



STATE OF KANSAS

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**Curt T. Schneider**  
Attorney General

December 18, 1975

ATTORNEY GENERAL OPINION NO. 75- 462

The Honorable Elwill M. Shanahan  
Secretary of State  
2nd Floor - State Capitol Building  
Topeka, Kansas 66612

Attn: Mr. Sherman Parks

Re: Corporations--Franchise tax

Synopsis: Undistributed earnings of banking corporation in which majority of stock is held by parent corporation should not be included in determining amount of franchise tax due from latter corporation.

\* \* \*

Dear Secretary Shanahan:

You enclose a portion of the annual report filed by Midwest Bancorporation, Inc. You advise that based upon Opinion No. 73-294, dated August 24, 1973, you have computed the franchise tax to be \$681.00, instead of the amount of \$175.00 shown on the report. This computation, of \$681.00, is based upon the view that no deduction is permitted for non-taxed subsidiaries. Counsel for the corporation has taken exception to this computation.

K.S.A. 17-7503(c) prescribes the amount of the franchise tax thus:

"At the time of filing each such annual report it shall be the duty of each domestic corporation organized for profit to pay to the secretary of state an annual franchise tax in an amount equal to one dollar (\$1) for each one

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thousand dollars (\$1,000) of the corporation's shareholder's equity attributable to Kansas, except that no such tax shall be less than twenty dollars (\$20) nor more than two thousand five hundred dollars (\$2,500)."

The form which you enclose includes, in paragraph 11, as a component of shareholder's equity, the following:

"(d) Treasury Stock and unrealized Equity  
in Subsidiary Bank (\$1,013,662)"

The underscored portion was inserted by the reporting corporation.

K.S.A. 17-7501(d) defines "shareholder's equity" as the sum of:

"(1) Paid-in capital stock, except that paid-in capital stock shall not include any capital stock issued by a corporation and reacquired by such corporation through gift, purchase or otherwise and available for resale or retirement; (2) capital paid in, in excess of par; and (3) retained earnings . . . ."

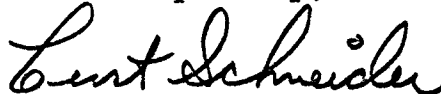
We agree with the corporation in this instance that this definition does not include undistributed earnings never received by Midwest, and which are retained in undistributed form by Farmers State Bank. Midwest Bancorporation, Inc., has reported \$888,158 of retained earnings as a component of its shareholders' equity. The earnings of Farmers State Bank and Trust Company, which are identified as "unrealized equity," of Midwest Bancorporation, based upon the equity method of accounting used by the latter, are not yet retained earnings of the parent corporation.

We think that counsel for Midwest Bancorporation correctly distinguishes this question from that presented and discussed in Opinion No. 73-294, in which Johnson County Bankshares, Inc., claimed to deduct from its shareholder's equity the amount of \$4,616,807 as the "carrying value of subsidiaries taxed separately or exempt." Insofar as appears regarding that matter, the corporation sought to deduct from its shareholders' equity its entire investment in its bank subsidiary, apparently relying on K.S.A. 17-7512, which

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provides that the "payment of franchise taxes shall not apply to banking . . . corporations . . . ." As pointed out earlier, the franchise tax is not a tax upon the shareholders' equity in and of itself, but a tax which is computed according to the value of that equity as defined by K.S.A. 17-7501(d) and (e). That exemption extends only to banking corporations, and does not exempt equity in a banking corporation held by another corporation from being considered in the determination of the franchise tax due from such other corporation. Here, however, the undistributed earnings of the Farmers State Bank and Trust Company of Hays, Kansas, do not fall within the statutory definition of "shareholder's equity" found in K.S.A. 17-7501(d), and accordingly, we cannot but agree that the amount designated as "unrealized Equity," representing retained and undistributed earnings of Farmers State Bank and Trust, should not be considered in determining the amount of the franchise tax due from Midwest Bancorporation.

Yours very truly,



CURT T. SCHNEIDER  
Attorney General

CTS:JRM:kj