



BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
HENRY INVESTMENT COMPANY)

Appearances:

For Appellant: Ralph H. Smith, Attorney at Law; Homer H. Tooley and Raymond C. Beecher, Accountants
For Respondent: Albert A. Manship, Franchise Tax Commissioner

O P I N I O N

This is an appeal pursuant to Section 25 of the Bank-and Corporation Franchise Tax Act (Chapter 13, Statutes of 1929, as amended) from the action of the Franchise Tax Commissioner in overruling the protest of Henry Investment Company, a corporation, to a proposed assessment of an additional tax in the amount of \$13,163.66 for the year 1929 based on Appellant's return for the year ended December 31, 1928.

During the year 1928, the Appellant realized a profit of \$1,024,203.37 from certain transactions in the way of purchases and sales of securities on the New York Stock Exchange.. This amount was not included in the taxable income of the Appellant in its return for said year. The Commissioner, however, include this amount in the income to be used as a measure of a tax on Appellant for the privilege of doing business in this State during the year 1929, and accordingly proposed to assess the additional tax involved herein.

The Appellant claims that it took no orders for others but used its own funds exclusviely and simply directed the brokerage firms of Walsh, O'Connor and Company, and Chapman de Wolfe and Company, both having their principal place of business in San Francisco, to purchase on margin certain securities on the New York Exchange. The above brokerage firms transmitted the Appellant's orders to brokers in New York who executed them. None of the securities involved was actually delivered to the San Francisco brokers nor were any of them ever listed in the name of the Appellant.

In view of the provisions of Section 10 of the Act to the effect that if the business of a corporation is done partly within and partly without the state, the tax imposed by the Act: shall be measured only by the income-derived from business done in the state; it would seem that if the income in question in this appeal was derived either wholly or partially from business done in New York such income to the extent that it was derived from business done in New York, should not be considered in determining the amount of tax due from Appellant under the Act.

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We think it also follows from the provisions of Section 10 that if the activities of Appellant by which the income in question was produced did not amount to doing business in New York such income should be allocated 100 per cent to California and the full amount thereof should be included in the measure of the tax imposed by the Act. Thus, the question presented for our determination is whether the Appellant can be considered as having engaged in business in New York, and if so, what portion of the above item of income was derived from business done in New York and what portion, if any, was derived from business done in California.

The Appellant insists that the income in question was derived from transactions completed by it entirely within the State of New York inasmuch as the New York broker, being appointed the California brokers under a general authorization from Appellant, acted as agent for Appellant, and inasmuch as the purchase and sales of securities were consummated within the State of New York.

It should be noted, however, that Appellant apparently did not qualify to do business in New York, did not maintain an office or make investments of its capital there, and did not have any employees, there who held themselves out as representatives of Appellant. The New York broker, even though he may have acted as an agent of Appellant, did not make purchases in the name of Appellant and apparently did not know for whom he was acting in making purchases and sales of securities. Furthermore, it would seem that the broker in purchasing and selling securities simply carried on the usual and customary activities of his business and not the business of Appellant.

In this connection we think it pertinent to refer to the case of Southern Cotton - Oil Co. v. Roberts, 25 App. Div. 13, in which it was held that a foreign corporation which sent goods to a commission merchant in New York, who sold the goods and deposited the proceeds to the credit of the corporation in a bank in New York, was not doing business in New York so as to be subject to a franchise tax imposed by that state on corporations doing business in New York. In the course of its opinion, the Court expressed itself as follows:

"The goods consigned to the commission merchants were in their possession and control, and their disposition in accordance with the directions of the relator was a part of their business, not the business of the relator..... It should not, I think, be held that the consignment of goods by a nonresident manufacturer to a resident commission merchant for cash sale constitutes a doing of business by the manufacturer within this state..... In this view of the character and effect of the dealings between the relator and..... (the commission merchant), coupled with the fact that the relator has here no office or place of business, the

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conclusion is reached that the relator was not subject to the tax in question."

We think consideration should be given not only to the form but also to the actual nature and purpose of the transaction by which the income in question was produced. As noted above, Appellant simply gave orders to local brokers to buy and sell on margin certain securities on the New York Exchange. Inasmuch as none of the securities bought was ever called for by, or delivered to, Appellant, it would seem that the Appellant never intended to become the owner of the securities (Sheehy v. Shinn, 103 Cal. 325).

Furthermore, it does not appear that any of the securities sold were furnished by, or were ever in the possession of the Appellant. Consequently, it would seem that it was a matter of indifference to Appellant whether any securities were actually bought or sold so long as the proper entries were made in the books of the local brokers (Cashman v. Root, 89 Cal. 373). Under these circumstances, we think it evident that the only purpose of the transactions was to enable the Appellant to speculate on the rise or fall of the market price of certain securities. This speculation was accomplished when the orders were given to, and margin deposited with, the local brokers,, The profit or loss to Appellant resulting therefrom was not affected by transactions entered into by the brokers subsequently thereto. The brokers were not under obligation either to purchase or sell securities (Ingraham v. Taylor, 58 Conn. 503). Hence, it would seem that in arranging with a New York broker for the purchase and sale of securities, the brokers acted to protect themselves, and not the Appellant.

For the reasons above stated, we must hold that the income in question was not derived from business done by Appellant in New York, and, consequently, that the Commissioner acted correctly in including the full amount thereof in the measure of the tax imposed by the 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 Henry Investment Company, a corporation, against a proposed assessment of an additional tax of \$13,163.66 under Chapter 13, Statutes of 1929, 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 March, 1933, by the State Board of Equalization.

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

ATTEST: Dixwell L. Pierce, Secretary