



'BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of }
MAGALIA MINING COMPANY }

Appearances:

For Appellant: **McCutchen**, Olney, **Mannon** and Greene,
San Francisco
For Respondent: Reynold E. Blight, Franchise Tax Commis-
sioner; Frank L. Guerena, San Francisco

O P I N I O N

This is an appeal, pursuant to Section 25 of the California Bank and Corporation Franchise Tax Act (Chap. 13, Stats. 1929), from the action of the Franchise Tax Commissioner in overruling the protest of Magalia Mining Company against a proposed assessment of the minimum tax, with interest.

The facts are not controverted. The Appellant has engaged in no activity either within or without the State of California for more than the last twenty years, other than the holding of the annual corporate meetings necessary to preserve its existence. No income or revenue from any source whatever has accrued to the company, and all its taxes and incidental expenses have been met from fund remaining on hand as the result of business done more than twenty years ago, or by contributions from stockholders. The only property of the company within or ~~without~~ the State of California is certain mining property located in Butte County, acquired in 1894, and not operated, leased or in any way utilized during the last twenty years.

It is the contention of the Appellant that under these facts, it is not "doing business within the limits of this State", and, consequently, is not taxable under the Bank and Corporation Franchise Tax Act, (Supra). It is the view of the Franchise Tax Commissioner that the Appellant is "doing business" within the meaning of the Act, and, therefore, is liable for at least the minimum tax. The determination of this appeal devolves consequently, upon the definition to be given to the term "doing business" as found in Section 4 of the Act.

The constitutional provision under which the tax contemplated by the Act is imposed, is in part as follows:

"All financial, mercantile, manufacturing and business corporations doing business within the limits of this state subject to be taxed pursuant to subdivision (d) of section 14 of this article, in lieu of the tax thereby provided for, shall annually pay to the state for the privilege of exercising their corporate

Appeal of Magalia Mining Company

franchises within this state a tax according to or measured by their net income." (Const. Art XIII, Sec. 16, Par. 2.)

There is further provision that the Legislature shall define what constitutes "doing business". (Const. Art. XIII, Sec. 16, Par. 5.)

In Section 5 of the Act there is the following:

"The term 'doing business', as herein used, means any transaction or transactions in the course of its business by a corporation created under the laws of this state, or by a foreign corporation qualified to do or doing intrastate business in this state."

As observed by the Attorney General of California in the course of an opinion rendered to the Franchise Tax Commissioner on November 15, 1929:

"The definition is not an apt one as it employs the very words which it seeks to define; therefore, practically no assistance is given us by the definition itself, and our conclusion must in the end be based upon the interpretation given by the courts, especially of our own state, to the words 'doing business'".

In this same opinion the Attorney General points out that there are only a few cases in California which throw any light on the matter. Under our former method of corporate franchise taxation the doing of business was not made the test of taxability of a domestic corporation, as the possession of a franchise to be was sufficient to subject the company to assessment by the State Board of Equalization. (Const. Art. XIII, Sec. 14, Sub. (d); Political Code, Sec. 3664d)

The kinds of corporations specified in Section 4 of the Bank and Corporation Franchise Tax Act (Supra), i.e., financial, mercantile, manufacturing and business, are taxable if they "do business" within California. Section 5 of the Act, above quoted, provides that a corporation is "doing business" if it engages in any transaction or transactions in the course of its corporate purpose, that is, in the course of its business. Thus, under this definition, regardless of the kind of corporation, any act done to further its purpose is "doing business", although such "doing business" makes the corporation subject to taxation only if the act done furthers a corporate purpose classified as "financial," "mercantile," "manufacturing," or "business" within the meaning of Section 4.

From the California cases relating to the question of whether or not certain corporate activity constitutes doing business we deduce that the character of an act in furtherance of a corporate purpose is determined, not by the nature of the act itself, but by the nature of the corporate purpose it serves. (Silveira v. Associated Milk Producers, 63 Cal. kpp. 572; General Conference of Free Baptists v. Berkey, 156 Cal. 466; Finance and

Appeal of Magalia Mining Company

Construction Co. of Cal. v. Sacramento, 76 Cal. Dec. 73)

Authorities construing the term "doing business" as used in state statutes prescribing requirements as conditions precedent to the right of a foreign corporation to do business within the state are not directly in point, as they involve simply the question whether the corporation is "doing business" at a particular place. For the purpose of determining whether a domestic corporation is "doing business" and, therefore, taxable under the Bank and Corporation Franchise Tax Act, cases arising under Federal Statutes are more helpful. With reference to federal corporate excise and capital stock taxes, taxability of a corporation has turned upon the question of whether it was "doing business" at all during the tax year. (36 Stat. at L. 112; 39 Stat. at L. 789; 40 Stat. at L. 1126; 42 Stat. at L. 294; 43 Stat. at L. 324). This determination seems directly analogous to the problem now confronting us.

In the case of Jasper & E. Ry Co. v. Walker, 238 Fed. 533, 537, the United States Circuit Court of Appeals has said:

"The expression ("engaged in business") is one in common use. It has the same meaning, whether applied to a corporate or to a natural person. It is not apt or appropriate to describe one who has retired from business in which he had engaged and confines his activities to maintaining property let to another and used exclusively by the lessee in carrying on that business.

Clearly, mere possession of a franchise-to-be does not make the Appellant subject to the tax, (Fore River Shipbuilding Corporation v. Commonwealth (Mass) 142 N. E. 812). To maintain that franchise it must hold annual corporate meetings, but these cannot be regarded as "doing business" otherwise the effect of the law would be to accomplish by indirection what cannot be done directly, i. e., to tax a corporation as "doing business" for the bare retention of its corporate charter or franchise. There remains, then, the question of whether or not ownership by a mining corporation of real property situated in California, acquired years ago in connection with the company's mining activities, but now wholly in disuse, constitutes "doing business

The United States Circuit Court of Appeals has held that a corporation which is organized to deal in property, real and personal, and which merely holds title to a tract of land, paying taxes thereon, and employing agents to make sales, not in fact made, is not engaged in business. (Lane Timber Co. v. Hynson, 4 Fed. (2nd) 66, 40 A. L. R. 1448). This case involved the construction of the term "doing business" within the meaning of the Federal Revenue Act of 1919 (40 Stat. at L. 1126), and, as we have already observed, the provisions of that law and ours with respect to this term are analogous.

Discussing the issue the Court said:

"Plaintiff (Lane Timber Co.) contends that it was not engaged in business during that year, and, consequently, that it

Appeal of Magalia Mining Company

was not liable for the tax. Whether or not it was so engaged is the only question in the case.

"It is defendant's contention that a corporation which does what its charter authorizes it to do is liable for the **corporatic tax**, and that the plaintiff, because it was authorized to hold **title** to the land and was **doing** so with the expectation of selling at a profit, was engaged in business. If a corporation is not engaged in business? it cannot make any difference that what it is doing is authorized by its charter. Owning land is not doing business, nor is paying taxes, Most owners of land, whether corporations or individuals, would be **willing to sell** at a profit."

Finding support for this view in the decisions of the United States Supreme Court in the cases of Flint v. Stone Tracy 220 U. S. 107; McCoach v. Minehill & S. H. R. Co. 228 U. 295, and Von Baumbach v. Sargent Lumber Co., 242 U.S. 503, the Court concluded that the Lane Timber Co. was not "doing business. In particular, it relied upon the rule expressed in the Von Baumbach case as follows:

"The fair test to be derived from a consideration of all of them is between a corporation which has reduced its activities to the owning and holding of property and the distribution of its-avails and doing only the acts necessary to continue that status, and one which is still active and is maintaining its organization for the purpose of continued efforts in the pursuit of profit and gain and such activities as are essential to those **purposes.**"

Citing all of these holdings, the United States District Court has epitomized the problem thus:

"These cases establish that this tax is laid, not on the existence of the corporation, but on its activities as such. The charter powers and purposes may be considered in determining whether the corporation is in business or out of business, but the use rather than the existence of corporate powers is the true point. If the only substantial corporate activity is the ownership and preservation of real and personal property, the receipt of its ordinary income, which arises from the property itself, rather than from active use and management of it, and the distribution of such income to the stockholders, with only such corporate organization and activity as is necessary thereto, there is not such a doing of business as is meant by the act. While such activity is "business" in a broad sense, a tax upon such **business** would be in substance one **on** the mere ownership of property, becoming thus a direct tax and beyond the power of Congress, **except** when apportioned to the **states** according to population." (Nunnally Inv. Co. v. Rose, 14 Fed. (2nd) 189.)

Particularly illuminating is the recent holding of the United States Circuit Court of Appeals with reference to Hotchkiss Redwood Company, a California corporation, owning a large tract of timber in Del Norte County, acquired in 1906 by its predecessor, Hotchkiss Timber Company. Both companies held the

Appeal of Magalia Mining Company

timber land for the sole purpose of owning and holding the same and reselling it as a whole for profit. The transfer from one corporation to the other was effected in 1919.

Mr. Justice Rudkin reviewed the situation in the following language:

"Since its organization the new company has from time to time levied and collected assessments on its capital stock to pay taxes, interest on its **bonded indebtedness**, and other necessary charges and expenses; to avoid condemnation proceedings, it sold a strip of land to Del Norte **County** for highway purposes for approximately \$5,000; from November, 1919, to June, 1923, it paid the sum of \$50 per month as salary to its secretary, and from July, 1923, to June 30, 1924, the president was paid the sum of \$150 per month on account of office expenses it has at all times maintained its corporate existence, and from time to time **has** carried on negotiations through its president with prospective purchasers and brokers, looking to the sale of its lands as a whole, but no person or agent has been employed for that purpose, the land has never been advertised for sale, and no part of it has been sold, except the right of way to Del Norte **County**. Such, in brief, were the activities of the corporation from the time of its organization up to June 30, 1924.

"The present action was instituted by the corporation against the United States to recover taxes imposed and **collected** under the Revenue Acts of February 24, 1919, and November 23, 1921 (40 Stat. 1126; 42 Stat. 294), for the tax year ending June 30, 1924, and for the four **years** immediately preceding. The plaintiff had judgment below, and the United States sued out the present writ of error. The sole question presented for decision is: Was the defendant in error carrying on or doing business during the period in question, within the meaning of the Revenue Acts? If so, the judgment should be reversed; otherwise, it must be affirmed.

"The mere substitution of one mortgage or one form of indebtedness for another, the levy of stock assessments to pay taxes and interest, the maintenance of corporate existence, the sale of a right of way for a public road to avoid **condemnation** proceedings, and the payment of nominal salaries to the **secretary** and president, did not, without more, constitute carrying on or **doing** business, within the meaning of the law. Of course, we must judge the activities of the corporation as a whole; but, if it was not carrying on or doing business because of the **activities** mentioned, it has done nothing else, and was not subject to the tax, unless, as contended by the government, every corporation organized for the purpose of holding property for gain or profit is doing business, regardless of its other activities.

"As said by the Circuit Court of Appeals of the Second Circuit, in Eaton v. Phoenix Securities Co., 22 F. (2d) 497: 'We do not think that anything will be gained by an extended discussion of * * * this tangled subject.' Suffice it to say

Appeal of Magalia Mining Company

that, under the authority of Zonne v. Minneapolis Syndicate, 220 U.S. 187, 31 S. Ct. 361, 55 L. Ed. 428, McCoach v. Minehill & Schuylkill Haven R. Co., 228 U. S. 295, 33 S. Ct. 419, 57 L. Ed. 842, and United States v. Emery, Bird, Thayer Realty Co., 237 U. S. 28, 35 S. Ct. 499, 59 L. Ed. 825, we are of opinion that the defendant in error was not carrying on or doing business during the period in question within the meaning of the law.

"Von Baumbach v. Sargent Land Co., 242 U. S. 503, 37 S. Ct. 201, 61 L. Ed. 466, Edwards v. Childs Corp., 270 U. S. 452, 46 S. Ct. 345, 70 L. Ed. 678, and Phillips v. International Salt Co., 274 U. S. 718, 47 S. Ct. 589, 71 L. Ed. 1323, are not in conflict with the earlier decisions. although they rather indicate that the rule of exemption will not be extended. See, also, Lane Timber Co. v. Hynson (C. C. A.) 4 F. (2d) 666, 40 A. L. R. 1448; Cannon v. Elk Creek Lumber Co. (C. C. A.) 8 F. (2d) 996; United States v. Three Forks Coal Co. (C. C. A.) 13 F. (2d) 631; Rose v. Nunnally Investment Co. (C. C. A.) 22 F. (2d) 102."

A similar view has been expressed with direct reference to a mining company such as the Appellant. Fink Coal & Coke co., organized under the laws of West Virginia in 1902, was authorized under its charter to engage in the following activities:

"The purchase and holding of real estate and sale of the same; the mining and shipping of coal; the manufacture of coal into coke and other products, and marketing the same; the building of houses and other buildings for the accommodation of employees and others; the constructing and laying of sidings, turnouts, and switches for connecting their work with railroads the' constructing and maintaining magnetic telegraph and telephor lines between its works and other points.; the establishing of gas and water works; the manufacture of electricity from coal or other materials; the carrying on of mercantile business."

The taxes in controversy were federal capital stock taxes for the years 1919 to 1925. During that period the corporation owned about 10,000 acres of coal land in West Virginia, but as found by the Court:

"The sum total of the activities of the company during the taxable years 1919 to 1925, inclusive, consisted of the yearly meetings of the directors and stockholders, and the assessment of the stockholders to meet the expenses of the company. The expenses consisted of the payment of taxes, the payment of salaries of \$100 and \$15 yearly to its treasurer and secretary, respectively, and the payment for printing and postage in connection with letters relevant to the assessment of the stockholders. The company maintained no office. Its books consisted of a minute book, an individual ledger containing the account with each stockholder, a bank book and a check book. At the directors' and stockholders' meetings no business was transacted other than the election of officers, the reading of the treasurer's report, and the annual assessment upon the stockholders, and, in several meetings, the authorization to option the

Appeal of Magalia Mining Company

properties mentioned, supra.

"During the period for which taxes were collected by the defendant, the stockholders of plaintiff company hoped---possibly expected---that conditions would change at some future time, and by that change they might be able to mine their coal, or sell their coal lands, at a profit." (Fink Coal & Coke Co. v. Heiner, 26 F. (2d) 136.)

The Court went on to say that:

"The accepted definition of 'business,' as used in the taxing statute, is:

"That which occupies the time, attention and labor of men for the purpose of a livelihood or profit. Corporation Tax Cases, 220 U. S. 107, 31 S.Ct. 361, 55 L. Ed. 428."

After extended analysis of the decisions of the United States Supreme Court on the subject, the District Court concludes that:

"Nowhere has that court laid down the proposition that control over the property held must be gone before the corporation may claim release from the tax." (Page 138)

The court referred with approval to the holding in Lane Timber Co. v. Hynson, supra, and directed attention to the similarity between that case and the Fink Coal & Coke Co. case.

Dismissing the contention that any of the earlier Cases had been overruled by Edwards v. Chile Copper Co., 270 U. S. 452 the court said:

"The Chile Copper Co. Case, with its intimation just quoted, unquestionably tends to limit the number of corporations 'not engaged in business.' But it is a case treating of the association of two corporations which was not the ordinary relation between a parent organization and a holding company, and was not designed to overturn all previous decisions of the court and the principles therein set forth. In the opinion Mr. Justice Holmes, for example, cites the Emery, Bird, Thayer Case, and distinguishes it, but does not overrule it. The decision would be unduly extended if it were to be held that it sets aside the declaration in Flint v. Stone Tracy Co., 220 U. S. 107, 31 S. Ct. 342, 55 L. Ed. 389, Ann. Cas. 1912B 1312, repeated in McCoach v. Minehill Railway Case, to the effect that the corporation tax was not imposed upon the franchises of the corporation irrespective of their use in business, nor upon the property of the corporation."

The court determined that Fink Coal & Coke Co. was not doing business, saying:

"In view of the fact that the testimony shows that the plaintiff company, during the taxable periods for which tax was

Appeal of Magalia Mining Company

paid, did not pursue its prime purpose of mining and marketing coal, and did not engage in any activity whatsoever other than the maintenance of its corporate existence and its ownership of property, it is our opinion that the plaintiff is entitled to judgment for the amount claimed in its statement."

Desirable as "broad general policies" for the administration of the office of the Franchise Tax Commissioner may be, these should never be used as a guise for taxing any citizen except under specific statutory authority. Such procedure would be repugnant to our fundamental conception of American government, and would deprive citizens of their constitutional right not to have their property taken save by due process of law. Whether or not the requirement that a corporation must be "doing business" before the State can tax it is a wise provision we are not called upon to decide. If, perchance, its enforcement seriously curtails state revenues, much as we might regret the consequences, we should not be justified in nullifying the requirement.

In an opinion to the Franchise Tax Commissioner, dated November 26th, 1929, and supplemental to the opinion of November, 15th, 1929, already mentioned, the Attorney General has advised that the acquisition by a corporation of property essential to its primary purpose is "doing business". With this view we are in complete agreement, but we do not understand the Attorney General to advise that the acquisition of lands in 1894 constitutes "doing business" now. Certainly, such an interpretation of the law would do violence to the numerous authorities which we have reviewed above and would be without support of any decision brought to our attention.

It has been many years since Magalia Mining Company has acquired any property, save possibly office supplies, or the like, indispensable to maintenance of its bare corporate existence. Consequently, we do not apprehend that the Attorney General meant to advise that its acquisition thirty-five years ago of mining property, now in disuse, would involve liability today for the privilege of "doing business."

We conclude that the Appellant is not "doing business" within the meaning of the Bank and Corporation Franchise Tax Act, and, therefore, is not subject to taxation thereunder.

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 Reynold E. Blight, Franchise Tax Commissioner, in overruling the protest of Magalia Mining Company, a corporation, against a proposed assessment of the minimum tax and interest thereon under Chapter 13, Statutes of 1929, be and the same is hereby reversed, Said ruling is hereby set aside and said Commissioner

Appeal of Magalia Mining Company

is hereby directed to proceed in conformity with this order.

Done at Sacramento, California⁴ this 7th day of January,
1930, by the State Board of **Equalization**.

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

ATTEST: Dixwell L. Pierce, Secretary