



OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of }
 DOUGLAS AIRCRAFT COMPANY, INC. }

Appearances:

For Appellant: Ernst & Ernst, Los Angeles

For Respondent: Reynold E. Blight, Franchise Tax Commissioner

O P I N I O N

This is an **appeal**, pursuant to Section 25 of the California Bank and Corporation Franchise Tax Act (Stats. 1929, Chap. 13), from the action of the Franchise Tax Commissioner in overruling the protest of Douglas Aircraft Company, Inc., against a proposed additional assessment based on its net income for the year ended November 30, 1929.

There is no controversy concerning the facts. The Appellant is a Delaware corporation doing business in California, where it is engaged in designing, manufacturing and **constructing** airplanes. Its income is derived mainly from contracts with the Army and Navy Departments of the United States Government for the manufacture and construction of airplanes for military and naval **purposes**.

The contracts under which these military and naval planes are manufactured are entered into pursuant to bids made in the City of Washington, D. C., all negotiations concerning the execution of contracts being actually handled in the City of Washington, and the contracts themselves are actually executed on behalf of the government and through the medium of an officer on behalf of the corporation in that city. The planes are manufactured in the State of California at the plant of the company, but at all times the construction is under the supervision of Army and Navy officers, a detail of **whom are** maintained at the plant. Deliveries of planes are made either by flying planes under their own power to the point of delivery: or by crating and shipping them. The United States Government from time to time advances money to the company on unfinished work in process. The work, while in **progress**, is insured in favor of the United States.

It is the contention of the taxpayer that in the manufacture of airplanes for the Federal Government, under the arrangement described, it is acting as a Federal instrumentality not subject to state tax. **It is** further contended that the tax is a direct burden on the operations of the Federal Government

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because of the "cost plus" basis upon which the planes are manufactured.

These propositions are rejected by the Commissioner, who proposes to assess an additional tax on income derived from such transactions but excluded by the taxpayer in its self-assessment.

In support of its position, the taxpayer relies upon the decisions of the United States Supreme Court in the cases of Macallen v. Massachusetts, 279 U. S. 620, and Panhandle Oil Co. v. Knox 277 U.S. 218. The former case held that, "under the guise of an excise tax measured by net income, a state may not tax income from exempt sources, such as federal and state bonds, thereby accomplishing by indirection what it is forbidden to do directly."

The latter was to the effect that the State of Mississippi could not compel payment of a gasoline tax, based on a specific amount per gallon, by an oil company selling its fuel to the United States Government, thereby increasing the cost of the gasoline to the Government.

As observed in our decision in the Matter of the Appeal of Vortex Manufacturing Company (filed August 4, 1930), it is plain that our law contemplates the inclusion of income from all sources in the tax base. (Secs. 6, 7 and 8, Chap. 13, Stats. 1929). If we should rule that the Commissioner erred in proposing the additional assessment questioned by the Appellant, we should have to do so upon the assumption that the Act is unconstitutional. For the reasons stated in the Vortex decision, even conceding that this case is parallel, which is not clearly apparent to us, we do not feel warranted in deciding that income may be excluded from the tax base because of its exempt origin.

O R D E R

Pursuant to the views expressed in the opinion of the Board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, that the action of Reynold E. Blight, Franchise Tax Commissioner, in overruling the protest of Douglas Aircraft Company, Inc., a corporation, against a proposed assessment of an additional tax of \$6,742.15 with interest, under Chapter 13, Statutes of 1929, be and the same is hereby sustained.

Done at Sacramento, California, this 20th day of November, 1930, by the State Board of Equalization.

R. E. Collins, Chairman
Fred. E. Stewart, Member
Jno. C. Corbett, Member
H. G. Cattell, Member

ATTEST: Dixwell L. Pierce, Secretary