TAXATION:
CREDIT INSTITUTIONS:
PARTNERSHIPS:

Par. 3, Sec. 148.150 RSMo 1949 of Credit Institutions Tax Act of 1946, construed by general rule of statutory construction. Read, construed and harmonized with subsequent uniform Partnership Act. Former law construed strictly against state; deduction of said statute construed strictly against taxpayer. Partnership Act prohibits parties from drawing salary, hence in arriving at net income taxable to partnership under Credit Institutions Tax Act, partners salaries not deductible under Par. 3; Sec. 148.150, thereof.

FILED

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August 25, 1952

8-29-52

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

Dear Sir:

Your recent request for a legal opinion of this department has been received and reads as follows:

"Re: Partnership operation
of credit institutions

"In the administration of the credit institution tax, a question has arisen with regard to the interpretation of the Law as set out in Section 148.150, Paragraph 3, R.S.Mo 1949, and a ruling is desired in connection with the interpretation of certain phraseology included therein with regard to a partnership operation, the taxpayer in the case involved being the A.B.C. Finance Company of Kansas City, Missouri, which is a partnership consisting of four partners.

"Two of these partners devote their full time to the running of the business and as payment therefor are paid $700 a month each. Taxpayer complains in studying the Act that they can find no distinction made between corporations or partnerships and the Act states that in computing net income, there is provided 'reasonable allowance for salaries and other compensation for <u>personal service actually rendered</u>.' (Underscoring ours)

"This Department has refused to permit the deduction herein referred to salaries to be claimed for partners as a deduction in arriving at net taxable income for

> the purpose of the credit institution tax. Taxpayer claims that to allow such a deduction to a corporation and not allow it to a partnership would be discriminatory. The contention of this Department is that a partner of any business may not draw a salary and that under the provisions of the Act that such an item could not be classified as ordinary and necessary expense paid or incurred by the taxpayer.
>
> "Will you kindly advise whether in your opinion such a deduction as herein referred to would be within the meaning of the Statute for the purpose of arriving at taxable income for credit institution tax."

The opinion request calls for an interpretation of paragraph 3 of Section 148.150, RSMo 1949, which is a part of what has been termed the "Credit Institutions Tax Act of 1946." This section allows the taxpayer certain deductions in computing net income subject to the tax, and reads as follows:

> "In computing net income there shall be allowed as deductions all ordinary, and necessary expenses paid or incurred by the taxpayer during the income period in carrying on its trade or business in the State of Missouri. Without limiting the generality of the foregoing there shall be allowed as deduction: A reasonable allowance for salaries and other compensation for personal services actually rendered; rents, repairs, bad debts and debts ordered to be charged off by the commissioner of finance; interest, cost of insurance and advertising; all taxes paid or accrued during the income period to the United States and all taxes paid or accrued on real estate to the state of Missouri or any political subdivision thereof; all contributions paid or accrued pursuant to the unemployment compensation law of Missouri; reasonable allowances for depreciation and depletion; armortization of premiums on bonds, debentures, notes or other securities or evidences of indebtedness; a reasonable allowance for payments or contributions to or on account of any pension or retirement fund or plan for its officers or employees; contributions to any corporation, association or fund organized and operated exclusively for religious, charitable, scientific, literary or educational purposes, no part of the net earnings of which inure to the benefit of any private shareholder or individual

> to an amount which does not exceed five per cent of the taxpayer's net income as computed without the benefit of this deduction; losses from the sale or disposition of any property, real or personal, tangible or intangible; and all other losses sustained during the income period not compensated for by insurance; provided, however, that deductions allowed to pawnbrokers shall be the same per cent of the total deductions allowable under this section as the total volume of their loan business bears to the total volume of their loan and merchandise business combined."

The opinion request does not state whether the salaries thus paid are in addition to the share of profits of the business to which these partners, along with the others are entitled, but it is assumed that the salaries are paid in addition to the share in the firm's profits received by the salaried partners.

The term "taxpayer" as used in above mentioned Credit Institutions Tax Act, has been defined by paragraph 6, Section 148.130 RSMo 1949, to mean any credit institution subject to the tax provided by said act, and the term "credit institution," has been defined by paragraph (2) of said section and reads as follows:

> "(2) The term "credit institution" means every person, firm, partnership or corporation engaged principally in the consumer credit or loan business in the making of loans of money, credit, goods, or things in action, or in the buying, selling, or discounting of, or investing in negotiable or non-negotiable instruments given as security for or in payment of the purchase price of consumer goods. Without limiting the generality of the foregoing, the term "credit institution" shall include persons, firms, partnerships, and corporations, operating or licensed under the small loan laws of this state, or under the laws of this state relating to loan and investment companies, and pawnbrokers, but shall not include banks, trust companies, credit unions, insurance companies, mutual savings and loan associations, savings and loan associations or real estate mortgage loan companies; * * *."

The courts have never passed upon the proposition embodied in your inquiry, and the meaning intended to have been given this section by the legislature will have to be determined by the general rules of statutory construction.

Mr. T. R. Allen

While taxing statutes are to be construed strictly against the taxing authority and liberally in favor of the taxpayer, it has long been the rule in Missouri that a taxpayer who claims to be entitled to an exemption from taxes has the burden of proving that he unmistakeably falls within the class of taxpayers specifically exempted from the payment of the taxes. This general rule was stated to be the law in the case of In Re: First National Safe Deposit Company 351 Mo. 423, in which the court said at l. c. 427:

> "It is the general rule that taxing statutes are to be strictly construed in favor of the taxpayer, and against the taxing authority; but this does not extend to exemption provisions of such statutes. The applicable rule in the latter connection is as stated in State ex rel. St. Louis Y.M.C.A. v. Gehner, 320 Mo. 1172, 11 S. W. (2d) 30: ' . . . no such exemption can be allowed, except upon clear and unequivocal proof that such release is required by the terms of the statute. If any doubt arises as to the exemption claimed, it must operate most strongly against the party claiming the exemption. . . . "Such statute and constitutional provisions are construed with strictness and most strongly against those claiming the exemption . . . . the burden is on the claimant to establish clearly his right to exemption." . . . " [See, also, State ex rel. Spillers v. Johnston, 214 Mo. 656, 113 S. W. 1083; 1 Cooley on Taxation (3d Ed.) 357-358.]"

(Underscoring ours.)

We cannot and do not agree with the taxpayer that the salaries of the partners are proper legal deductions against the tax, and that Section 148.150, supra, is broad enough to include such deductions. It is obvious that in construing paragraph 3 of this section the legislature never intended it to have the meaning ascribed to it by the taxpayer, for to construe it thus, one must necessarily presume that the legislature was ignorant of the laws pertaining to partnerships at the time of the enactment of said section. One must also presume that the legislature subsequently passed the Uniform Partnership Act, certain provisions of which (to be hereinafter noted), were intended to be in conflict with Section 148.150 supra, if the interpretation placed upon said section by the taxpayer is correct.

One cannot presume that the legislature did not know the law pertaining to partnerships, or of taxation at the time of the passage of the section under consideration, for such presumption would be in conflict with certain well established principles of law to the contrary. Regarding presumptions, the St. Louis Court of Appeals, in the case of Sikes v. St. Louis & S.F.R. Co., 127 Mo. App. 326, at l. c. 334, said:

> "In examining this statute and seeking to arrive at the legislative intention therein manifested, we must do so with the knowledge that <u>the Legislature is presumed to know the existing state of the law relating to subjects with which they deal at the time they act on a given question, and therefore are deemed to have dealt with the matter in the light of the state of the law then existing. * * * *"</u>
>
> (Underscoring ours)

Therefore, we must presume that the legislature knew the laws pertaining to taxation at the time of the passage of Sectión 358.180 supra, and did not intend that the Uniform Partnership Act, should be in conflict with any of the previously established principles of law pertaining to taxation or of partnerships, particularly the provisions of the Credit Institutions Tax Act.

In Missouri, a partnership has long been recognized as a contractual relationship between two or more competent persons by which they pool their money, effect, labor, skill, some or all of them into a business and divide the profits and bear the losses in certain proportions.

It is apparent that in the legal contemplation, of partnerships, a partner is an owner, and, in a general partnership, such as the one mentioned in the opinion request, each partner is authorized to act for the partnership and to bind the firm within the scope of its business. The individual partners are the owners, and aside from them the partnership has no separate existence, and is not a legal entity. This principle of law was decided in the case of Chambers v. Macon Wholesale Grocer Co. et al., 70 S.W. (2d) 884. We quote from a portion of the opinion found at l.c. 889:

> "* * * * That a partner is solely an owner and employer, and not an employee, within the meaning of our act, would seem to be true from the very nature of a partnership as well as from the terms of the act. <u>A partnership is not an entity apart from the individuals composing it</u>. 47 C. J. 947, Sec. 457; 20 R.C.L. 799-806, Secs. 1-6. Certainly no one would contend that a partner who was injured

by some defective condition of partnership property or by negligence of a partnership employee could recover from the other partners, who did not participate directly in the act, for the fault would be his as much as theirs. The partners own the property and the business individually just the same as if one of them owned it all, although their ownership is subject to the rights of all. 47 C. J. Secs. 176, 188, 805; 20 R.C.L. 850, Sec. 56; 20 R.C.L. 870, Sec. 81. There is a difference, however, between mere joint ownership of property and partnership ownership (20 R.C.L. 806, 807, Secs. 7, 8), and that is the distinction between the Ellis Case and sharp v. Carswell, S. C. 391, 47 S. L. R. 335, 3 B.W.C.C. 552, cited by respondent. 'A partner cannot maintain an action at law against his copartners for services rendered or for premises leased to the firm, although the partnership agreement secures to him a fixed sum therefor; * * *nor for money loaned to or paid for the firm'; because 'it would be useless for one partner to recover what, upon taking a general account among all the partners he might be liable to return'; and because 'such transactions do not result in one partner becoming a debtor to or creditor of the others.' Burdick on Partnership,333. Accordingly, the remedy of a partner is an action in equity for an accounting whereby he is entitled to have his claim considered in the distribution of the partnership property. 47 C.J. 802, Sec. 250; 20 R.C.L. 873, Sec. 84, 924, Sec. 139. Even a cause of action against third persons is a partnership asset, and all partners must ordinarily join in the suit. 20 R.C.L. 920, Secs. 132, 133.

"Besides the partner's personal ownership of the business, in all partnership affairs, each partner acts, or has authority to act, both as principal for himself and as agent for the other partners, while an agent, servant, or other employee does not act for himself but for his principal alone; an agent being employed to bring about contractual relations between his principal and third persons, not between such persons and himself, while a servant is employed only to deal with things on behalf of and as directed by his master, not for his own purposes. 2 C. J. 423 and 425, Secs. 9

> and 12; 20 R.C.L. 882, Sec. 94. It would therefore seem evident that, as the Ellis Case so well states, whether a partner receives only a fixed share of profits or, because he puts in more of his time than the others advancing their joint activities, 'receives sums which are called wages, it really does not create the relation of employers and employed, but is, in truth, a mode of adjusting the amount that must be taken to have been contributed to the partnership assets by a partner who has made what is really a contribution in kind, and does not affect his relation to the other partners, which is that of co-adverturer and not employee.
> * * * * * * * * * * * * * * * * "

We also quote paragraph 6, Section 358.180, giving the rules for determining the rights and liabilities of general partners under Uniform Partnerships Law, RSMo 1949, which provides that no partner can be paid a salary for his services in performing partnership business, and reads as follows:

> "No partner is entitled to remuneration for acting in the partnership business, except that a surviving partner is entitled to reasonable compensation for his services in winding up the partnership affairs;"

The interpretation of Section 148.150 by the taxpayer cannot be given effect, for to do so would be to nullify the provisions of the Uniform Partnership Act quoted above, and such an interpretation would be unreasonable and contrary to the intention of the legislature in the passage of Section 148.150, supra. Said section was passed by the Sixty-fourth General Assembly, while the Uniform Partnership Act was passed by the Sixty-fifth General Assembly. The quoted portion of the partnership law clearly states that a partner shall not receive any remuneration for performance of partnership business except he shall be entitled to reasonable compensation for his services in winding up the partnership affairs.

We do not believe there is any conflict between the provisions of the two statutes noted above, nor do we believe that the legislature intended there should be any conflict between the two. However such a conflict would unavoidably be the result if the interpretation of Section 148.150 supra, given by the taxpayer is correct. In determining the actual intention of the legislature in the passage of Section 148.150 supra, and placing the proper construction on the section thus intended, it is our thought that said section should not be read alone but that it should be read along with Section 358.180, with a view of harmonizing and giving effect to both sections. This theory was held to be one of the guiding maxims to be observed in interpreting seemingly conflicting statutes in the case of McGill v. City of St. Joseph, 38 S.W. (2d) 725, in which the court said at l. c. 727-728:

> "In the case Kane v. Kansas City, Ft. S. & M. Ry. Co., 112 Mo. 34, 39, 20 S.W.532, 533, the court said: 'It is a recognized rule of rational interpretation of laws that, where two interfere in their application to particular facts, we should follow that which is recommended by the most beneficial reasons. * * * It is proper to inquire into the consequences of any proposed interpretation of a law in determining what was the probable intention in its enactment. * * * That the letter of a statute must occasionally be cut down to conform to its evident spirit and intent is a maxim of interpretation which is not new in Missouri.' In the interpretation of laws, it is the duty of all courts to ascertain the intention of the lawmaking power. 'To gather that intention, the courts are not confined exclusively to the consideration of the immediate statute in question, but many look to other legislation in part materia.' Manker v. Faulhaber, 94 Mo. 430, 442, 6 S.W. 372, 376. A statute should not be construed as if it stood alone and complete in itself. Glaser v. Rothschild, 221 Mo. 180, 120 S.W. 1, 22 L.R.A. (N. S.) 1045, 17 Ann. Cas. 576. And, where two statutes are susceptible of a construction that will give force to both, they must be so construed. State ex rel.v. Clayton, 226 Mo. 292, 126 S.W. 506."

CONCLUSION

It is the opinion of this department that in arriving at the net income of a partnership subject to taxation under the Credit Institution Tax Act, the amount paid to partners for managing the firm's business is not an ordinary, necessary and reasonable expense incurred by the partnership for personal services within the meaning of paragraph 3, Section 148.150 of said Act, and is not allowable as a deduction thereunder.

Respectfully submitted

PAUL N. CHITWOOD
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APPROVED:

J. E. TAYLOR
ATTORNEY GENERAL

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