

INTANGIBLE PERSONAL  
PROPERTY TAX:

Payments received by Educational Credit Bureau, Inc., a Missouri corporation, from students located outside the State of Missouri are not to be included for the purpose of determining the tax of that corporation under the provisions of Credit Institutions Act.

JOHN M. DALTON  
XXXXXXXXXX



July 9, 1953

XXXXXXX

J. C. Johnsen

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

Dear Mr. Allen:

Your recent request for an opinion as to whether the Educational Credit Bureau, Inc., is taxable on that part of its income as hereinafter set out under the Credit Institutions Act of 1946, Sections 148.120-148.230, inclusive, is at hand. The pertinent facts are set out below.

The Educational Credit Bureau, Inc., is a Missouri corporation with offices exclusively in Missouri, and it has no agents, employees or property in other states. It was organized to assist the Arthur Murray Dance Studios throughout the United States in the operation of their business by providing financing as hereinafter set out. The Arthur Murray Dance Studios give dance instruction, and many students desire to purchase instruction on deferred payment plan contracts. The studios-excepting those located in the State of Missouri, which are concededly taxable under this act-in other states agree to give dance instruction courses to students who agree to take a definite number of hours of instruction without the right of cancellation and to make payments therefor in accordance with installment payment contracts which they and the individual studios execute. If the individual studio desires, it may sell these installment contracts to the Educational Credit Bureau, Inc., who pays the studio an amount equal to 90% of the then unpaid balance, of which 50% is paid to the studio on receipt by the Educational Credit Bureau, Inc. of each contract, and the remaining 40% is remitted when payment of the full face amount of the contract has been made by the student. If default is made in the payment by a student, the studio re-purchases the contract involved without loss to Educational Credit Bureau, Inc., which retains 10% of the amounts collected by it from the student before defaulting. When the Educational Credit Bureau, Inc. purchases an

Mr. T. R. Allen

installment contract from a studio, it informs the student by mail that his contract is now owned by it and that the student should make his payments directly to the office of the Educational Credit Bureau, Inc. in Kansas City, Missouri. It sends an installment payment booklet to the student wherever he may live in the United States, and he is instructed to send slips from the booklet with his remittances.

The question here is as to whether the Educational Credit Bureau, Inc. is liable for payment of the tax under the Missouri Credit Institutions Tax Act of 1946, which said tax is levied according to and measured by its net income. Section 148.150 RSMo 1949, defines gross income as follows:

"Gross income" includes all gains, profits, earnings and other income of the taxpayer derived from sources within the state of Missouri, \* \* \*

and net income is defined by subsection 1 of said section to mean gross income minus certain allowed deductions.

There are no decided cases in the State of Missouri which construe this definition as it applies to these facts under the Credit Institutions Act. However, the Appellate Courts of this state have construed the language of the income tax statutes dealing with corporations, Sections 143.030-143.080, RSMo. 1949, which imposes a tax on their income "from all sources within this state." This language is so directly related to Section 148.150, RSMo. 1949, previously quoted, that the construction given the income tax wording by the courts must be considered.

Union Electric Company v. Coale, Mo. Sup., 146 S.W. 2d. 631, was a case in which the plaintiff taxpayer, a Missouri corporation, owned stock in foreign corporations from which it received dividends paid from funds derived from operations carried on and capital employed in the domicile states of the corporations paying the dividends, and none of the corporations either employed or had any capital in Missouri, nor carried on any operations or engaged in any business in Missouri during the taxable period. Defendants contend these dividends were taxable under the state income tax, and this suit was brought to abate that assessment. The court considered the word "source" as follows:

Mr. T. R. Allen

"Webster's New International dictionary, 2d Ed., defines source as 'that from which anything comes forth, regarded as its cause or origin; the first cause; the beginning; origin.' Also, source is defined as 'the individual, company, or corporation initiating a payment, as of dividends, interest', etc. Holmes' Federal Taxes, 6th Ed., p. 396, on the subject of source of income says: 'The word "source" conveys only one idea-that of origin. It is defined in the Standard dictionary as follows: "That from which any act, movement, or effect proceeds; a person or thing that originates, sets in motion, or is a primary agency in producing any course of action or result; an originator; creator; origin. A place where something is found or whence it is taken or derived." This is its natural, ordinary, and familiar meaning and it is particularly true that terms used in statutes describing objects of taxation should be construed according to their popular signification.'

The court then stated that the stock certificates belonging to the plaintiff in the foreign companies were nothing more than evidence of ownership "and neither the stock certificates nor the shares could be the source of the dividend income." In re Kansas City Star Company, Mo. Sup., 142 S.W. 2d 1029, was quoted: "The source of \* \* \* income is the place where it was produced" and that "taxing statutes should be construed strictly against the taxing authority unless a contrary legislative intent appears." The court concluded that it could not say that this income was produced in this state, and consequently it was held not to be taxable under the state income tax law.

Petition of Union Electric Company of Missouri, Mo. Sup. 161 S.W. 2d 968, involved the question of whether dividend and interest payments to a Missouri corporation by foreign corporations operating entirely outside the State of Missouri were income received by the taxpayer from sources within this state under the income tax statutes. The court at l.c. 970, 971, stated as follows:

"Income consists of an increase in the economic wealth of the taxpayer. The sources from which it is derived are said to be three: (A) labor; (B) the use of capital, in which term we include for

Mr. T. R. Allen

convenience land; and (C) profits derived from the sale or exchange of capital assets. These latter represent an accretion in the value of the assets while they are in the hands of the taxpayer. *Eisner v. Macomber*, 252 U.S. 189, 40 S. Ct. 189, 64 L. Ed. 521, 9 A.L.R. 1570; *Holmes*, *Federal Taxes*, 6th Ed., pp. 396 to 398. It is said that the locus of the source of income is determined as follows: In the case of income derived from labor, it is the place where the labor is performed; in the case of income derived from use of capital, it is the place where the capital is employed; and in the case of profits from the sale or exchange of capital assets, it is the place where the sale occurs. *In re Kansas City Star Co.*, 346 Mo. 658, 142 S.W. 2d 1029; *Holmes*, *Federal Taxes* (6th Ed.) pp. 396 to 398, *supra*.

\* \* \* \* \*

"It is also true that for many purposes the situs of personal property is considered to be at the domicile of its owner. This latter proposition, however, is purely fictitious and is now limited in its application to a few cases, principally those regarding the devolution of estates of decedents and bankrupts. *Eidman v. Martinez*, 184 U.S. 578, 22 S. Ct. 515, 46 L. Ed. 697; *Pullman's Palace Car Co. v. Pennsylvania*, 141 U.S. 18, 11 S. Ct. 876, 35 L. Ed. 613; *Ann.* 13 L.R.A. 741; 57 L.R.A. 523. The Income Tax Act, like all other tax statutes, must be construed as favorably as possible to the taxpayer and strictly against the taxing authority. *Artphone Corporation v. Coale*, 345 Mo. 344, 133 S.W. 2d 343; *F. Burkhart Manufacturing Co. v. Coale*, 345 Mo. 1131, 139 S.W. 2d 502. In the field of income taxation in particular it is important to penetrate beyond legal fictions and academic jurisprudence to the economic realities of the cases. It is conceded that the actual expenditure of labor and the actual use of capital which gave rise to the income represented by these dividends

Mr. T. R. Allen

took place outside the state of Missouri. We are forced to the conclusion therefore that the source of this income was outside the state and the dividends received by the taxpayer should not be included in its gross income for the purpose of computing its Missouri income tax. We believe that Division No. 1 of this court in the case of Union Electric Co. v. Coale, 347 Mo. 175, 146 S.W. 2d 631, supra, reached a proper conclusion. That conclusion is, we think, in complete harmony with the other recent decisions of this court and In re Kansas City Star Co., 346 Mo. 658, 142 S.W. 2d 1029, supra; Artophone Corporation v. Coale, 345 Mo. 344, 133 S.W. 2d 343, supra; and F. Burkhart Manufacturing Co. v. Coale, 345 Mo. 1131, 139 S.W. 2d 502, supra.

Further, in considering the interest payments on bonds of a foreign corporation held by the taxpayer in Missouri, the court, in the above case at l.c. 971 said:

"\* \* \*The nature and characteristics of interest payments cannot be changed by the fact that the debt upon which such interest is paid is evidenced by a bond. The character of the debt remains the same whether the fact of indebtedness is recorded in an instrument called a bond or in a promissory note or a mere open account. Nor is it of importance that the debtor is a corporation rather than an individual. The basic facts are these: That the taxpayer lent money to a person in another state which was used by that person in the other state and that the taxpayer, as an incident to such loan, was paid interest. It may be contended here that the interest was payable in Missouri because unless the parties to a contract otherwise agree all payments are to be made at the domicile or business place of the creditor. But an examination of the decisions previously cited shows that the actual place where income payments are turned over to the taxpayer is not determinative of the source of the income. For example, in the case of In re Kansas City Star Co., 346 Mo. 658, 142 S.W. 2d 1029, supra, the taxpayer's income consisted largely of the price of subscriptions to its

Mr. T. R. Allen

newspapers and money paid to it by advertisers. Most of these items would finally reach the hands of the taxpayer at its office in Missouri. Yet this court held that such portion of this income as was derived from transactions outside the state, that is from a sale of its publications outside of Missouri, was not taxable. Again a similar holding was made by the Board of Tax Appeals in the case of Appeal of Standard Marine Insurance Company, Limited, 4 B.T.A. 853, supra. These decisions and others like them make it plain that the mere point where payment reaches the hands of the taxpayer is not determinative of the source of the income. In the case of State ex rel. Manitowoc Gas Co. v. Wisconsin Tax Commission, 161 Wis. 111, 152 N.W. 848, supra, the Supreme Court of Wisconsin held that income paid in the form of interest by a Wisconsin corporation to bondholders in other states was not taxable in Wisconsin. We are unable to agree with the reasoning of this case, however. We think that the source of the income is the person paying the interest and not the mere bond itself, which is only an evidence of the indebtedness. It therefore follows that the interest payments must be treated in the same manner as the dividend payments, and what we have said in regard to dividends will largely apply also to interest."

In the request at hand the dance instruction is given entirely by the studios located in other states to students who reside in states other than Missouri. The students pay for the lessons with funds made in their individual callings in foreign states. The obligation is on the studios to furnish the dance instruction, and Educational Credit Bureau, Inc. assumes no responsibility therefor. The installment payments are made by the students through the mails, and if default is made the studio which entered into the contract with the student repurchases it. It is true that the Educational Credit Bureau, Inc. operates a going business based on the foregoing facts and that its places of business are located exclusively in Missouri. However, the determinative issue hinges on the wording of applicable statutes and the construction given them by the decided cases and the income tax statute and the construction placed on it by the cases quoted herein would seem to be determinative of the issue here involved. Probably the closest relationship between the decided cases and the situation involving the Educational Credit Bureau, Inc. was found in the case of Petition of Union Electric Company of Missouri, infra, concerning interest on bonds of a foreign corporation held in Missouri by this Missouri

Mr. T. R. Allen

corporation. The interest is payable on the bonds, irrespective of earnings, as are the payments on these installment contracts. The source of the income in that case was held to be the person paying the interest and not the bond itself, which the court said was only an evidence of the indebtedness. The source by analogy in the present situation is the person contracting with the Arthur Murray Dance Studios for the dancing lessons, who agree to pay therefor by installments without right of cancellation.

CONCLUSION

It is the opinion of this office that the installment payments received by Educational Credit Bureau, Inc., a Missouri corporation, from students located outside the State of Missouri for dancing lessons given by Arthur Murray Dance Studios in states other than Missouri are not to be included as income for the purpose of determining the tax of that corporation under the provisions of the Credit Institutions Act of 1946, since those payments do not constitute income "derived from sources within the State of Missouri," as provided by that act.

This opinion which I hereby approve was written by my assistant Mr. J. Robert Tull.

Yours very truly,

JOHN M. DALTON  
Attorney General

JRT:mw