

TAXATION:
BANKS AND BANKING:
FRANCHISE TAX
PREFERRED STOCK HELD
BY RFC:

Preferred stock of a bank owned by the Reconstruction Finance Corporation constitutes a part of the capital structure of such bank upon which the franchise tax may be based.

August 20, 1938

4-73

Mr. Richard Chamier
Prosecuting Attorney
Randolph County
Moberly, Missouri



Dear Sir:

Yours of June 27, 1938, and of July 19, 1938, pertaining to the franchise tax of The City Bank & Trust Company of Moberly, Missouri, have been referred to me for attention.

From your letters, I find that the question involved is the right of the State Tax Commission to assess the entire capital stock of a corporation for franchise tax when a part of the capital structure of such corporation is represented by preferred stock which is owned by the Reconstruction Finance Corporation.

The franchise tax is assessed and levied by the Tax Commission by virtue of the provisions of Section 4641, R. S. Mo. 1929, which is as follows:

"For the taxable year of 1929 and thereafter every corporation organized under the laws of this state shall, in addition to all other fees and taxes now required or paid, pay an annual franchise tax to the state of Missouri equal to one-twentieth of one per cent of the par value of its outstanding capital stock and surplus, or if the capital stock of such corporation or any part thereof consists of no par value stock, then in that event, for the purposes herein contained such stock shall be considered as having a value of

\$5.00 per share unless the actual value of such shares should exceed \$5.00 per share, in which case the tax shall be levied and collected on the actual value and the surplus. If such corporation employs a part of its capital stock in business in another state or country, then such corporation shall pay an annual franchise tax equal to one-twentieth of one per cent of its outstanding capital stock and surplus employed in this state, and for the purposes of this article such corporation shall be deemed to have employed in this state that proportion of its entire outstanding capital stock and surplus that its property and assets in this state bears to all its property and assets wherever located. Every corporation not organized under the laws of this state, and engaged in business in this state, shall pay an annual franchise tax to the state of Missouri equal to one-twentieth of one per cent of the par value of its capital stock and surplus employed in business in this state, or if the capital stock of such corporation or any part thereof consists of no par value stock, then in that event, for the purposes herein contained, such stock shall be considered as having a value of \$5.00 per share, unless the actual value of such shares should exceed \$5.00 per share, in which case the tax shall be levied and collected on the actual value and the surplus, and for the purposes in this article such corporation shall be deemed to have employed in this state that portion of its entire capital stock and surplus that its property and assets in this state bears to all its property and assets wherever located: Provided, that this law shall not apply to corporations not organized for profit, nor to express companies, which now pay an annual tax on their gross receipts in this state, and insurance companies, which pay an annual tax on their gross premium receipts

in this state: Provided, bank deposits shall be considered as funds of the individual depositor, left for safe-keeping and shall not be considered in computing the amount of tax collectible under the provisions of this article. If this provision, exempting bank deposits shall be declared unconstitutional by the courts, then the legislature hereby declares that it is the intention that the remainder of this article shall be in full force and effect and further declaring that it would have passed this article irrespective of the said exempting provision."

Banking institutions are authorized to issue preferred stock by authority of Section 1, Laws of Missouri, 1933, page 406, which is as follows:

"Notwithstanding any other provision of the laws of this State governing the organization, incorporation, management, and control of corporations, and more particularly the organization, incorporation, management, and control of banks, trust companies doing a banking business, and other financial institutions organized, incorporated, and existing, under the laws of this State and subject to the jurisdiction of, and control by, the Finance Commissioner of the State of Missouri, any such corporation may, with the consent of all its stockholders, issue and sell its shares of preferred stock, of one or more classes, subject to the provisions of this act and the approval of the Finance Commissioner of the State of Missouri. Wherever the term 'corporation' is used in this Act, it shall be held to mean any trust company doing a banking business or banks in the state of Missouri."

Section 2 of said Act, Laws of Missouri, 1933, page 407, provides that the preferred shares of stock of a banking corporation may be issued as a part of the existing capital of the existing corporation or as an increase of its capital. In either event, such preferred stock is a part of the capital structure of the corporation issuing same and upon which the franchise tax is to be based.

It is because the Reconstruction Finance Corporation holds the preferred stock that the bank seems to claim such stock should not be included in the capital structure of the bank for the purpose of levying the franchise tax.

The Reconstruction Finance Corporation was organized January 22, 1932, by Act of Congress, Title 15, Section 81, U. S. Code Annotated, page 69, 1934 Cumulative Pocket Part. Section 602 of said Act provides that the capital stock is owned by the United States.

Section 10 of the Reconstruction Finance Corporation Act, page 86, provides in part as follows:

"The corporation, including its franchise, its capital, reserves and surplus, and its income, shall be exempt from all taxation now or hereafter imposed by the United States or by any territory, dependency, or possession thereof, or by any state, county, municipal or local taxing authority; except that any real property of the corporation shall be subject to state, territorial, county, municipal, or local taxation to the same extent according to its value as other real property is taxed."

An instrumentality or agency of the United States Government, being wholly owned by the United States, is not subject to taxation without the consent or express legislation of Congress. In *United States v. Coghlan*, 261 Fed. 425, 426, the United States District Court of Maryland said:

"It was shown that all the stock of the Fleet Corporation was owned by the government, and that all it did was done for government account, and that all the profits

which it made would inure to the government, which would have to stand all the losses. Under such state of facts, it is unnecessary to inquire whether for all purposes the Fleet Corporation is the government. It suffices that it is a governmental agency, exclusively employed in governmental work, and as such its property is not liable to state taxation."

On the question of deducting from the returns for the assessment of the franchise tax for the bank the amount of preferred stock owned by the Reconstruction Finance Corporation, we find that the Supreme Court of the United States has held that a state statute could assess to the stockholders shares of stock in a bank and measure the value of such shares by assets from exempt property. In the case of *Des Moines National Bank v. Fairweather*, 263 U. S. 103, (1923), the court said:

"The next contention--that the statute subjects securities of the United States to taxation contrary to exempting laws of the United States, in that it requires that the assessment be based on the aggregate of the capital, surplus, and undivided earnings, without any deduction or allowance on account of the investment in such securities--confuses the shares, which are the property of the stockholders, with the corporate assets, which are the property of the bank. It is quite true that the states may not tax such securities, but equally true that they may tax the shares in a corporation to their owners, the stockholders, although the corporate assets consist largely of such securities, and that in assessing the shares it is not necessary to deduct what is invested in the securities. The difference turns on the distinction between the corporate assets and the shares,--the one belonging to the corporation as an artificial entity and the other to the stockholders."

By your letter of July 19, 1938, you state that the bank thinks that there is a distinction between capital stock notes and preferred stock notes when same are held by the Reconstruction Finance Corporation. Capital stock notes and preferred stock both go in to make up the capital structure of the bank. Both are issued to increase the capital structure of such institution.

In the case of *Hilson County v. State Board of Assessors*, 82 N. J. 2, l. c. 4, the court in discussing debentures, which are similar to capital notes, which were issued by the bank, said:

"I have no doubt that the act of the State Board of Assessors in treating these certificates as representing a part of the outstanding stock of the corporation for the purpose of determining the amount of franchise tax to be assessed against it was proper notwithstanding the fact that the certificates in their form exhibit a dual character, namely, a certificate of indebtedness and a certificate of stock ownership."

In the case of *Kansas City Ry. Co. v. Kansas*, 60 L. Ed. 617, 240 U. S. 227, 232, the court in discussing franchise tax, said:

"In examining the statute in the present case, we see no reason to doubt the accuracy of the description of the tax by the state court. We take it to be simply a tax on the privilege of being a corporation,--on the primary corporate franchise granted by the state. The authority of the state to tax this privilege, or franchise, has always been recognized, and it is well settled that a tax of this sort is not necessarily rendered invalid because it is measured by capital stock which in part may represent property not subject to the state's taxing power."

In the case of Home Ins. Co. of New York v. People of the State of New York, 33 L. Ed. 1025, the Supreme Court of the United States held:

"Where a state statute imposes a tax upon the 'corporate franchise or business' of a company, and reference is only made to its capital stock and dividends for the purpose of determining the amount of the tax to be exacted each year, this is not a tax on the capital stock or property of the company, but upon its corporate franchise, and is not therefore subject to the objection that it is a tax on United States securities, although a portion of its capital stock is invested in such securities.

"By the term 'corporate franchise or business,' as here used, is meant the right or privilege of being a corporation, that is, of doing business in a corporate capacity.

"The validity of the tax can in no way be dependent upon the mode which the State may deem fit to adopt in fixing the amount for any year which it will exact for the franchise. Its action in this matter is not the subject of judicial inquiry in a federal tribunal.

"The taxation of a corporate franchise has no limitation but the discretion of the taxing power, and its value is not measured like that of property, but may be fixed at any sum that the Legislature may choose.

"Such tax cannot be affected in any way by the character of the property in which its capital stock is invested."

From the foregoing authorities, it is evident that it makes no difference who owns the stock, whether preferred, common, or capital notes, of a corporation in considering

the franchise tax of such corporation. The tax is based upon the amount of stock outstanding, regardless of its ownership. The tax is against the corporation for the privilege of doing business. This tax is not a property tax. It is in the nature of an excise tax.

CONCLUSION

From the foregoing, it is the opinion of this department that preferred stock of a banking corporation which is owned by the Reconstruction Finance Corporation or any other governmental agency shall be considered as representing stock issued and outstanding for the purpose of determining the amount of the franchise tax assessable against such corporation.

Respectfully submitted

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Assistant Attorney General

APPROVED:

J. E. TAYLOR
(Acting) Attorney General

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