

TAXATION: Bank Tax Act of 1946, Income representing the payment of interest for which the liability to pay had become fixed and absolute before the commencement of the taxable period would not be subject to the tax imposed by this act.

FILED 1

May 1, 1950



Mr. T. R. Allen
Supervisor, Income Tax,
Department of Revenue,
Jefferson City, Missouri.

Dear Mr. Allen:

This is in reply to your request for an opinion from this department, which request reads as follows:

"In connection with the administration of the Bank Tax Act of 1946, this department desires a ruling with respect to interest which accrues on intangible instruments prior to the year of 1945 which is recovered in years subsequent to that date as to whether or not such interest should be included in arriving at net income when recovery of such accruals are made at a later date.

"The question herein involved is similar to that on which you rendered an opinion under date of January 23, 1950, with respect to the General Intangible Tax Act. It is the contention of this department that due to the fact that under the General Intangible Tax Act, which uses the yield of an intangible instrument as the basis of valuation for the purpose of that tax, that the ruling rendered by you on January 23, 1950, could not be used in connection with the administration of the Bank Tax Act, my reason being that the basis of the General Intangible Tax and that of the Bank Tax is entirely different.

"I would appreciate a ruling from your office in order that we may properly administer the Bank Tax Act. I would appreciate your prompt response as this question has arisen in connection with the preparation of bank tax returns. My inquiries so far have been principally with regard to the maturity of government bonds. In such cases the full amount of interest for the

Mr. T. R. Allen:

May 1, 1950

period of time for which the bonds run is not actually recovered until the bond is eligible for redemption.

"I will appreciate your prompt reply."

The question presented by your letter requires an interpretation of the "Bank Tax Act of 1946" enacted Laws of 1945, page 1921, and imposing a tax on banks in lieu of the tax imposed by Mo. R.S. 1939, Sections 10959 and 10960, under which state and counties levied an ad valorem tax on shares of stock of state and national banks.

For purposes of this opinion your attention is particularly directed to those sections of the Bank Tax Act reading as follows:

Laws of 1945, page 1921, Section 3 is as follows:

"A. Every national banking association shall be subject to an annual tax according to and measured by its net income in accordance with method numbered (4) authorized by the Act of Congress of March 25, 1926, amending Section 5219 of the Revised Statutes of the United States, and every other banking institution as herein defined shall be subject to an annual tax for the privilege of exercising its corporate franchises within the State of Missouri according to and measured by its net income pursuant to the provisions of this Act.

"B. For the period in the taxable year 1946 between the effective date of this Act and the end of the calendar year, the tax shall be measured by the taxpayer's net income as hereinafter defined for the calendar year 1945, or such portion thereof during which the taxpayer was engaged in business.

"C. For the taxable year 1947 and each taxable year thereafter the tax shall be measured by the taxpayer's net income as hereinafter defined for the preceding calendar year.

"D. The rate of tax for each taxable year shall be seven per cent (7%) of such net income.

"E. Each taxpayer shall be entitled to credits against the tax imposed by this Act for all taxes

paid to the State of Missouri or any political subdivision thereof during the relevant income period, other than taxes on real estate, contributions paid pursuant to the Unemployment Compensation Tax Law of Missouri, and taxes imposed by this Act, except that no credit shall be allowed for any tax paid by any such taxpayer in the year 1945 for its shareholders based upon the value of its shares."

Laws of 1945, page 1921, Section 5 is in part as follows:

"A. 'Net Income' means gross income as defined in paragraph B of this Section minus the deductions allowed in paragraph C of this Section.

"B. 'Gross Income' includes: all gains, profits, earnings and other income of the taxpayer from whatever sources derived during the income period, including but not limited to interest from obligations issued by the United States Government or any political subdivision or any instrumentality thereof, or any state or political subdivision thereof, or issued by any foreign country or nation or political subdivision thereof; all rents, compensation for services, commissions, brokerage and other fees; all gains or profits from the sale or other disposition of any property, real or personal, tangible or intangible; and all recoveries on losses sustained in the ordinary course of business subsequent to the effective date of this Act; * * *

* * * * *

"D. Net income shall be computed in accordance with the method of accounting regularly employed in keeping the books of the taxpayer, unless such method does not clearly reflect the income, in which case the computation shall be made in accordance with such method as in the opinion of the Director does clearly reflect the income."

Laws of 1945, page 1921, Section 11 is as follows:

"It is the purpose and intent of the General Assembly to substitute the tax provided by this

Mr. T. R. Allen:

May 1, 1950.

Act for the tax on bank shares which was imposed by Section 10959, Revised Statutes of Missouri, 1939, and for all taxes on all tangible and intangible personal property of all banking institutions subject to the provisions of this Act, and for all property taxes on the shares of such banking institution."

The question herein involved is whether interest which accrued on intangible instruments prior to the effective date of the Bank Tax Act, but which is received subsequent to that date, is to be included as "income" in computing the tax due.

It is our understanding that a bank may report its income for the purposes of this tax either on an "accrual" basis, or report the entire income from intangibles, such as government bonds, in the year in which the bond matures or is redeemed. Many banks have elected to report their income on an accrual basis, by reporting as income the amount of interest which has accrued to the intangible during the preceding year. Those banks electing that option will not pay a tax on that portion of the interest which accrued to intangibles owned by them prior to the effective date of this act, but are taxed only on that interest accruing after the act became effective.

The act directs (Section 5 D) that net income shall be computed in accordance with the method of accounting regularly employed in keeping the books of the taxpayer, unless such method does not clearly reflect the income, in which case the computation shall be made in accordance with such method as in the opinion of the Director of Revenue does clearly reflect the income. Interest due prior to the effective date of this act, could have been reduced to possession prior to the incidence of this tax. It is, therefore, capital. Interest accruing on or after that date is taxable income. Money owed is income accrued from the time when the liability to pay becomes absolute and in the case of the government bonds mentioned in your letter the liability to pay became absolute before the commencement of the taxable period, though payment was not to be made until after that date. Interest which has accrued after the effective date of the act would, of course, be reported in the year in which it is received if the taxpayer has failed to elect to pay on an "accrual" basis.

The general rule for Federal income taxation, and in substantially all income tax states, is that the tax may be imposed upon income earned or accrued prior to the enactment of the income tax statute. Missouri follows a contrary rule because of the constitutional provision that no ex post facto law, nor law impairing

Mr. T. R. Allen;

May 1, 1950

the obligation of contracts, or retrospective in its operation can be enacted. (Mo. C.T. par. 10-003).

From the foregoing statements, we reach the conclusion that the taxpaying bank should report that income which accrues after the effective date of the Bank Tax Act and should not report as income that interest on government bonds mentioned in your letter which accrued prior to the effective date of the act, i.e., where the liability to pay, and the right to receive interest, becomes absolute before the commencement of the taxable period, the payments received thereafter should not be reported as income for that taxable year.

In the case of *Plant v. Walsh*, (280 F. 722) which involved the question of whether dividends declared by a corporation prior to the effective date of the Federal Income Tax Law should be reported as income if received after that law became effective, the court ruled that the interest represents income accrued to the owners of the bonds prior to the incidence of the tax, and does not constitute taxable income when received thereafter. The court said as to the interest payable prior to the effective date of the Income Tax Act of 1913, the liability to pay became absolute before the commencement of the taxable period, though payment was not due until after the beginning of that period. Therefore, the corporate bondholder was not liable to assessment of income tax on interest which was to be paid after the effective date of the taxing act when the liability to pay had become fixed before the taxing act was effective.

Only one case has been reported under the Bank Tax Act. This case, (205 S.W. (2d) 726, 356 Mo. 1204) was an action by the First National Bank of St. Joseph, et al. v. Buchanan County, et al., for a declaratory judgment determining whether plaintiffs were bound to pay, either or both, (1) a tax levied by the City of St. Joseph under the method and plan provided in Mo. R.S. Section 10959, relating to county assessors and assessments under which state and counties levied an ad valorem tax on shares of stock of state and national banks and, (2) the tax levied by the "Bank Tax Act of 1946." The court in that case said:

"The 1945 Constitution changed the scheme of taxation in Missouri. For the purpose of taxation property was divided into three classes; real property, tangible personal property and intangible personal property. As to intangible personal property the Constitution provides that All taxes on property in Class 3 and its subclasses, and the tax under any other form of taxation substituted by the general assembly for the tax on bank shares, shall be assessed, levied and collected by the state and returned as pro-

vided by law, less two per cent for collection, to the counties and other political subdivisions of their origin, in proportion to the respective local rates of levy.' Const. Mo. 1945 Art. 10, Sec. 4.

"To effectuate the purposes of the Constitution and particularly to carry out the contemplated tax scheme the 1945 General Assembly enacted a series of laws. Among other laws, the General Assembly repealed Articles 1 of Chapter 74, R.S. Mo. 1939, Mo. R.S.A. Secs. 10936-10942, entitled 'What Property Taxable and Where,' and enacted the scheme of taxation contemplated by Section 4 of Article 10 of the 1945 Constitution. This act was effective December 19, 1945, Laws Mo. 1945, p. 1799, Mo. R.S.A. Sec. 10942.1 et seq. Another act, effective as of December 5, 1945, repealed the older law relating to county assessors and the assessment of property, Mo. R.S.A. Secs. 10943 - 10969, 10971 - 10995, 10997 - 11000, and enacted a different method and plan relating to county assessors and assessments. Laws No. 1945, p. 1782, Mo. R.S.A. Sec. 11000.1 et seq. This act plainly repealed the previous law, Mo. R.S.A. Secs. 10959 - 10960, under which the state and counties levied an ad valorem tax on the shares of stock of state and national banks. A new act, approved April 19, 1946, which did not specifically repeal any previous law, provided for the taxation of intangible personal property in accordance with the contemplated new scheme. Laws Mo. 1945, p. 1914, Mo. R.S.A. Sec. 11456.1 et seq. A further law, the 'Bank Tax Act' (House Bill 888), levied 'an annual tax according to and measured by its net income in accordance with method numbered (4) authorized by the Act of Congress of March 25, 1926' on all national banks and on all state banking institutions. Laws Mo. 1945, p. 1921, Mo. R.S.A. Sec. 11456.101 et seq. This act provides that 'For the period in the taxable year 1946 between the effective date of this Act, and the end of the calendar year, the tax shall be measured by the taxpayer's net income as herein-

May 1, 1950

after defined for the calendar year 1945, * * * And, 'For the taxable year 1947 and each taxable year thereafter the tax shall be measured by the taxpayer's net income * * * for the preceding calendar year.' This act was approved on April 23, 1946, but it recited, in conclusion, 'Since the Constitution of Missouri of 1945 provides that all inconsistent laws shall be void after July 1, 1946, * * * this act shall become effective from and after its passage and approval but shall become operative on July 1, 1946.' Finally, in so far as they bear on this case, the General Assembly enacted a law relating to assessors in cities of the first class and the taxation of real and tangible personal property. Laws Mo. 1945, p. 1253, Mo. R.S.A. Secs. 6301 - 6304, 6306, 6307, 6348.

* * * * *

"But there is a further reason why the Bank Tax Act, Laws of Mo. 1945, p. 1921, could not operate as to these banks in St. Joseph for the entire fiscal year 1946 and thus supplant or supersede the city's tax. The act was approved on the 23rd day of April, 1946 but by its own terms was to 'become operative on July 1, 1946.' As we have noted the act levies an annual tax on banks based on their net incomes. It provides: 'B. For the period in the taxable year 1946 between the effective date of this Act (July 1, 1946) and the end of the calendar year, the tax shall be measured by the taxpayer's net income as hereinafter defined for the calendar year 1945 * * *.' Mo. R.S.A. Sec. 11456.103. For the tax year 1947 and thereafter the tax is to be measured by the taxpayer's income 'for the preceding calendar year,' or here 1946. Plainly, therefore, the act which by its own terms is to become operative on July 1, 1946, levies a tax for the year 1946 on the taxpayers, the banks, income for one half year prior to the operative period of the act if not upon their incomes for 1945. In so doing the act clearly falls within the prohibition of another section of the Constitution. The Constitution of Missouri, the old as well as the new, unlike most constitutions (annotations 11 A.L.R. 518; 109 A.L.R. 523; 118 A.L.R.

1153) provides 'That no ex post facto law, nor law impairing the obligation of contracts, or retrospective in its operation, * * * can be enacted.' Const. Mo. 1945, Art. 1, Sec. 13. The Schedule does not indicate that any exception to this provision of the Bill of Rights was intended by the Constitution or contemplated in the General Assembly's effectuating the new tax pattern. Even though a tax to be assessed and collected in one year on the income of the preceding year 'is a tax for the year of its collection, and not for the year in which the income was received' (61 C.J. Sec. 2331, p. 1581), the tax imposed by the Bank Tax Act, however it is viewed, is retrospective in its operation and could not be effective in the circumstances of this case and in any event prior to July 1, 1946.

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"The Bank Tax Act is certainly retrospective and inoperative as to all the parties in the City of St. Joseph prior to July 1, 1946. The various constitutional and legislative enactments having authorized cities of the first class to levy an ad valorem tax on national bank shares for the tax year 1946 the Bank Tax Act on net income could not be operative as to national banks in the City of St. Joseph after July 1, 1946 because 'The imposition by any State of any one of the above four forms of taxation shall be in lieu of the others, * * *.' 12 U.S.C.A. Sec. 548; Buder v. First National Bank, 8 Cir., 16 F. 2d 990; State ex rel Orr v. Buder, 308 Mo. 237, 271 S.W. 508, 39 A.L.R. 1199; Board of Commissioners of Oklahoma County v. State Board of Equalization, 155 Okl. 183, 8 P. 2d 732. The Bank Tax being inoperative in St. Joseph for the year 1946 as to national banks there could be no question of credits in the national banks' 1947 taxes. State ex rel. Meyer Bros. Drug Co. v. Koeln, 282 Mo. 438, 222 S.W. 389; State ex rel. American Mfg. Co. v. Koeln, 278 Mo. 28, 211 S.W. 31. The only reason offered for the Bank Tax Act not being applicable to the state banks after July 1, 1946, is the state's

Mr. T. R. Allen:

May 1, 1950.

policy of maintaining them on a parity with competing national banks. But no legal reason for their being exempted after July 1, 1946, is suggested and we know of none, consequently from and after that date the appellant state banks in St. Joseph are subject to the act and are entitled to the corresponding credits provided 'during the relevant income period.' * * *

From the ruling of the Missouri Supreme Court in this case we find that the Bank Tax statute levying an annual tax on banks based on net income which by its terms was to become operative on July 1, 1946, could not operate retrospectively on income received before such date; that when the liability to pay interest on an intangible became fixed and absolute before the commencement of the taxable period as would be true of interest due on a government bond, then such payment shall not represent income subject to the tax, even though actual payment is made after the act became effective.

CONCLUSION

It is therefore the opinion of this office that the "Bank Tax Act of 1946" does not operate so as to impose a tax based on interest accrued on intangibles before July 1, 1946, when the liability to pay such interest became fixed and absolute before the commencement of the taxable period, even though actual payment of the interest is realized after the operative date of the act.

Respectfully submitted,

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APPROVED:

J. E. TAYLOR
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