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OPINION	:	No. 84-402
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THE HONORABLE BRUCE BUNNER, INSURANCE COMMISSIONER, has requested an opinion on the following questions:

1. Are insurance agent license fees paid in California by insurance agents includable in the retaliatory tax computations of nondomestic insurers?

2. Are other taxes and license fees, not imposed pursuant to the Insurance Code or section 28 of article XIII of the Constitution, paid in California by insurance agents includable in the retaliatory tax computations of nondomestic insurers?

3. Where an insurance agent represents more than one nondomestic insurer, how are the fees and taxes of the agent that are includable in the retaliatory tax computations to be calculated for each insurer?

CONCLUSIONS

1. The insurance agent license fees paid in California by insurance agents are includable in the retaliatory tax computations of nondomestic insurers.

2. Other taxes and license fees, not imposed pursuant to the Insurance Code or section 28 of article XIII of the Constitution, paid in California by insurance agents are not includable in the retaliatory tax computations of nondomestic insurers unless specifically so provided in the retaliatory tax law.

3. Where an insurance agent represents more than one nondomestic insurer, the fees and taxes of the agent that are includable in the retaliatory tax computations are to be calculated at the full amount for each insurer.

ANALYSIS

Paragraph (3) of subdivision (f) of section 28 of article XIII of the Constitution provides:

> "When by or pursuant to the laws of any other state or foreign country any taxes, licenses and other fees, in the aggregate, and any fines, penalties, deposit requirements or other material obligations, prohibitions or restrictions are or would be imposed upon California insurers, *or upon the agents or representatives of such insurers*, which are in excess of such taxes, licenses or other fees, in the aggregate, or which are in excess of the fines, penalties, deposit requirements or other obligations, prohibitions, or restrictions directly imposed upon similar insurers, *or upon the agents or representatives of such insurers*, of such other state or country under the statutes of this state; so long as such laws of such other state or country continue in force or are so applied, the same taxes, licenses and other fees, in the aggregate, or fines, penalties or deposit requirements or other material obligations, prohibitions, or restrictions, of whatever kind shall be imposed upon the insurers, *or upon the agents or representatives of such insurers*, of such other state or country doing business or seeking to do business in California. Any tax, license or other fee or other obligation imposed by any city, county, or other political subdivision or agency of such other state or country on California insurers *or their agents or representatives* shall be deemed to be imposed by such state or country within the meaning of this paragraph (3) of subdivision (f).

"The provisions of this paragraph (3) of subdivision (f) shall not apply as to personal income taxes, nor as to ad valorem taxes on real or personal property nor as to special purpose obligations or assessments heretofore imposed by another state or foreign country in connection with particular kinds of insurance, other than property insurance; except that deductions, from premium taxes or other taxes otherwise payable, allowed on account of real estate or personal property taxes paid shall be taken into consideration in determining the propriety and extent of retaliatory action under this paragraph (3) of subdivision (f).

". . . . . ." (Emphases added.)

This constitutional provision is codified in Insurance Code sections 685-685.4[1] and is known as the "retaliatory" insurance tax law. (See *Western & Southern L.I. Co.* v. *Bd. of Equalization* (1981) 451 U.S. 648, 649-651; *Bankers Life Co.* v. *Richardson* (1923) 192 Cal. 113, 117; *American Alliance Ins. Co.* v. *State Bd. of Equalization* (1982) 134 Cal.App.3d 601, 604; *Western & Southern Life Ins. Co.* v. *State Bd. of Equalization* (1970) 4 Cal.App.3d 21, 25-26; *Atlantic Ins. Co.* v. *State Bd. of Equalization* (1967) 255 Cal.App.2d 1, 4.) We are asked three questions concerning its language where taxes and fees are paid in California by insurance agents[2] of nondomestic insurers.

Preliminarily, we note that insurance companies are not taxed in the same manner as other businesses but rather pay a "gross premiums" tax in lieu of most other state and local taxes. (See Cal. Const., art. XIII, § 28; Rev. & Tax Code, §§ 12001-12277; *Metropolitan Life Ins. Co.* v. *State Bd. of Equalization*, *supra*, 32 Cal.3d 649, 652; *Franklin Life Ins. Co.* v. *State Bd. of Equalization* (1965) 63 Cal.2d 222, 224-226; *Massachusetts Mutual Life Ins. Co.* v. *City and County of San Francisco*, *supra*, 129 Cal.App.3d 876, 881-882.) "[T]he gross premiums measure is apparently designed to approximate the volume of business done in this state, and thus the extent to which insurers have availed themselves of the privilege of doing business in California." (*Metropolitan Life Ins. Co.* v. *State Bd. of Equalization*, *supra*, 32 Cal.3d 649, 656; see *Illinois Com. Men's Assn.* v. *State Bd. of*

[1] All statutory section references hereafter are to the Insurance Code unless otherwise stated.

[2] "Agents" are authorized to transact insurance by and on behalf of insurers (§§ 31, 1621), while "brokers" are not so authorized; the two are treated differently for purposes of insurance company taxation. (See *Metropolitan Life Ins. Co.* v. *State Bd. of Equalization* (1982) 32 Cal.3d 649, 658-660; *Western States Bankcard Assn.* v. *City and County of San Francisco* (1977) 19 Cal.3d 208, 218-219; *Hughes* v. *Los Angeles* (1914) 168 Cal. 764, 765; *Massachusetts Mutual Life Ins. Co.* v. *City and County of San Francisco* (1982) 129 Cal.App.3d 876, 885; *Marsh & McLennan of Cal., Inc.* v. *City of Los Angeles* (1976) 62 Cal.App.3d 108, 113-120.)

Equalization (1983) 34 Cal.3d 839, 849-854; *Ins. Indem. Exch*. v. *State Bd. of Equalization* (1945) 26 Cal.2d 772, 775-776.)

The retaliatory tax is assessed against insurance companies in addition to the gross premiums tax. Imposition of the tax was described in *American Alliance Ins. Co.* v. *State Bd. of Equalization*, *supra*, 134 Cal.App.3d 601, 605:

> "Simply stated, the retaliatory tax provides that if a foreign state charges a California insurance company a greater tax for doing business in that state than is levied by California on an insurance company doing business in California, then California will levy an additional tax upon insurers domiciled in that foreign state and doing business in California. The additional tax will be an amount equal to the difference between the two taxes."

The additional tax is assessed by the State Board of Equalization and is administered in part by the Insurance Commissioner. (See Cal. Const. art. XIII, § 28, subd. (h); § 685.3; Rev. & Tax. Code, §§ 12281-12290; Cal. Admin. Code, tit. 10, § 2325.)

The design and purpose of the retaliatory tax is to deter other states from excessively taxing domestic (California) insurance companies doing business in their jurisdictions. (See *Western & Southern L.I. Co.* v. *Bd. of Equalization*, *supra*, 451, U.S. 648, 668-673 ["The impetus for passage of the tax comes from the nationwide insurance industry," "'[t]he actual rationale for the provision is that the application of the retaliatory laws acts as a deterrent to state taxation on the insurance industry," "the retaliatory tax has often been criticized as a distortion of the tax system and an impediment to the raising of revenue from the taxation of insurance," "'in the long run, insurers as a group pay less in taxes because of the provisions,'" "retaliatory taxes 'have kept premiums lower and insurers' profits higher than would otherwise have been the case'"]; see also *American Alliance Ins. Co.* v. *State Bd. of Equalization*, *supra*, 134 Cal.App.3d 601, 604-607; *Massachusetts Mutual Life Ins. Co.* v. *City and County of San Francisco*, *supra*, 129 Cal.App.3d 876, 882,884; *Western & Southern Life Ins. Co.* v. *Bd. of Equalization*, *supra*, 4 Cal.App.3d 21, 34; *Atlantic Ins. Co.* v. *State Bd. of Equalization*, *supra*, 255 Cal.App.2d 1, 4; Pelletier, *Insurance Retaliatory Laws* (1964) 39 Notre Dame Law. 243, 246-24, 267 (hereafter "Pelletier").)

Since the purpose is not to raise revenue as one would anticipate, questions of interpretation naturally arise. The language itself is less than a model of clarity.[3] The

[3] We note that the first sentence of the constitutional provision at issue contains 184 words.

administrative difficulties in applying the retaliatory tax laws of the various states have been set forth in detail. (See Pelletier, *supra*, pp. 226-269.)

1. Insurance Agent License Fees

The first question presented for resolution is whether the insurance agent license fees paid in California by insurance agents are includable in the retaliatory tax computations of nondomestic insurers. We conclude that they are.

The specific fees at issue are: an original license application fee, a qualifying examination fee, and an annual license renewal fee. (§§ 1750-1751.6.) The fees range up to $31 each and are the legal obligations of the agents.[4] The literal language of the retaliatory tax law appears to be applicable to these fees. They constitute "taxes, licenses and other fees, in the aggregate . . . directly imposed upon similar insurers, or upon the agents or representatives of such insurers." (Cal. Const., art. XIII, § 28, subd. (f).)

That these fees are regulatory in nature rather than revenue raising and are personal to the agent do not remove them from this express constitutional language.

The rationale for including such fees in the retaliatory tax computation (placing them on both the California and the foreign state sides of the equation) is that they represent a governmental economic burden upon the business of insurance within each state. They are mandatory, with payment a condition precedent directly related to the conducting of the business of insurance. If these fees were not part of the equation, states would be free to leave the gross premiums tax as is and raise the insurance agent license fees to whatever limit without the threat of retaliation. (See Pelletier, *supra*, pp. 255, 258-259.)

In a different context (the "in lieu" provision), the Supreme Court stated in *Hughes* v. *Los Angeles*, *supra*, 168 Cal. 764, 765:

> "The distinction sought to be drawn in this case is that this particular license fee is not imposed upon the companies but upon the agents of the companies. This is true, but upon the other hand it is equally true that every insurance corporation must act through agents and can act only through agents, and that, therefore, in a direct and immediate sense a tax upon such agents for the right to do business is a tax upon the corporation's right to do business."

[4] Two other agent license fees, the insurance company agent "appointment" and "termination" fees, are chargeable to the insurer. (§ 1751.3.)

Consequently, inclusion of the fees in the retaliatory tax computation would be consistent with their treatment for purposes of the in lieu provision.

In the most relevant reported case of which we are aware, the Supreme Court of Ohio concluded that insurance agent license fees (imposed on the insurer) were includable when calculating the retaliatory tax obligations of nondomestic insurers. (*Indemnity Ins. Co. of North America* v. *Stowell* (1961) 172 Ohio St. 167 [174 N.E.2d 536, 539-541].)

Hence, we conclude that insurance agent license fees are part of the aggregate governmental exaction placed directly upon the business of insurance to be equalized under the retaliatory tax law. Those fees paid in California are to be balanced against those that would be paid under like circumstances in the foreign state by a California company (the "mirror image" approach) when calculating the retaliatory tax obligation of a nondomestic insurer.

2. Other Taxes and License Fees

The second question concerns those taxes and fees paid in California by insurance agents that are not directly imposed upon the business of insurance under the Constitution or the Insurance Code. We conclude that such taxes and fees are not includable in computing the retaliatory tax obligation of a nondomestic insurer unless specifically so provided in the retaliatory tax law.

As previously mentioned, the gross premiums tax is imposed "in lieu of all other taxes and licenses, state, county, and municipal, upon such insurers and their property, except . . . ." (Cal. Const., art. XIII, § 28, subd. (f).)

One exception is for taxes upon the real estate of an insurance company. Such taxes, therefore, paid by an insurance agent could conceivably be included in the retaliatory tax computation of a nondomestic insurer. The retaliatory tax law itself, however, expressly provides that these taxes are not to be calculated in the comparison except indirectly when in the form of deductions against premium taxes. (Cal. Const., art. XIII, § 28, subd. (f).)

Another express exception is for "[m]otor vehicle and other vehicle registration license fees and any other tax or license fee imposed by the state upon vehicles, motor vehicles or the operation thereof." (Cal. Const., art. XIII, § 28, subd. (f).) To the extent that these fees are imposed ad valorem (according to value), they would be treated under the same retaliatory tax provision as real estate taxes—they can only enter into the calculations indirectly when in the form of deductions allowed against premium taxes.

Personal income taxes paid by insurance agents would be another type of tax that conceivably would be subject to consideration. Again, however, the retaliatory tax law expressly precludes their incorporation into the computation. (Cal. Const., art. XIII, § 28, subd. (f).)

Other taxes paid by insurance agents would at most be an *indirect* burden upon the business of insurance. (See *Western State Bankcard Assn*. v. *City and County of San Francisco*, *supra*, 19 Cal.3d 208, 218; *Bunker Hill Associates* v. *City of Los Angeles* (1982) 137 Cal.App.3d 79, 87; *Occidental Life Ins. Co.* v. *State Bd. of Equalization* (1982) 135 Cal.App.3d 845, 847; *Massachusetts Mutual Life Ins. Co.* v. *City and County of San Francisco*, *supra*, 129 Cal.App.3d 876, 880-886; *Marsh & McLennan of Cal., Inc.* v. *City of Los Angeles*, *supra*, 62 Cal.App.3d 108, 115, 119; see also, *American Alliance Ins. Co.* v. *State Bd. of Equalization*, *supra*, 134 Cal.App.3d 601, 606-607.)

We find no purpose in applying the retaliatory tax law to such types of taxes. For the same reason (the tangential nature) the tax would be imposed outside the scope of the "in lieu" provision, it should be excluded from the retaliatory tax computation. (See *Pacific Mut. Life Ins. Co.* v. *Gerber* (1961) 22 Ill.2d 196 [174 N.E.2d 862, 865]; Pelletier, *supra*, pp. 258-259.) The retaliatory tax law is concerned with those taxes and fees "directly imposed" upon insurers and their agents. The administrative difficulties in making such a calculation would be another reason for such exclusion being made by the Legislature and the framers of the Constitution. (See *Kay* v. *Pacific Tel. & Tel. Co.* (1978) 83 Cal.App.3d 814, 817; *City of San Jose* v. *Donohue* (1975) 51 Cal.App.3d 40, 45; Pelletier, *supra*, pp. 254, 262-268.)

In answer to the second question, we conclude that taxes and license fees not imposed pursuant to the Insurance Code or section 28 of article XIII of the Constitution that are paid by insurance agents are not includable in the retaliatory tax computations of nondomestic insurers unless the retaliatory tax law specifically so provides.

3. Calculation of the Fees

The final question concerns the method by which the insurance agent license fees paid in California are to be calculated in the retaliatory tax computation of a nondomestic insurer. We conclude that the full amount of such fees are includable even where the agent represents more than one nondomestic insurance company.

An insurance agent may be authorized to represent any number of insurers. Where some of these companies are nondomestic insurers, the question arises as to how the retaliatory tax should be calculated with respect to the license fees of the agent. Should

the fees be apportioned among the nondomestic insurers? What if the companies reimburse (or do not) the agent for the fees?

As previously mentioned, the purpose of the retaliatory tax law is not to raise state tax revenues but to equalize tax burdens placed upon insurance companies. (*Western & Southern L.I. Co.* v. *Bd. of Equalization*, *supra*, 451 U.S. 648, 668-673; *American Alliance Ins. Co.* v. *State Bd. of Equalization*, *supra*, 134 Cal.App.3d 601, 604-605.) In keeping with this purpose, the law is applied in both a "real world" and hypothetical setting. (See *Western & Southern Life Ins. Co.* v. *Bd. of Equalization*, *supra*, 4 Cal.App.3d 21, 27; Pelletier, *supra*, pp. 252-253.)

We believe that the license fees of an agent should be calculated on both sides of the equation at the full amounts when calculating a nondomestic insurer's additional retaliatory tax liability—regardless of who pays the amounts or how many other insurers are represented by the agent. Each insurer is to look to its own state's exactions placed upon a similarly situated California insurer (and its agents) for comparison with the liability of the insurer's agents in California. This fulfills the purpose of the statutory scheme of equalizing the economic burdens placed upon the insurance industry, allows for administrative convenience,[5] and does not frustrate any important governmental objective.

In answer to the third question, therefore, we conclude that where an insurance agent represents more than one nondomestic insurer, the fees and taxes of the agent includable in the retaliatory tax computation are calculated at the full amount for each insurer.

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[5] Besides the fact that the fees are relatively insignificant in amount and are offset against those in the foreign state, we note that the insurer would not be in a position to calculate an apportionment of the fees. Limiting the inclusion to whatever amount is reimbursed by the insurer would be feasible, but such limitation does not appear to be contained in the retaliatory tax law as previously discussed.