



BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
HOWARD AUTOMOBILE COMPANY)

Appearances:

For Appellant: Orville R. Vaughn of San Francisco

For Respondent: A. A. Manship, Franchise Tax Commissioner

O P I N I O N

This is an appeal under Section 25 of the Bank and Corporation Franchise Tax Act (Chapter 13, Statutes of 1929) from the action of the Franchise Tax Commissioner in overruling the protest of Howard Automobile Company against a proposed assessment of an additional tax of \$279.45 based upon the return of the corporation for the year ended December 31, 1928. The grounds urged on appeal are that the Commissioner erred by including as taxable income the following items:

1. Interest received from obligations and instrumentalities of the United States, and

2. Dividends received from a national banking association located in the State of New York.

So far as the first item above enumerated is concerned, for the reasons set forth in the opinion of the Board in the case of Vortex Manufacturing Company (filed August 4, 1930) and in view of the recent decision of the Supreme Court of this State in the case of The Pacific Co., Ltd. v. Johnson, 81 Cal. Dec. 519, holding the Act constitutional as against a similar objection, we believe that the action of the Commissioner to include such income must be sustained.

The second item is said to have been illegally included because of the provisions of Section 5219 of the Revised Statutes of the United States relating to the taxation of national banking associations and their shareholders. It is claimed by the Appellant that since California has adopted the fourth method authorized by Section 5219, i.e., a tax on national banking associations "according to or measured by" their net income the conditions embodied in Subdivision C of Clause 1 of said section prohibited the inclusion in the measure of the tax of a corporation, under this act, of dividends derived from a national banking association located outside of California. Therefore, we shall proceed with an analysis of the provisions of the federal statute on this subject.

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In the first place, it must be borne in mind that Section 5219 purports only to regulate the method of taxation to be employed with reference to national banking **associations** or their shares. It does not attempt to provide how any other banking association, corporations or their shares shall be taxed. Subdivision C of Clause 1 of Section 5219 contains provisions limiting the rate of taxation to be imposed under the third or fourth alternatives permitted by the section. There is the proviso that a state which imposes a tax "on or according to or measured by the net *income* of, or a franchise or excise tax on, financial, mercantile, manufacturing, and business **corporations** organized under its own laws or laws of other states and also imposes a tax upon the income of individuals, may include in such individual income dividends from national banking associations located within the state on condition that it also includes dividends on domestic corporations and may likewise include dividends from national banking associations located without the state on condition that it also includes dividends from foreign corporations, but at no higher rate than is imposed *on* dividends from such other corporations."

Through a process of omission counsel for Appellant constructs from this language the following:

"A state which imposes a tax according to or measured by the net income of financial, mercantile, manufacturing, and business corporations and also imposes a tax upon the income of individuals, may include dividends from national banking associations located without the state."

Because California does not impose a tax on individual incomes it is asserted that it can not legally include dividends from national banks in income as a measure of the franchise tax on corporations by virtue of the foregoing language.

The difficulty with the reasoning of the counsel for the Appellant is that in his omissions he has excluded language which is vital to a proper application of the entire proviso **in the** federal statute. A careful reading of the statute will disclose that its intent is to provide that a state which imposes a tax according to or measured by the net income of financial, mercantile, manufacturing, and business corporations, and also imposes a tax upon the income of individuals, may include in such individual income dividends from national banking **associations located** without the state on condition that it **also** includes dividends from foreign corporations, further, provided, that no higher rate is imposed upon the income from the bank dividends than from such other corporate dividends. The **proviso** does not relate in any manner to what may be included in the net income of a corporation for the purpose of determining the measure of its state tax. It applies only to the inclusion of national bank dividends in the net income of an individual for the **purpose** of state taxation.

Further reference to the provisions of Section 5219 will disclose that the four methods for the taxation of national

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banking associations or their shares are expected to be mutually exclusive with the exception contained in the proviso in Sub-division C of Clause 1 above quoted, -and that the effect of the proviso is to permit the taxation of national banking associations "on or according to or measured by" their net income and under certain conditions at the same time to permit the taxation, as a part of individual income, of dividends received from national bank shares. The clause has no reference whatever to such a situation as is presented to us in the instant case and we perceive nothing in its language which would prohibit the inclusion of dividends from a national bank located outside of this State in the net income of the corporation for the purposes of taxation under this Act.

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 the Franchise Tax Commissioner in overruling the protest of Howard Automobile Company, a corporation, against a proposed assessment of an additional tax of \$279.45 based upon the net income of said corporation for the year ended December 31, 1928, be and the same is hereby sustained.

Done at Sacramento, California, this 15th day of May, 1931, by the State Board of Equalization.

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

ATTEST: Dixwell L. Pierce, Secretary