. The court rejected this argument finding that Hawaii in fact provided services in exchange for the mooring and anchorage fees, and that the fees were not a duty on tonnage. Barber v. Hawaii, 42 F.3d at 1196.

The plaintiffs in Barber v. Hawaii apparently did not argue the tonnage clause issue very well, and the court's discussion of the clause is cursory. However, the case upheld the fees in question. In contrast, a recent Rhode Island case held that a registration fee on all boats operated in Rhode Island waters for more than 90 days was an unconstitutional tonnage tax, because the revenues from the fee would not necessarily be used for services benefitting boaters. State v. Turnbaugh, 705 A.2d 530 (R.I. 1997).

The Rhode Island statute provided that the proceeds from the registration fee, subject to approval of the General Assembly, should be allocated to fund expenses of the Department of Environmental Management, harbor maintenance, boating safety and other boating related programs. *Id.* at 532. The court wrote:

> [I]t should be noted that any funds collected under the provisions of this chapter were required to be allocated, distributed, and used subject to the approval of the General Assembly. Thus this alleged restricted receipt account was entirely subject to being used as a general-revenue measure and not merely for the purpose of providing services to boats, boaters, and navigational improvements.

The court rejected the state's argument that the registration fee was merely a property tax, and instead concluded that it was "a classic form of tonnage tax specifically prohibited by the Constitution of the United States." *Id.* at 533.

Unlike the Ninth Circuit case cited above, the Rhode Island case would not be binding precedent on a federal district court in Alaska. Neither the Ninth Circuit case nor the Rhode Island case would be binding on an Alaska state court, but a state court might regard such authorities as persuasive. The Rhode Island decision certainly demonstrates that the tonnage clause is not a dead letter, and in light of the Rhode Island decision, caution would certainly be in order in imposing any fee or tax exclusively on vessels, unless the proceeds were used to provide services to vessels.

Other Potential Constitutional Issues

A number of other constitutional provisions might be raised in an attack on a tax on passengers traveling on commercial passenger vessels.

If a tax can survive scrutiny under the second prong of the Complete Auto test and is at least minimally rational, it can probably survive a due process challenge as well. *See* Keane v. Local Boundary Commission, 893 P.2d 1239, 1248 (Alaska 1995) ("As long as services are available, the issue of usage by the taxpayer is irrelevant."); Katmailand, Inc. v. Lake and Peninsula Borough, 904 P.2d 397, 402 (Alaska 1995).

Equal protection is another potential issue. Alaska uses a sliding scale equal protection test, but the interests involved in taxation fall at the low end of the scale and are reviewed under "relaxed scrutiny." *Id.* at 401, n. 6. The federal equal protection clause requires only that the tax be "rationally related to a legitimate governmental interest." *Id.* at 401. As the Alaska Supreme Court observed, "[t]axes are rarely found to be without a rational basis." *Id.* at 400.

Other potential arguments might be based on the foreign commerce clause or the privileges and immunities clause of the federal constitution.

Conclusion

A head tax on cruise ship passengers might encounter challenges based on several provisions of the United States constitution, particularly the commerce clause and tonnage clauses.

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HOUSE BILL NO. 207

IN THE LEGISLATURE OF THE STATE OF ALASKA

TWENTY-THIRD LEGISLATURE - FIRST SESSION

BY REPRESENTATIVE GATTO

Introduced: 3/24/03
Referred:

A BILL

FOR AN ACT ENTITLED

"An Act relating to taxes regarding certain commercial passenger vessels operating in the state; and providing for an effective date."

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

*** Section 1.** AS 43 is amended by adding a new chapter to read:

Chapter 52. Excise Tax on Passengers Traveling Aboard a Commercial Passenger Vessel.

Sec. 43.52.010. Levy of excise tax on passengers traveling aboard a commercial passenger vessel. There is imposed an excise tax on passengers traveling in the marine waters of the state aboard a commercial passenger vessel that provides overnight accommodations.

Sec. 43.52.020. Rate of tax. The tax imposed by this chapter is levied at a rate of $100 a passenger a voyage.

Sec. 43.52.030. Liability for payment of tax. (a) A passenger traveling in the marine waters of the state aboard a commercial passenger vessel that provides

overnight accommodations is liable for the tax imposed by this chapter. The tax

(1) shall be collected by the person who provides the travel to the passenger; and

(2) is due and payable to the department

(A) by the person who provides the travel to the passenger, regardless of whether the person actually collects the tax from the passenger; and

(B) in the manner and at the times required by the department by regulation.

(b) A passenger is not liable for the tax under this chapter if that passenger was liable for the tax within the preceding 30 days.

(c) A person who provides travel for a passenger who, under (b) of this section, would not be liable for the tax under this chapter is not required to collect and pay the tax to the department if the person reasonably believes that the passenger is not liable for the tax under (b) of this section.

Sec. 43.52.040. Disposition of proceeds. The proceeds from the tax imposed by this chapter shall be deposited in the general fund.

Sec. 43.52.050. Administration. (a) The department shall

(1) administer this chapter; and

(2) collect, and supervise and enforce the collection of, taxes due under this chapter and penalties as provided in AS 43.05.

(b) The department may adopt regulations to carry out the purposes of this chapter.

Sec. 43.52.900. Definitions. In this chapter, unless the context otherwise requires,

(1) "commercial passenger vessel" means a vessel that is used in the common carriage of passengers in commerce; "commercial passenger vessel" does not include a

(A) vessel with an overnight accommodation capacity for fewer than 12 passengers;

(B) noncommercial vessel or a vessel operated by the state, the

United States, or a foreign government; or

(C) vessel licensed under AS 16.05.490 and used in charter service for the recreational taking of fish and shellfish;

(2) "marine waters of the state" means the marine bays, sounds, rivers, inlets, straits, passages, canals, Pacific Ocean, Gulf of Alaska, Bering Sea, and Arctic Ocean within the territorial limits of the state, and all other bodies of marine water that are wholly or partially within the state or are under the jurisdiction of the state;

(3) "passenger" means a person with whom a common carrier has contracted for carriage from one place to another.

* **Sec. 2.** The uncodified law of the State of Alaska is amended by adding a new section to read:

TRANSITION: REGULATIONS. Notwithstanding sec. 4 of this Act, the Department of Revenue may proceed to adopt regulations to implement sec. 1 of this Act. The regulations take effect under AS 44.62 (Administrative Procedure Act), but not before the effective date of sec. 1 of this Act.

* **Sec. 3.** Section 2 of this Act takes effect immediately.

* **Sec. 4.** Section 1 of this Act takes effect January 1, 2004.

LEGAL SERVICES

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Juneau, Alaska 99801-1182
Deliveries to: 129 6th St., Rm. 329

MEMORANDUM March 22, 2002

SUBJECT: Cruise Ship Head Tax; SB 290

TO: Senator John Cowdery
Attn: Don Smith

FROM: Kathryn L. Kurtz KLK
Legislative Counsel

An excise tax on passengers traveling on commercial passenger vessels might engender challenges based on the commerce and tonnage clauses of the Constitution of the United States.

Commerce Clause

When the framers wrote the federal constitution, they were very concerned about removing barriers to free trade between the states. This concern was addressed in the Commerce Clause in Article I, section 8 of the Constitution of the United States. The commerce clause expressly permits Congress to regulate commerce among the several states. It has also been interpreted to include a "negative command, known as the dormant Commerce Clause, prohibiting certain state taxation even where Congress has failed to legislate on the subject." Oklahoma Tax Commission v. Jefferson Lines, Inc., 514 U.S. 175, 179 (1995).

The Supreme Court has developed a four-part test for determining the validity of a tax under the federal commerce clause:

(1) whether the activity taxed has a sufficient nexus with the taxing state;
(2) whether the tax is fairly related to benefits provided by the state to the taxpayer;
(3) whether the tax is fairly apportioned to local activities; and
(4) whether it discriminates against interstate commerce.

Siong v. State, Department of Revenue, 622 P.2d 967, 973 (Alaska 1981), *citing* Complete Auto Transit, Inc., v. Brady, 430 U.S. 274, 279 (1977).[1]

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[1] Although this is an older case, the four-part test it describes is still good law. *See for example* Oklahoma Tax Commission v. Jefferson Lines, Inc., 514 U.S. 175, 183 (1995). Sometimes courts first analyze whether a law treats in-state and out-of-state interest

The first prong of the Complete Auto deals with "nexus," or the quantity and quality of connections between the taxing state and the activity being taxed. The many interactions between cruise ships and coastal communities in Alaska would be found sufficient to satisfy the first prong of the Complete Auto test. Cruise ships and ferries provide overnight accommodations in part to enable passengers to enjoy the goods, services, and attractions available on shore in Alaskan communities. Cruise ships and ferries dock in Alaska ports, purchase goods and services from local vendors, and cruise ships sell on-shore tours and other services to disembarking passengers. Other state taxes involving vessels have easily met this prong of the Complete Auto test by virtue of less extensive contacts with shore. *See* Sjong v. State, Department of Revenue, 622 P.2d 967, 970-971 (Alaska 1981); Hartley Marine v. Mierke, 474 S.E.2d 599, 608-609 (W. Va. 1996).

The second prong, requiring a fair relationship to benefits provided by the state to the taxpayer, is also easily met. This relationship need not be especially close. According to the United States Supreme Court,

> If the event is taxable, the proceeds from the tax may ordinarily be used for purposes unrelated to the taxable event. ... The bus terminal may not catch fire during the sale, and no robbery may be foiled while the buyer is getting his ticket, but police and fire protection, along with the usual and usually forgotten advantages conferred by the State's maintenance of a civilized society, are justifications enough for the imposition of a tax.

Oklahoma Tax Commission v. Jefferson Lines, 514 U.S. at 199-200 (upholding an Oklahoma sales tax on the full price of bus tickets, including tickets for travel between states).[2] *See also* Hartley Marine v. Mierke, 474 S.E.2d at 610 ("There simply is no requirement that the tax imposed result in a direct and attributable benefit to a taxpayer.") Cruise ships and disembarking ferry and cruise ship passengers use many services provided by state and local government. For purposes of the commerce clause, it is not necessary that each vessel or passenger actually need or use each service in order to justify the tax.

The apportionment prong of the Complete Auto test is intended to ensure that "each State taxes only its fair share of an interstate transaction." *Id.* at 184, *quoting* Goldberg v. Sweet, 488 U.S. 252 (1989). Although there may be some question about how to

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differently, and then move to the Complete Auto test. *See* Barber v. Hawaii, 42 F.3d 1185, 1194 (9th Cir. 1994); Hartley Marine Corporation v. Mierke, 474 S.E.2d 599, 607 (W.Va. 1996).

[2] Similarly, to satisfy the requirements of due process, the relationship does not have to be particularly close--"[a]s long as the services are available, the issue of usage by the taxpayers is irrelevant." Keane v. Local Boundary Commission, 893 P.2d 1239, 1248 (Alaska 1995).

apportion nights spent in transit between Canada and Alaska, assuming there is an equivalent Canadian tax, there should be no apportionment problem if the tax is calculated based on nights spent on Alaska waters.

The final commerce clause test element is whether the tax discriminates against interstate commerce. This prong of the Complete Auto test, according to the Alaska Supreme Court, means that a state cannot impose a tax which discriminates against interstate commerce by providing a direct commercial advantage to local businesses relative to interstate business. Siong v. Department of Revenue, 622 P.2d 967, 973 (Alaska 1981).

The Tonnage Clause

The tonnage clause is a relative of the commerce clause; it too is concerned with ensuring the free flow of commerce between states. It prohibits a state from laying "any Duty of Tonnage" without the consent of Congress. The term "tonnage" originally referred to the internal capacity of a vessel. Clyde Mallory Lines v. Alabama ex rel State Docks, 296 U.S. 261, 265 (1935). However, the clause has been interpreted more expansively to include "all taxes and duties regardless of their name or form, and even though not measured by the tonnage of the vessel, which operate to impose a charge for the privilege of entering, trading in, or lying in a port." *Id.* The clause prohibits "reliance on tonnage duties to raise general revenues, to regulate trade, or to charge for the privilege of entering, lying in, or trading in a port." New Orleans S.S. v. Plaquemines Port, Harbor and Terminal District, 874 F.2d 1018, 1023 (5th Cir. 1989).

The clause permits states to charge for services rendered to a vessel, such as pilotage, wharfage, use of locks on a navigable river, or policing of a harbor, Clyde Mallory Lines, 296 U.S. at 265, or for ensuring the availability of a service, such as fire fighting, even though not every vessel will actually need the service. Plaquemines, 874 F.2d at 1023.

The first question to ask in a tonnage clause analysis is whether the tax in question fits into the tonnage clause framework--whether it might reasonably be construed as a charge for the privilege of entering, trading in, or lying in a port.

West Virginia considered this issue in Hartley Marine Corporation v. Mierke, 474 S.E.2d 599 (W.Va. 1996). The statute challenged in that case taxed the use or consumption by "motor carriers"--including buses, trucks, and aircraft as well as barges and watercraft--of fuel purchased outside the state. Id. at 672. The court held:

> Appellants urge this Court to view the use tax at issue as a charge for navigation of the rivers in violation of the Duty of Tonnage Clause. If this use tax were solely imposed for fuel consumption on the waters of this state, Appellants' arguments would be more convincing. The use tax at issue, however, is not a prohibited toll on the use of this state's navigable waterways, but an excise tax on the use of fuel which is imposed on all motor carriers operating within this state, including, buses, trucks, trains, and aircraft.

Id. at 612. Because the tax did not fall exclusively on users of the state's waterways, the court did not see it as a tonnage tax.

The tax imposed in West Virginia affected vessels and buses and aircraft, as well as commercial passenger vessels. A tax dealing exclusively with commercial passenger vessels may be more vulnerable to a tonnage clause argument.

Hawaii imposes fees for anchoring and mooring in state harbors. In Barber v. Hawaii, 42 F.3d 1185 (9th Cir. 1994), the plaintiffs argued that mooring and anchorage fees collected by the state were a duty on tonnage that violated the federal tonnage clause. The plaintiffs conceded that under the Clyde Mallory case, a state was permitted to charge reasonable fees for services rendered. They apparently also conceded that provision of restroom facilities, parking, trash disposal and security services would be sufficient to satisfy the requirements of the Clyde Mallory case. The plaintiffs then tried to argue that because the services provided were open to the public and not provided specifically for those paying the fees, that the state was effectively not providing those services. The court rejected this argument finding that Hawaii in fact provided services in exchange for the mooring and anchorage fees, and that the fees were not a duty on tonnage. Barber v. Hawaii, 42 F.3d at 1196.

The plaintiffs in Barber v. Hawaii apparently did not argue the tonnage clause issue very well, and the court's discussion of the clause is cursory. However, the case upheld the fees in question. In contrast, a recent Rhode Island case held that a registration fee on all boats operated in Rhode Island waters for more than 90 days was an unconstitutional tonnage tax, because the revenues from the fee would not necessarily be used for services benefitting boaters. State v. Turnbaugh, 705 A.2d 530 (R.I. 1997).

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> [I]t should be noted that any funds collected under the provisions of this chapter were required to be allocated, distributed, and used subject to the approval of the General Assembly. Thus this alleged restricted receipt account was entirely subject to being used as a general-revenue measure and not merely for the purpose of providing services to boats, boaters, and navigational improvements.

The court rejected the state's argument that the registration fee was merely a property tax, and instead concluded that it was "a classic form of tonnage tax specifically prohibited by the Constitution of the United States." *Id.* at 533.

Unlike the Ninth Circuit case cited above, the Rhode Island case would not be binding precedent on a federal district court in Alaska. Neither the Ninth Circuit case nor the Rhode Island case would be binding on an Alaska state court, but a state court might regard such authorities as persuasive. The Rhode Island decision certainly demonstrates that the tonnage clause is not a dead letter, and in light of the Rhode Island decision, caution would certainly be in order in imposing any fee or tax on exclusively on vessels, unless the proceeds were used to provide services to vessels.

Other Potential Constitutional Issues

A number of other constitutional provisions might be raised in an attack on a tax on passengers traveling on commercial passenger vessels.

If a tax can survive scrutiny under the second prong of the Complete Auto test and is at least minimally rational, it can probably survive a due process challenge as well. *See* Keane v. Local Boundary Commission, 893 P.2d 1239, 1248 (Alaska 1995) ("As long as services are available, the issue of usage by the taxpayer is irrelevant."); Katmailand, Inc v. Lake and Peninsula Borough, 904 P.2d 397, 402 (Alaska 1995).

Equal protection is another potential issue. Alaska uses a sliding scale equal protection test, but the interests involved in taxation fall at the low end of the scale and are reviewed under "relaxed scrutiny." *Id.* at 401, n. 6. The federal equal protection clause requires only that the tax be "rationally related to a legitimate governmental interest." *Id.* at 401. As the Alaska Supreme Court observed, "[t]axes are rarely found to be without a rational basis." *Id.* at 400.

Other potential arguments might be based on the foreign commerce clause or the privileges and immunities clause of the federal constitution.

Conclusion

A head tax on cruise ship passengers might encounter challenges based on several provisions of the United States constitution, particularly the commerce clause and tonnage clauses.

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MEMORANDUM May 5, 2000

SUBJECT: Cruise Ship Head Tax

TO: Representative Ramona Barnes

FROM: Pamela Finley
Revisor of Statutes

You have asked whether there are legal problems with adding a cruise ship head tax like that in CSSB 308(FIN) to HB 3002.

Single Subject
HB 3002 addresses public employee compensation and benefits. The only conceivable link between HB 3002 and a cruise ship head tax would be "public finance," but this may be too broad to be upheld. See Harbor v. Deukmejian, 742 P.2d 1290 (Calif. 1987). Of course, the Senate could decide to introduce and pass the "head tax" bill as separate legislation.

Constitutional Issues
The tax in CSSB 308(FIN) may be subject to constitutional challenges. In particular, I think it might engender challenges based on the commerce and tonnage clauses of the Constitution of the United States.

Commerce Clause
When the framers wrote the federal constitution, they were very concerned about removing barriers to free trade between the states. This concern was addressed in the Commerce Clause in Article I, section 8 of the Constitution of the United States. The commerce clause expressly permits Congress to regulate commerce among the several states. It has also been interpreted to include a "negative command, known as the dormant commerce Clause, prohibiting certain state taxation even where Congress has failed to legislate on the subject." Oklahoma Tax Commission v. Jefferson Lines, Inc., 514 U.S. 175, 179. (1995).

The Supreme Court has developed a four-part test for determining the validity of a tax under the federal commerce clause:

(1) whether the activity taxed has a sufficient nexus with the taxing state;
(2) whether the tax is fairly related to benefits provided by the state to the taxpayer;
(3) whether the tax is fairly apportioned to local activities; and
(4) whether it discriminates against interstate commerce.

Siong v. State, Department of Revenue, 622 P.2d 967, 973 (Alaska 1981), *citing* Complete Auto Transit, Inc., v. Brady, 430 U.S. 274, 279 (1977).[iv]

The first prong of the Complete Auto deals with "nexus," or the quantity and quality of connections between the taxing state and the activity being taxed. The activity taxed by a bed tax would be either the provision of accommodations, or the privilege of renting or using accommodations, depending on how the tax was structured. In either case, the many interactions between cruise ships and coastal communities in Alaska would be sufficient to satisfy the first prong of the Complete Auto test. Cruise ships and ferries provide overnight accommodations in part to enable passengers to enjoy the goods, services, and attractions available on shore in Alaskan communities. Cruise ships and ferries dock in Alaska ports, purchase goods and services from local vendors, and cruise ships sell on-shore tours and other services to disembarking passengers. Other state taxes involving vessels have easily met this prong of the Complete Auto test by virtue of less extensive contacts with shore. *See* Siong v. State, Department of Revenue, 622 P.2d 967, 970-971 (Alaska 1981); Hartley Marine v. Mierke, 474 S.E.2d 599, 608-609 (W. Va. 1996).

The second prong, requiring a fair relationship to benefits provided by the state to the taxpayer, is also easily met. This relationship need not be especially close. According to the United States Supreme Court,

> If the event is taxable, the proceeds from the tax may ordinarily be used for purposes unrelated to the taxable event. ... The bus terminal may not catch fire during the sale, and no robbery may be foiled while the buyer is getting his ticket, but police and fire protection, along with the usual and usually forgotten advantages conferred by the State's maintenance of a civilized society, are justifications enough for the imposition of a tax.

Oklahoma Tax Commission v. Jefferson Lines, 514 U.S. at 199-200 (upholding an Oklahoma sales tax on the full price of bus tickets, including tickets for travel between states).[v] *See also* Hartley Marine v. Mierke, 474 S.E.2d at 610 ("There simply is no requirement that the tax imposed result in a direct and attributable benefit to a taxpayer.")

[iv] Although this is an older case, the four-part test it describes is still good law. *See for example* Oklahoma Tax Commission v. Jefferson Lines, Inc., 514 U.S. 175, 183 (1995). Sometimes courts first analyze whether a law treats in-state and out-of-state interest differently, and then moves to the Complete Auto test. *See* Barber v. Hawaii, 42 F.3d 1185, 1194 (9th Cir. 1994); Hartley Marina Corporation v. Mierke, 474 S.E.2d 599, 607 (W.Va. 1996).

[v] Similarly, to satisfy the requirements of due process, the relationship does not have to be particularly close—"[a]s long as the services are available, the issue of usage by the taxpayers is irrelevant." Keane v. Local Boundary Commission, 893 P.2d 1239, 1248 (Alaska 1995).

Cruise ships and disembarking ferry and cruise ship passengers use many services provided by state and local government. For purposes of the commerce clause, it is not necessary that each vessel or passenger actually need or use each service in order to justify the tax.

The apportionment prong of the Complete Auto test is intended to ensure that "each State taxes only its fair share of an interstate transaction." *Id.* at 184, *quoting* Goldberg v. Sweet, 488 U.S. 252 (1989). Although there may be some question about how to apportion nights spent in transit between Canada and Alaska, assuming there is an equivalent Canadian bed tax, there should be no apportionment problem if the tax is calculated based on nights spent on Alaska waters.

The final commerce clause test element is whether the tax discriminates against interstate commerce. This prong of the Complete Auto test, according to the Alaska Supreme Court, means that a state cannot impose a tax which discriminates against interstate commerce by providing a direct commercial advantage to local businesses relative to interstate business. Sjong v. Department of Revenue, 622 P.2d 967, 973 (Alaska 1981). The coverage of the proposed tax (which does not affect non-commercial vessels, or vessels with fewer than 50 berths) is very similar to that of Juneau's cruise ship head tax ordinance. John Corso, the City Attorney for the City and Borough, has expressed concern that the cruise industry will challenge the city's ordinance based on this prong of the Complete Auto test. Memo from John R. Corso to the Mayor and Assembly, dated July 22, 1999. Mr. Corso opined that the Juneau head tax "would have a much better chance of surviving a discrimination claim" without those exemptions. *Id*, page 4. That point is worth considering in regards to the proposed tax.

The Tonnage Clause

The tonnage clause is a relative of the commerce clause; it too is concerned with ensuring the free flow of commerce between states. It prohibits a state from laying "any Duty of Tonnage" without the consent of Congress. The term "tonnage" originally referred to the internal capacity of a vessel. Clyde Mallory Lines v. Alabama ex rel State Docks, 296 U.S. 261, 265 (1935). However, the clause has been interpreted more expansively to include "all taxes and duties regardless of their name or form, and even though not measured by the tonnage of the vessel, which operate to impose a charge for the privilege of entering, trading in, or lying in a port." *Id.* The clause prohibits "reliance on tonnage duties to raise general revenues, to regulate trade, or to charge for the privilege of entering, lying in, or trading in a port." New Orleans S.S. v. Plaquemines Port, Harbor and Terminal District, 874 F.2d 1018, 1023 (5th Cir. 1989).

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The first question to ask in a tonnage clause analysis is whether the tax in question fits into the tonnage clause framework--whether it might reasonably be construed as a charge for the privilege of entering, trading in, or lying in a port.

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> Appellants urge this Court to view the use tax at issue as a charge for navigation of the rivers in violation of the Duty of Tonnage Clause. If this use tax were solely imposed for fuel consumption on the waters of this state, Appellants' arguments would be more convincing. The use tax at issue, however, is not a prohibited toll on the use of this state's navigable waterways, but an excise tax on the use of fuel which is imposed on all motor carriers operating within this state, including, buses, trucks, trains, and aircraft.

Id. at 612. Because the tax did not fall exclusively on users of the state's waterways, the court did not see it as a tonnage tax.

The tax imposed in CSSB 308(FIN) is distinguishable from the tax in the West Virginia case, however, because it affects commercial passenger vessels exclusively (not vessels and buses and aircraft, like the West Virginia tax). That makes it more likely that a court will entertain a tonnage clause argument.

Hawaii imposes fees for anchoring and mooring in state harbors. In Barber v. Hawaii, 42 F.3d 1185 (9th Cir. 1994), the plaintiffs argued that mooring and anchorage fees collected by the state were a duty on tonnage that violated the federal tonnage clause. The plaintiffs conceded that under the Clyde Mallory case, a state was permitted to charge reasonable fees for services rendered. They apparently also conceded that provision of restroom facilities, parking, trash disposal and security services would be sufficient to satisfy the requirements of the Clyde Mallory case. The plaintiffs then tried to argue that because the services provided were open to the public and not provided specifically for those paying the fees, that the state was effectively not providing those services. The court rejected this argument finding that Hawaii in fact provided services in exchange for the mooring and anchorage fees, and that the fees were not a duty on tonnage. Barber v. Hawaii, 42 F.3d at 1196.

The plaintiffs in Barber v. Hawaii apparently did not argue the tonnage clause issue very well, and the court's discussion of the clause is cursory. However, the case upheld the fees in question. In contrast, a recent Rhode Island case held that a registration fee on all boats operated in Rhode Island waters for more than 90 days was an unconstitutional tonnage tax, because the revenues from the fee would not necessarily be used for services benefitting boaters. State v. Turnbaugh, 705 A.2d 530 (R.I. 1997).

The Rhode Island statute provided that the proceeds from the registration fee, *subject to approval of the General Assembly*, should be allocated to fund expenses of the department of environmental management, harbor maintenance, boating safety and other boating related programs. *Id.* at 532. The court wrote:

> [I]t should be noted that any funds collected under the provisions of this chapter were required to be allocated, distributed, and used subject to the approval of the General Assembly. Thus this alleged restricted receipt account was entirely subject to being used as a general-revenue measure and not merely for the purpose of providing services to boats, boaters, and navigational improvements.

The court rejected the state's argument that the registration fee was merely a property tax, and instead concluded that it was "a classic form of tonnage tax specifically prohibited by the Constitution of the United States." *Id.* at 533.

Unlike the Ninth Circuit case cited above, the Rhode Island case would not be binding precedent on a federal district court in Alaska. Neither the Ninth Circuit case nor the Rhode Island case would be binding on an Alaska state court, but a state court might regard such authorities as persuasive. The Rhode Island decision certainly demonstrates that the tonnage clause is not a dead letter, and in light of the Rhode Island decision, caution would certainly be in order in imposing any fee or tax on exclusively on vessels, unless the proceeds were used to provide services to vessels. A bed tax that was imposed on beds on land as well as beds in ships would probably avoid tonnage clause problems.

Other Potential Constitutional Issues

There are a number of other constitutional provisions frequently used to challenge tax statutes which might be raised in an attack on the proposed tax.

If a tax can survive scrutiny under the second prong of the Complete Auto test and is at least minimally rational, it can probably survive a due process challenge as well. *See* Keane v. Local Boundary Commission, 893 P.2d 1239, 1248 (Alaska 1995) ("As long as services are available, the issue of usage by the taxpayer is irrelevant."); Katmailand, Inc. v. Lake and Peninsula Borough, 904 P.2d 397, 402 (Alaska 1995).

Equal protection is another potential issue. Alaska uses a sliding scale equal protection test, but the interests involved in taxation fall at the low end of the scale and are reviewed under "relaxed scrutiny." *Id.* at 401, n. 6. The federal equal protection clause requires only that the tax be "rationally related to a legitimate governmental interest." *Id.* at 401. As the Alaska Supreme Court observed, "[t]axes are rarely found to be without a rational basis." *Id.* at 400.

Other potential arguments might be based on the foreign commerce clause or the privileges and immunities clause of the federal constitution.

Conclusion

Putting a cruise ship head tax in HB 3002 would raise serious single subject questions. In addition, a tax like that in CSSB 308(FIN) might encounter challenges based on several provisions of the United States constitution, particularly the commerce clause and tonnage clauses.

PF:pl
00-180.plm

FISCAL NOTE

STATE OF ALASKA
2007 LEGISLATIVE SESSION

Fiscal Note Number: HB222-COM-DCA-04-02-07
Bill Version: HB 222
() Publish Date:

Revision Date/Time (Note if correction):
Dept. Affected: Commerce
Title: Passenger Vessel Tax Credit
RDU: Community Assist & Ec Dev (405)
Component: Community Advocacy
Sponsor: Ramras
Requester: House Community & Regional Affairs
Component No.: 2703

Expenditures/Revenues (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

OPERATING EXPENDITURES	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
Personal Services						
Travel						
Contractual						
Supplies						
Equipment						
Land & Structures						
Grants & Claims						
Miscellaneous						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0
CAPITAL EXPENDITURES						
CHANGE IN REVENUES ( )						

FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other (Specify Type--Do not abbreviate)						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY2007) cost: 0.0
Mark this box (X) if funding for this bill is included in the Governor's FY 2008 budget proposal:

POSITIONS

Full-time						
Part-time						
Temporary						

ANALYSIS: *(Attach a separate page if necessary)*

This legislation provides that a passenger liable for the tax under AS 43.52.220 would be entitled to a credit against the tax equal to the total amount of the passenger tax paid to one or more of the first five municipalities that are ports of call for the vessel on which the passenger is traveling. The credit is equal to the amount paid. This provision retroactively takes effect on December 17, 2006.

This legislation would have no fiscal impact on the division, nor would it financially impact the first five municipalities that are ports of call. They would still collect their local tax from the passenger.

Prepared by: Mike Black, Director
Phone 907.269.4535
Division: Community Advocacy
Date/Time 4/2/07 3:25 PM
Approved by: Emil Notti, Commissioner
Date 4/2/2007
Agency: Commerce, Community, and Economic Development

FISCAL NOTE

STATE OF ALASKA
2007 LEGISLATIVE SESSION

Fiscal Note Number: HB222-DOR-TAX-4-2-07
Bill Version: HB 222
() Publish Date:

Revision Date/Time (Note if correction):
Dept. Affected: Revenue 04
Title: Passenger Vessel Tax Credit
RDU: Taxation and Treasury
Sponsor: Representative Ramras
Component: Tax Division
Requester: House Community and Regional Affairs
Component No.: 2476

Expenditures/Revenues (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

OPERATING EXPENDITURES	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
Personal Services						
Travel						
Contractual						
Supplies						
Equipment						
Land & Structures						
Grants & Claims						
Miscellaneous						
TOTAL OPERATING	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
CAPITAL EXPENDITURES						
CHANGE IN REVENUES ( )	*	*	*	*	*	*

FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other (Specify Type--Do not abbreviate)						
TOTAL	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**

Estimate of any current year (FY2007) cost: 0.0
Check this box (X) If funding for this bill is included in the Governor's FY 2008 budget proposal:

POSITIONS

Full-time						
Part-time						
Temporary						

ANALYSIS: *(Attach a separate page if necessary)*

*See attached.

Prepared by: Johanna Bales and Nels Tomlinson
Phone (907) 269-6628
Division: Tax
Date/Time: 2 April 2007/12:00
Approved by: Jerry Burnett
Date: 2 April 2007
Agency: Dept. of Revenue

FISCAL NOTE

STATE OF ALASKA **BILL NO.** HB 222
2007 LEGISLATIVE SESSION

ANALYSIS CONTINUATION

Bill Language: This bill would grant commercial vessel passengers who are liable for the $46 tax under AS 43.52.220 a tax credit equal to any passenger taxes they may pay in any of their first five ports of call.

Revenues: Since Juneau and Ketchikan currently have a $5 and a $7 tax on commercial vessel passengers, respectively, this bill will cost the state at least $12 per passenger. Since the cruise industry projects approximately one million passengers for the 2007 cruise season, we anticipate that this will cost the state approximately $12 million in fiscal year 2008.

One effect of this bill will be to remove the current dis-incentive for communities to tax cruise passengers. Each community will have the option to tax passengers, and that tax will effectively be paid by the state rather than by the passenger, up to a total of $46 for all communities. Therefore, we anticipate that by the next cruise season, more communities will have imposed passenger taxes which take advantage of the credit. These hypothetical local taxes will be higher than the $5 which the ports of call could get from the state. Therefore, it is possible that this measure could eventually erode essentially all of the state's revenues from the commercial passenger vessel tax.

The current law calls for the state to share $5 per passenger with each of the first five ports of call which do not charge their own tax. The state is also called to share 25% of the money collected with regions which are impacted by the cruise industry. Funds for impacted regions could potentially be reduced to nothing by this bill.

Expenditures: It is not anticipated that this bill will result in any additional expenditures for the Department of Revenue.

LEGAL SERVICES

DIVISION OF LEGAL AND RESEARCH SERVICES
LEGISLATIVE AFFAIRS AGENCY
STATE OF ALASKA

(907) 465-3867 or 465-2450
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State Capitol
Juneau, Alaska 99801-1182
Deliveries to: 129 6th St., Rm. 329

MEMORANDUM January 26, 2007

SUBJECT: 33 U.S.C. 5(b) and appropriations (Work Order No. 25-LS0451)

TO: Representative Mike Hawker
Attn: Juli Lucky

FROM: Donald M. Bullock Jr.
Legislative Counsel

You asked whether appropriations from revenue received from the cruise ship passenger tax in AS 43.52.200 - 43.52.295 must be used for an appropriate purpose only in an area in which the passenger vessel operates to avoid conflict with 33 U.S.C. 5(b).[1]

The short answer is that the use of money from the tax in an area in which the vessel carrying taxable passengers does not operate may be disallowed under 33 U.S.C. 5(b) unless the money is used "solely to pay the cost of a service to the vessel or water craft."

State-imposed taxes related to the operation of vessels or other water craft are generally prohibited under 33 U.S.C. 5(b),[2] with limited exceptions. That subsection of the United States Code reads as follows:

> (b) No taxes, tolls, operating charges, fees, or any other impositions whatever shall be levied upon or collected from any vessel or other water craft, or from its passengers or crew, by any non-Federal interest, if the vessel or water craft is operating on any navigable waters subject to the authority of the United States, or under the right to freedom of navigation on those waters, except for--
>
> (1) fees charged under section 208 of the Water Resources Development Act of 1986 (*33 U.S.C. 2236*);
>
> (2) reasonable fees charged on a fair and equitable basis that--

---

[1] I provided you with a general discussion of the limitations on the use of revenues derived from the cruise ship passenger tax in a memo dated Jan. 23, 2007, under Work Order No. 25-LS0431.

[2] 33 U.S.C. 5(b) was enacted in 2002 and amended in 2003. P.L. 107-295, Title IV, § 445, 116 Stat. 2133 (2002); P.L. 108-176, Title VIII, § 829(a), 117 Stat. 2597 (2003).

> (A) are used solely to pay the cost of a service to the vessel or water craft;
>
> (B) enhance the safety and efficiency of interstate and foreign commerce; ***and***
>
> (C) do not impose more than a small burden on interstate or foreign commerce; ***or***
>
> (3) property taxes on vessels or watercraft, other than vessels or watercraft that are primarily engaged in foreign commerce if those taxes are permissible under the United States Constitution. [Emphasis added.]

Note the emphasized words "and" and "or" in the excerpt above. The word "or" in 33 U.S.C. 5(b)(2)(C) means that any one or more of the three options in 33 U.S.C. 5(b)(1) - (3) qualifies as an exception to the general prohibition on state[3] " taxes, tolls, operating charges, fees, or any other impositions." On the other hand, the word "and" that is emphasized in the excerpt at the end of subparagraph (2)(B) implies that the state's use of "reasonable fees" must meet all three criteria under paragraph (b)(2).

The use of the words "and" and "or" and the problems of possible ambiguity are discussed in Dickerson, *The Fundamentals of Legal Drafting*, 2d ed. (1986), sec. 6.2, pp. 104 - 14. The introduction to the discussion in Dickerson is as follows:

> Problems of multiple modifications or reference are perhaps best approached through the peculiar uncertainties involved in the use of "and" and "or." The difference between "and" and "or" is usually explained by saying that "and" stands for the conjunctive, connective, or additive and "or" for the disjunctive or alternative. The former connotes "togetherness" and the latter tells you to "take your pick." So much is clear.

Dickerson at 104.[4]

In other words, if the fees were used to enhance the safety and efficiency of interstate and foreign commerce and do not impose more than a small burden on interstate or foreign commerce, but are not used to pay the cost of service to the passenger vessel linked to the fee, the fee would be prohibited under this section. To qualify as an exception under paragraph (b)(2) to the general prohibition in subsection (b), the purpose of the appropriation must meet all three criteria; an appropriation for expenditure in an area in which the vessel does not operate would fail to qualify unless the money is somehow used "solely to pay the cost of service" to the passenger vessel.

---

[3] The state is a "non-federal interest" and is therefore subject to the general prohibition and limited exceptions in 33 U.S.C. 5(b).

[4] Dickerson is referenced numerous times in the *Manual of Legislative Drafting* (2005). See, e.g. pages 60, 68, and 72.

In closing, and with reference to the memorandum to you dated January 23, 2007 that also discussed 33 U.S.C. 5(b), note that a "fee" and a "tax" may not be the same thing for the purposes of that subsection. The terms "taxes" and "fees" are listed separately in the first sentence in the subsection, "fees" are referred to in subparagraphs (1) and (2), and "taxes" are referred to subparagraph (3). There is a possibility that a court may not consider the state's "tax" at a rate of "$46 a passenger per voyage" a "fee" when interpreting 33 U.S.C. 5(b)(1) and (2), in which case an exception under those paragraphs would not apply. I cannot predict whether a distinction may be made between the two, but wanted to point this possibility out to you.

If I may be of further assistance, please let me know.

DMB:ljw
07-030.ljw

HB 222 - Summary of Legal Opinions

The Initiative's $46.00 passenger head tax violates federal law in at least three ways:

First, it violates 33 U.S.C. § 5, which prohibits taxes or fees on vessels operating in navigable waters, or their passengers, except in narrowly tailored circumstances that enhance the "safety and efficiency" of interstate commerce. The passenger tax imposed by the Initiative does not come close to satisfying the test for a proper fee under 33 U.S.C. § 5.

To summarize Donald Bullock's, January 26, 2007 memorandum to Representative Mike Hawker. The use of money from the tax in an area in which the vessel carrying taxable passengers does not operate may be disallowed under 33 U.S.C. 5(b) unless the money is used "solely to pay the cost of a service to the vessel or watercraft."

State-imposed taxes related to the operation of vessels or other water craft are generally prohibited under 33 U.S.C.(b)(2), with limited exceptions. These exceptions in subsection (b)(2)read as follows:

> (2) reasonable fees charged on a fair and equitable basis that—
>
> (A) are used solely to pay the cost of a service to the vessel or water craft;
>
> (B) enhance the safety and efficiency of interstate and foreign commerce; ***and***
>
> (C) do not impose more than a small burden on interstate or foreign commerce.

By using the word ***and*** the statutory meaning is conjunctive, connective, or additive, meaning that all three premises must apply for this exception to apply. Therefore, to qualify as an exemption under paragraph (b)(2) to the general prohibition in subsection (b), the purpose of the appropriation must meet all three criteria.

The opinion concludes by stating, There is a possibility that a court may not consider the state "tax" at a rate of "$46 a passenger per voyage" a "fee" when interpreting 33 U.S.C. 5(b)(1) and (2), in which case an exception under those paragraphs would not apply.

Second, it violates the Tonnage Clause of the United States Constitution, which the Supreme Court has interpreted to prohibit any taxes or fees on vessels in interstate commerce except those directly related to services provided to those

vessels. Here, the tax operates not as a user fee but as a revenue generating device, which is clearly prohibited under the Tonnage Clause.

Under the Tonnage Clause of the U.S. Constitution, Article 1, Section 10, which provides, "No state shall, without the Consent of Congress, lay any Duty of Tonnage..." The tonnage clause prohibits charges "for the privilege of entering, trading in, or lying in a port," but permits charges "for services rendered to and enjoyed by the vessel, such as pilotage, wharfage, or charges for the use of locks on a navigable river, or fees for medical inspection." *Clyde Mallory Lines v. State of Alabama,* 296 U.S. 261 (1935). However, the prohibition against tonnage duties does not extend to charges made by state authority for services rendered to and enjoyed by the vessel. *See* Attorney General, Gregg Renkes' letter to Representative Cheryll Heinze, dated May 16, 2003.

Furthermore, Kathryn Kurtz wrote in her February 16, 2004 legal opinion to Representative Carl Gatto, "Other services included on the list, such as state parks and the Alaska Railroad, appear to have a much more attenuated relationship to the vessels that may not be sufficient to bring them under the rubric of 'services to vessels' for purposes of the Tonnage Clause."

Third, it violates the Commerce Clause under Article 1, Section 8 of the United States Constitution. The tax fails the "internal consistency" test, which asks whether interstate commerce would be unduly burdened if every state imposed a similar tax, as well as the requirement that the tax be fairly related to the services provided by the state.

For the reasons stated above, it is our belief that the Initiative's $46.00 passenger head tax violates federal law and that funds collected under the "Regional Cruise Ship Impact Fund" can only be distributed to municipalities that actually are ports of call to the cruise ship industry and not throughout the State of Alaska as the Initiative language implied.

TO: H Community & Regional Affairs Committee
FR: Chip Thoma, Juneau, Cruise Initiative Law Supporter
RE: HB 222, Taxation of Cruise Lines Issues
DATE: April 17, 2007

I apologize for not being present this morning, but I have jury duty.

Importantly, I submitted written testimony April 3 on HB 222 with attached legal opinions from Juneau City & Borough attorneys Corso & Hartle. The opinions demonstrate how Juneau has correctly applied the new federal law to spend its cruise passenger fees. The fees have benefited the cruise lines, their passengers and the local community through improved capital infrastructure and CBJ services.

The present cruise tax law specifically benefits ALL parties and treats port communities equally, but prohibits communities from "double-dipping"; charging a local tax and participating in the state revenue sharing program. This allows future cruise ports capital funds for infrastructure without draining the new cruise fund, and allows existing ports with private docks to also apply for state appropriations from that cruise fund. Some examples of ports with private docks are Skagway, Hoonah, and Whittier.

Present and future ports that could well benefit from existing cruise law are Sitka, Cordova, Valdez, Kodiak and Unalaska. I urge you to reject HB 222, and to hold interim hearings this summer in some of these smaller communities. The Committee can then determine the true fiscal impact of cruise ships, and a fair state taxing regime that benefits all Alaska port communities. Thank you for your balanced consideration of these important policy and tax matters. CT

TO: H Community & Regional Affairs Committee 4-17-07

Attached is the Primary Election Voter Pamphlet which was sent to all state voters in early August, 2006.

The Voter Pamphlet was very clear about the uses of the new passenger fee fund, stating that "towns that receive that money cannot impose local cruise ship head taxes." Page 12, Leg. Affairs Summary.

Page 13 of the Pamphlet has a long section on the use of revenues, the establishment of "Impact Funds", and the estimated level of revenues generated for the state of Alaska.

Page 14 contains the initiative language on the disposition of receipts from the passenger tax, including allowed uses, determining the ports-of-call and the status of impact funds.

On Page 19, the statement in support describes the uses of passenger fees and states,"Communities preferring their own tax program can opt-out of the new state program."

Finally, Page 20, the opposition statement, does not discuss the taxing regime at all, though there was full opportunity to do so. I note that Mayor Weinstein of Ketchikan is listed on the opposition page as endorsing that letter, again, without any discussion of taxation.

I hope this Alaska Voter Pamphlet is instructive to the Committee that full and adequate notice was given, and that local and state taxation was thoroughly discussed, except by initiative opponents.

Thank you for considering this information. Chip Thoma, Juneau

City of Seward
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Main Office (907) 224-4050
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City of Seward, Alaska
1963 1965 2005
All-America City

Hon Anna Fairclough
Co-Chairperson
House Community and Regional Affairs

Hon Gabrielle Ledoux
Co-Chairperson
House Community and Regional Affairs

Honorable Chairpersons

The City of Seward would like to go record in support of the intent of HB 222 and what we understand to be a forthcoming proposed amendment from the sponsor Rep Ramras.

It is our understanding that under federal law revenue from head taxes and fees can only be used to "service the vessel" much like fees charged to aircraft passengers can only be used to "service the aircraft" at airport facilities.

It follows then that these funds can only legally be spent at ports of call where cruise ships actually visit.

The concepts proposed by HB222 go a long way to make the Cruise initiative passed by the voters much more effective in getting the revenues to the port cities where the "vessel servicing" costs actually are.

In addition the bill structures things so that a predictable and stable revenue flow makes financing of significant qualitative improvement to port facilities a possibility.

Thank you for the opportunity to comment.

Sincerely,
Vanta Shafer
Mayor

SOUTHEAST CONFERENCE

Working for strong economies, healthy communities, and a quality environment in Southeast Alaska

April 6, 2007

222

Representative Jay Ramras
State of Alaska
State Capitol, Room 118
Juneau, AK 99801-1182

RE: Southeast Conference Comments on HB 222

Representative Ramras,

Southeast Conference is a regional, nonprofit corporation that advances the collective interests of the people, communities and businesses in Southeast Alaska. Members include municipalities, Native corporations and village councils, regional and local businesses, civic organizations and individuals from throughout the region. The mission of Southeast Conference is to undertake and support activities that promote strong economies, healthy communities, and a quality environment in Southeast Alaska. After deliberation and recommendations by the Southeast Conference Tourism Committee, Southeast Conference offers the following comments.

The initiative passed last year provides for a marine passenger fee of $50 per passenger to be imposed upon all passengers of large cruise ships calling at ports in the State. The current arbitrary $5 limit per port, for up to five ports, as written in the initiative will, based on the real ship schedules: direct an average of only $18 of the $50 to the communities that are directly impacted by the cruise ships. This is because the average cruise ship stops at 3.5 ports. In our opinion, this is not enough money to meet needs in directly affected communities.

In the present formula, **none** of the state fee goes to the municipalities that have port fees equal to or greater than $5. This further reduces the amount above and it puts ports with local port fees at a big competitive disadvantage against ports without such fees because the port fee is now on top of the $50 tax per person.

We believe that without amendment the formula contemplated by the initiative may not comply with federal law. In 2002 Congress passed Section 445 of the Maritime Transportation Security Act, which essentially requires a connection between the fee, and a service to the vessel, passengers, and/or crew. The present formula does not appear to comply with that requirement.

We believe that HB 222 will encourage the cruise lines to work with each port community to develop a plan to provide improvements to port and related facilities, and set a fee at an appropriate level to do so. This should result in a much more productive relationship between cruise lines and their host communities.

P.O. Box 21989 Juneau, Alaska 99802-1989 Tel. (907) 463-3445 FAX (907) 463-5670
An Alaska Regional Development Organization
USDA - NRCS Resource Conservation & Development Council

Furthermore, we believe that HB 222 helps assure that marine passenger fees flow to local communities so that those being impacted the most by the cruise ships can improve their port infrastructure and compete on the world market with ports around the world that are making significant investments.

Finally, we believe that HB 222 is consistent with the initiative, as $50 would still be assessed against each passenger on cruise vessels entering Alaska waters, and with federal law, as the fees collected would be spent on services reasonably related to the vessels, their passengers, and their crews.

Southeast Conference urges you and your colleagues to pass HB 222 this session.

Sincerely,

Carol Rushmore

Carol Rushmore
President

Cc: House of Representative Members ✓

TO: House Community & Regional Affairs Committee

FR: Chip Thoma, Juneau, Cruise Initiative Supporter

RE: HB 222 Written Testimony & Legal Opinions

DATE: April 3, 2007

Here is my submitted written testimony from the hearing today in your committee on HB 222, the Cruise Tax Credit.

I have also attached two legal opinions that explain the application and use of passenger fees in Alaska, as defined by federal law.
I hope these opinions and my testimony help you in deciding to reject HB 222 as an unnecessary repeal of the 2006 Cruise Initiative.

Thank you for considering this information.

TO: House Community and Regional Affairs Committee
FR: Chip Thoma, Juneau, Cruise Initiative Supporter
RE: HB 222, Cruise Tax Credit
DATE: April 3, 2007

HB 222 would have a negative impact on the finances of the State of Alaska. Importantly, the bill would not help municipalities cope with hosting the 1 million cruise passengers coming to Alaska each year in a compressed, 5 month season, May through September.

The proposed 'credit' that a cruise passenger would receive under HB 222 will never benefit that actual passenger. In reality, this is a tax rebate program that returns new state revenues directly to the cruise companies in Miami. For that reason alone, I oppose HB 222.

Also, HB 222 is not good public policy. It will again encourage competition between port towns to curry industry favor on ship taxes, rather than making sound, community-based decisions on long-term improvements to waterfronts. Local waterfront activities are the heart and soul of each town, and those uses and improvements should be made without undue cruise influence over summer taxes. The initiative ends the practice of comparing and selecting communities based on the local tax climate.

Instead, the cruise initiative is an opt-in, revenue-sharing program of choice for local municipalities. In the years ahead, there could be smaller cruise ports in the state that will benefit, such as Cordova, Valdez and Kodiak, because the cruise demand and market are certainly there. Other cruise ports that also benefit from the initiative are those that now have private cruise docks, such as Skagway and Whittier.

In these latter two ports, dock owners charge ships a private passenger fee for using their property. The new state fees would allow cruise ports without local head taxes to make extensive improvements to their adjacent city docks and harbor lands used by cruise passengers when they visit. This is a plus for all cruise ports.

As the initiative was written, each community has the choice when to opt-in or opt-out. They can choose to have the state collect and

distribute the cruise taxes, or charge and bond for municipal cruise docks and improvements with local passenger fees, such as Ketchikan and Juneau do.

Juneau is the best example of a port community that has defined the uses and parameters of the cruise passenger fee, as those relate to the 2002 Maritime Security Act. That federal law says that reasonable passenger fees can be spent on cruise docks and adjacent access areas for the safe and efficient movement of passengers and cargo. I refer you to the opinions issued by Juneau Borough attorney Corso in 2003 and by Juneau Borough attorney Hartle in 2005 (attached).

To paraphrase Abraham Lincoln, you can't fool all the people all of the time. 81,000 Alaskans voted correctly on the cruise initiative. They knew what they were voting for:

- Clean cruise ships, verified clean by Ocean Rangers;
- Fair state taxes spent on cruise infrastructure;
- Consumer protection for cruise passengers; and a
- Level playing field for Alaska businesses that want summer cruise customers.

The cruise lines in Alaska are a multi-billion dollar industry that overwhelms coastal towns throughout Alaska each summer. It is time that the state had a fair tax regime that provides new funds for the huge cruise infrastructure costs needed in the years ahead.

In my estimation, the simplest and most courageous action by an Alaska Governor was taken by Jay Hammond, defining the ground rules for doing business in Alaska:

- Industry pays its own way, without subsidy;
- Industry does not pollute; and,
- All industries pay a fair share in state taxes.

That's why it is deeply offensive that a multi-billion dollar industry that is loosely regulated and poorly controlled sends delegations of folks from Miami to Alaska to repeal state law, as just enacted by state voters. The ink was not even dry on the initiative results before an all-out repeal effort has transpired on every section of the 2006 initiative. Please reject HB 222 as a repeal of the cruise initiative. Thank you.

CBJ Law Department
MEMORANDUM

To: Assembly Finance Committee

From: John R. Corso, City & Borough Attorney

Subject: Port Fees; federal law

Date: April 21, 2003

I. Discussion

Last week, KTOO broadcast a story about the Murkowski administration reaction to recent changes in federal maritime law. The law in question is the Maritime Security Act of 2002, which, among other changes, amended 33 USC §5 to provide:

> (b) No taxes, tolls, operating charges, fees, or any other impositions whatever shall be levied upon or collected from any vessel or other water craft, or from its passengers or crew, by any non-Federal interest, if the vessel or water craft is operating on any navigable waters subject to the authority of the United States, or under the right to freedom of navigation on those waters, except for–
>
> (1) fees charged under section 208 of the Water Resources Development Act of 1986 (33 U.S.C. 2236); or
>
> (2) reasonable fees charged on a fair and equitable basis that--
>
> (A) are used solely to pay the cost of a service to the vessel or water craft;
>
> (B) enhance the safety and efficiency of interstate and foreign commerce; and
>
> (C) do not impose more than a small burden on interstate or foreign commerce.

The reference in (b)(1) is to a long-established program for harbor project fee review by the Federal Maritime Commission. The Port Director administers this program for CBJ. I have attached copies of the new language and the referenced FMC statute.

The new statutory language essentially restates the constitutional rule described in my July 22, 1999 memorandum to the Assembly on the passenger fee initiative. Briefly, the rule is that we ca. impose a fee on visitors only to the extent we provide a service to visitors. We cannot charge them a fee for services we provide to someone else, such as ourselves.

Some services, such as dock construction and maintenance, are clearly justifiable as a service to ships and passengers. Others are less defensible. The statute will prevent the most flagrant abuses, such as a fee imposed on ships that merely pass through local waters without stopping. So said Congressman Young in the November 22, 2001 *Congressional Record*, attached. However, it can be used in less egregious circumstances as well. Mr. Young speculated that "generally taxes will not be allowed under this section". *Id.*

Even though the statute does not break any new legal ground, it does provide a reasonably clear and concise statement of the law. In this respect, it is more usable, (both for us and for plaintiffs) than a fuzzy principle extracted from constitutional text and a few judicial cases; which is all we had to work with before the statute.

Also, the statute adds some new emphasis to the constitutional rule. The new language says that fees must be use "solely" to provide a service to the vessel, must "enhance the safety and efficiency" of interstate and foreign commerce, and must impose only a "small" burden on that commerce. We must await judicial interpretation to learn exactly what these qualifiers mean, but they certainly do not make things easier for local port fees.

According to the KTOO story, the Murkowski administration has concluded that the new law prohibits passenger fees. I'm not sure that the Attorney General shares this view: informal contact with his staff suggests that they see it pretty much as I do.

II. Conclusion:

For the most part, the new statute just restates existing constitutional law. It makes no fundamental changes and does not invalidate our port or passenger fees.

However, it will serve to focus attention on how we use the fee revenue. Also, the statutory language is slightly more stringent than the constitutional rule it supplements. As a result, we should take extra care to spend passenger fee revenues on programs (or parts of programs) that benefit only the people who pay the fee. We may not balance our budget by taxing people who cannot vote.

CBJ Law Department
MEMORANDUM

To: Mayor and Assembly

From: John W Hartle, City Attorney JWH

Subject: Fees on Cruise Lines; Resolution 2294b.

Date: March 12, 2005

You have asked for an analysis of the objections raised by Jim Reeves of Dorsey and Whitney regarding the proposed increases in cruise line fees in Resolution 2294b. I have analyzed all the cases cited by Mr. Reeves, and the other major case law as well. The short answer is that, while there is always some risk regarding particular expenditures, and federal law does provide special protection to interstate and foreign shipping, it appears that the present proposal would pass muster under the U.S. Constitution because the proposal is a fee for services and facilities that benefit the cruise industry, rather than a tax to raise general revenues.

The Tonnage Clause.

The Tonnage Clause of the U.S. Constitution gives the shipping industry a measure of special protection from state and local taxation. The clause provides: "No State shall, without the Consent of Congress, lay any Duty of Tonnage." U.S. Const. Art. I, § 10, cl. 3. It was added to the Constitution on September 15, 1787, according to the notes of James Madison, essentially as a supplement to the Commerce Clause, which also serves to limit state and local regulation or taxation of interstate or foreign commerce.

Under the Tonnage Clause, a municipality cannot levy a general tax on ships for the privilege of entering port; fees for services and facilities, however, can be imposed. There are many cases that make this point. Closest to home is the July, 2004, Superior Court decision in *Polar Tankers, Inc. v. City of Valdez*. Case No. 3AN-00-9665CI. In that case, the court struck down the City of Valdez's Ordinance 99-17 which imposed the "Tanker Tax," a business personal property tax levied mainly on oil tankers. Because the tax was imposed for the admitted purpose of raising general revenues, not based on a particular service or facility for the tankers, the court struck it down.

The fee increase proposed in Resolution 2294b, by contrast, is not intended as a general revenue measure. The resolution would impose fees for the purpose of constructing facilities outlined in the Long-Range Waterfront Plan that benefit the cruise industry. *See* Resolution 2294b, Sec. 2(e), pg 3, line 22. Courts have consistently found that state or local fees for services or facilities do not violate the Tonnage Clause. In 1877, the U.S. Supreme Court summarized the law as follows:

> To determine whether the charge prescribed by the ordinance in question is a duty of tonnage, within the meaning of the Constitution, it is necessary to observe carefully its object and essence. If the charge is clearly a duty, a tax, or burden, which in its essence is a contribution claimed for the privilege of entering the port of Keokuk, or remaining in it, or departing from it, imposed, as it is, by authority of the State, and measured by the capacity of the vessel, it is doubtless embraced by the constitutional prohibition of such a duty. *But a charge for services rendered or for conveniences provided is in no sense a tax or a duty.* It is not a hindrance or impediment to free navigation. *The prohibition to the State against the imposition of a duty of tonnage was designed to guard against local hindrances to trade and carriage by vessels, not to relieve them from liability to claims for assistance rendered and facilities furnished for trade and commerce.*

Keokuk Northern Line Packet Co. v. City of Keokuk, 95 U.S. 80, 84 -85 (1877) (emphasis added).

125 years later, courts are still saying the same thing:

> "[A] charge for services rendered or for conveniences provided is in no sense a tax or a duty. It is not a hindrance or impediment to free navigation."); see also *Barber v. Hawai'i*, 42 F.3d 1185, 1196 (9th Cir.1994) ("[A] state is not prohibited from charging reasonable fees in return for services rendered.")...For example, a harbor fee charged for the use of restroom facilities, parking, trash disposal, and security is not a "duty of tonnage" because services are provided in exchange for the fee. See *Barber*, 42 F.3d at 1196. Similarly, if fees are for pilotage, wharfage, use of locks on a navigable river, or for medical inspection, those fees are not unconstitutional duties of tonnage. *See Clyde Mallory*, 296 U.S. at 266, 56 S.Ct. 194.

Captain Andy's Sailing, Inc. v. Johns, 195 F.Supp.2d 1157, 1172 (D.Hawai'i 2001).

> A fee charged to ensure that emergency services are available is also not a duty of tonnage, even if not every ship paying the fee needs the service.

New Orleans Steamship Ass'n v. Plaquemines Port, Harbor & Terminal Dist., 874 F.2d 1018, 1023 (5th Cir.1989), cert. denied, 495 U.S. 932 (1990).

The Commerce Clause.

The Commerce Clause of the U.S. Constitution provides: "The Congress shall have power . . . To regulate commerce with foreign nations, and among the several states . . .." Allocating this authority over foreign and interstate commerce to Congress means that such authority is *not* allocated to states or municipalities; the negative sweep of the Commerce Clause precludes state or local regulation. There are many cases interpreting the Commerce Clause from the earliest days of the federal courts. In the context of shipping, however, the Commerce Clause is not as restrictive as the Tonnage Clause. If a fee or practice is allowed under the Tonnage Clause, the Commerce Clause is not likely to prohibit it.

The Maritime Transportation Security Act of 2002.

As a fairly recent enactment of Congress, this act has no body of developed case law interpreting it. However, from its plain language, it can be seen as the most restrictive of the three main areas of federal law restricting municipal fees on shipping interests. Although not mentioned in Mr. Reeves' memo regarding Resolution 2294b, the Maritime Security Act of 2002 provides his best argument. It provides:

> (b) No taxes, tolls, operating charges, fees, or any other impositions whatever shall be levied upon or collected from any vessel or other water craft, or from its passengers or crew, by any non-Federal interest, if the vessel or water craft is operating on any navigable waters subject to the authority of the United States, or under the right to freedom of navigation on those waters, except for
>
> (1) fees charged under section 2236 of this title;
> (2) reasonable fees charged on a fair and equitable basis that--
> (A) are used solely to pay the cost of a service to the vessel or water craft;
> (B) enhance the safety and efficiency of interstate and foreign commerce; and
> (C) do not impose more than a small burden on interstate or foreign commerce; or
> (3) property taxes on vessels or watercraft, other than vessels or watercraft that are primarily engaged in foreign commerce if those taxes are permissible under the United States Constitution.

This federal statute, among others, in my view comprises "the Consent of Congress" contemplated by the Tonnage Clause. Accordingly, if a project fits its requirements, it will pass muster under the Tonnage Clause and the Commerce Clause as well. This is the statute CBJ has been acting under since its enactment. Sponsored by Rep. Don Young, it was intended to clarify the requirements of the Commerce Clause, according to his address to Congress upon its passage:

> Section 445 [the Act] addresses the current problem, and the potential for greater future problems, of local jurisdictions seeking to impose taxes and fees on vessels merely transiting or making innocent passage through navigable waters subject to the authority of the United States that are adjacent to the taxing community. We are seeing instances in which local communities are seeking to impose taxes or fees on vessels even where the vessel is not calling on, or landing, in the local community. These are cases where no passengers are disembarking, in case of passenger vessels, or no cargo is being unloaded in the case of cargo vessels and where the vessels are not stopping for the purpose of receiving any other service offered by the port. In most instances, these types of taxes would not be allowed under the Commerce Clause of the United States Constitution. Unfortunately, without a statutory clarification, the only means to determine whether the burden is an impermissible burden under the Constitution is to pursue years of litigation. . .
>
> ..

Conference Report on S. 1214, Maritime Transportation Security Act of 2002; Speech of Hon. Don Young, of Alaska, in the House of Representatives, Thursday, November 14, 2002.
The requirements of this federal statute appear to be straight out of the case law, particularly, the Fifth Circuit's summary of the U.S. Supreme Court *Clyde Mallory* decision. *See Plaquimines*, 874 F.2d 1018, 1021(5th Cir. 1989). One additional issue raised is that of the requirement that any fee "not impose more than a small burden on interstate or foreign commerce . . .." All indications are that the cruise industry is financially healthy at this time, and that the proposed additional one dollar per passenger could be contractually passed on to the cruise consumer, and, therefore, would not impose more than a small burden on interstate or foreign commerce.

Conclusion.

Resolution 2294b would increase the Port Development Fee by one dollar per passenger. Because the resolution requires that all funds collected by the Port Development Fund be spent on projects outlined in the Long-Range Waterfront Plan that benefit the cruise industry, the fee increase would very likely survive a challenge based on the case law from the U.S. Supreme Court and the U.S. Court of Appeals for the Ninth Circuit. In my view, so long as CBJ continues its vigilance in following the requirements of federal law and close cooperation with the industry in making expenditures (as required by Resolution 2294b), a legal challenge would be unlikely to succeed.

TESTIMONY ON HOUSE BILL 222

Bruce M. Botelho, Mayor
City and Borough of Juneau

I testify today on behalf of the assembly of the City and Borough of Juneau in support of Committee Substitute for House Bill 222, legislation that would provide a credit for certain municipal passenger fees against the statewide excise passenger tax established by 2006 Primary Election Ballot Measure No. 2.

I support the purpose that the sponsors sought to achieve in promoting the passenger tax: having users contribute to the infrastructure necessary to serve them in communities they visit by cruise ship. However, I believe that there is a fundamental flaw in the initiative that frustrates this purpose and that the Committee Substitute for House Bill 222 corrects that flaw. That flaw is the creation of a vast pool of money that can not be expended constitutionally. Let me explain.

Let me begin by addressing how Measure No. 2 is designed to work.

First, it imposes a $46 tax on each passenger traveling in Alaska on a large commercial passenger vessel. The proceeds from the tax are placed in a special account within the general fund of the state. Each of the first five ports of call for each vessel's voyage within Alaska is entitled to receive $5 per passenger per port visit.

Second, the initiative also establishes a "regional cruise ship impact fund" consisting of 25 percent of the total proceeds from the passenger tax. Regional cruise ship impact funds may be appropriated for distribution to local governments within regions of the state "impacted by cruise ship related tourism activities but not entitled to receive funds based on port of call visitation."

Finally, the remainder of the funds may be appropriated for "state-owned port and harbor facilities" or certain other services.

There are specific restrictions on these taxes.

- If a municipal port elects to receive its $5 per passenger share of the state's passenger tax, it may not impose its own local passenger tax.
- Conversely, a municipality that imposes its own local passenger tax may not access either the $5 per passenger share nor regional impact funds.
- Expenditure of the monies is limited to "provide services and infrastructure directly related to passenger vessel or watercraft visits or to enhance the safety and efficiency of interstate and foreign commerce related to vessel or watercraft activities."

This is the statutory scheme in place. How does this relate to the "fundamental flaw" in it? What's wrong with the scheme? The problems are of two kinds: constitutional and practical.

What are the constitutional problems? Federal law limits the kinds of taxes or fees that may be imposed on vessels in interstate commerce. Let me mention the laws I believe most directly apply:

- The Tonnage Clause of the United States Constitution (art. I, sec. 10) prohibits any taxes or fees on vessels except those directly related to services provided to those vessels.

- 33 USC Section 5 prohibits authorizes the levy of "reasonable fees charged on a fair and equitable basis" that (A) are used *solely* to pay the cost of a service to the vessel; (B) enhance the safety and efficiency of interstate and foreign commerce; *and* (C) do not impose more than a small burden on interstate or foreign commerce.

The sponsors of the initiative were aware of these restrictions and have tried to meet the high burden set by federal law. That's why the funds generated by this tax must be used "in a manner calculated to improve port and harbor facilities and other services to properly provide for vessel or watercraft visits and to enhance the safety and efficiency of interstate and foreign commerce."

Yet this language is of little import when applied to the regional impact fund. That's because that fund is available only to those ports that are not today "ports of call", that is ports that are not visited by cruise ships at all. So, applying the federal statute, what conceivable service to a vessel should be recovered and on what basis? Similarly, what state-owned port, harbor facilities or other service is being directly rendered that would permit these funds to be expended? I suggest that few expenditures could meet the federal test.

What are the practical problems?

First, there is little incentive for major ports of call to take part in the state program, rather than maintain or establish their own passenger fees. Why is this?

(1) Municipalities are able tc set higher or lower fees to meet local infrastructure needs without reliance on the state program. Thus, Juneau currently imposes two separate fees computed on the number of a vessel's passengers per port visit. The two fees now total $8.00. Ketchikan currently imposes a $7.00 per passenger fee.

(2) Municipal ports electing to receive the $5 per passenger tax would be required to come to the legislature each year and seek an appropriation for that purpose. It leaves municipalities dependent upon the legislative process and having port monies traded for other capital projects. In addition, reliance on annual appropriations to bond for projects is difficult because local government would have no direct authority to impose and receive taxes related to the port to repay the bonded indebtedness.

Let me apply all of this to the initiative. For purposes of this exercise, I am assuming a year in which 1 million passengers arrive by cruise ship (slightly more than are actually projected for this season):

$46,000,000 total amount to be remitted to the State

The cruise ship industry estimates that the average cruise ship vessel calls on 3.5 ports in Alaska. I've rounded up to four ports. The two largest ports of call, Juneau and Ketchikan do not participate. I have also assumed that a million passengers visited each of the next two ports of call. That allows me to subtract - **$10,000,000** as the total amount remitted to municipalities.

That leaves a total of **$36,000,000**. Another 25% is to be allocated to the regional impact fund. Again, it is doubtful whether much, if any, of that amount can be expended, but that amount totals **$11,500,000**. That leaves a total of **$24,500,000** to be expended on **state** harbors, ports and services to be used **solely** in direct service to cruise ship vessels. I submit that you cannot spend it. In the meantime, of the **$46,000,000** theoretically set aside for support of local governments servicing cruise ship vessels, at most **$10,000,000** reaches them.

Thus we are left with a municipal port revenue sharing program that will not work as intended: as a way to assist port communities to cope with cruise ship visits.

Fortunately, this problem can be fixed. Proposed Committee Substitute for House Bill 222 is one such way. The CS would allow municipal passenger taxes or fees to be taken as a credit against the State's $46 tax, up to a maximum credit of $10 per passenger, per community.

Let there be no question. Under this bill, the allowance of a tax credit will reduce the amount of proceeds going into the State general fund. And the cruise industry will end up remitting fewer total dollars to government entities, local and state, as a result.

But creating a credit is likely to achieve a couple of other results that I believe are highly desirable:

- Port cities that do not currently have a fee structure will be encouraged to enact one and to develop port projects that serve cruise ship passengers in the manner most compatible with their respective communities, without fear of adverse political consequences;
- In so doing, general fund revenues are taken off of the table—instead, the revenues go directly to communities—competition within the legislature for allocations is reduced.

To summarize: allowing the tax credit clearly benefits the port communities for the reasons I've outlined. At the same time, it will reduce the total amount of passenger tax proceeds received by the State. This reduction, however, should not raise major policy objections because of the severe legal restrictions on the ways that these tax proceeds may be spent.