

## Memorandum

To: Mr. L. Gene Mayer

Date: January 16, 1987

From: Ken McManigal

Subject: Assessment Responsibility on Railcar Repair Facilities

This is in response to your November 17, 1986, memorandum wherein you advised that Redacted Company had recently purchased Redacted Company's railcar fleet and repair facilities, had had its Redacted Services Co. subsidiary take ownership of and operate the railcar fleet, and had its Redacted Railcar Co. subsidiary take ownership of and operate the repair facilities; and you asked whether the Valuation Division should retain assessment jurisdiction of the repair facilities, which it had when both the railcar fleet and the repair facilities were owned by Redacted Company, or return assessment jurisdiction of such facilities to county assessors.

We believe that the Valuation Division should return assessment jurisdiction of the repair facilities to the appropriate county assessors. Article XIII, section 19 of the California Constitution provides in this regard that the Board shall annually assess property owned or used by car companies operating on railways in the state. As structured by Redacted Company, the car company operating on railways in California is Redacted Services Co., a subsidiary separate and distinct from the Company itself and from its other subsidiaries, including its Redacted Railcar Co., and thus, the Valuation Division should retain assessment jurisdiction over only that property owned or used by Redacted Services Co., primarily the railcar fleet.

Attached for your general information is a copy of an October 22, 1986, letter from Ms. Barbara Elbrecht to Mr. Max Goodrich which addressed the relationship between a parent corporation and its subsidiary corporations, sets forth and discusses circumstances under which corporate entities/subsidiary entities might be disregarded, and concludes that in light of the available information there is no basis for disregarding the separate existence of the parent corporation and its subsidiaries. In the same vein, there is nothing to suggest that the separate existence of Redacted Company, Redacted Services Co., and /or Redacted Railcar Co. should be disregarded in this instance.

JKM - rz

### Attachment

cc: Mr. Richard Ochsner  
Mr. Gordon P. Adelman  
Mr. Robert Gustafson  
Mr. Gene DuPaul  
Mr. Octavio Lee  
Mr. Chad McDonald  
Legal

0391H

## Memorandum

To: Mr. Richard Ochsner

Date: November 17, 1986

From: Louis E. Mayer, Chief  
Valuation

Subject: Assessment Responsibility on Railcar Repair Facilities

In 1986 and prior years we have assessed repair facilities owned by Redacted Company. These facilities, along with a railcar fleet, have been sold to Redacted Co.

Two separate subsidiaries have been set up by Redacted Company:

Redacted Services Co. which operates the railcar fleet

Redacted Co. which operates the repair facility

Gene DuPaul of my staff and Ken McManigal of yours participated in a meeting with Redacted of Redacted to discuss this and other issues connected with the sale. Gene concludes, and believes Ken agrees, that we should return assessment jurisdiction for these two shops to the county assessors.

This action would be consistent with the Board's earlier treatment of Redacted repair facility when it was operated by a subsidiary. The reason would be that there is not a strong enough connection between the two companies to meet the "owned or used by" criteria in Article XIII Sect. 19.

If you concur, we will advise the company and the two county assessors of this decision.

LEM:GD:js

cc: Mr. Gordon Adelman  
Mr. Robert Gustafson  
Mr. Ken McManigal  
Mr. Gene DuPaul  
Mr. Octavio Lee  
Mr. Chad McDonald

STATE OF CALIFORNIA



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October 22, 1986

Mr. Max Goodrich  
Chief-Ownership, Exemption &  
Mapping Division  
Los Angeles County Assessor  
500 West Temple Street  
Los Angeles, CA 90012

RE: Exemption Provided for Vessels Engaged in Transportation

Dear Mr. Goodrich:

This is in response to your letter of July 7, 1986, to Mr. Richard H. Ochsner wherein you request our opinion regarding the applicability of the exemption from taxation provided by Section 3 (1) of Article XIII of the California Constitution to vessels used by a subsidiary corporation to transport for hire the property of a parent corporation. The facts provided in your letter and the accompanying memoranda from the Office of the County Counsel can be summarized as follows:

The S. S. C Redacted and the S. S. S Redacted were both built in San Diego by Redacted Building Company and delivered to Redacted Company of California ("Redacted") on October 29, 1981, and December 18, 1981, respectively. Both vessels were bareboat chartered by Redacted to Redacted Company ("Redacted") a wholly-owned subsidiary of Redacted for \$550,000 per month. (Bareboat Charter Parties, p. 7.)

Redacted with its staff of 28 employees operates both state-of-the-art vessels as product carriers under transportation contracts with Redacted, delivering together more than nine million barrels per year of Redacted products to west coast markets. It also operates two other ships regarding which we have no information.

Two virtually identical transportation contracts between Redacted and Redacted dated September 29, 1981, (for the S. S. C Redacted and December 15, 1981, (for the S.S.S Redacted) require

Redacted, the carrier, to provide to Redacted, the shipper, the two tank vessels for the carriage of cargo designated by the shipper. The shipper has the right to name the vessels, display its insignia on the vessels' stacks, fly its house flag and determine the color of paint and the general scheme thereof on the vessels. (Transportation Contracts, p. 1)

The amount of freight agreed to by contract was the sum of all costs to the carrier, including all paid under the charter, plus a management fee. The shipper agreed to indemnify the carrier against all liabilities in excess of the carrier's insurance coverage, except for fraud, willful misconduct or criminal acts. (Transportation Contracts, p. 8)

The complex job of planning and coordinating the Redacted shipping operations is handled at the Redacted located in Redacted building. Redacted has an individual who keeps track of inventories at marketing terminals and production at the refineries . . . . He lets [Redacted] know what's needed at each location, as well as what each wants to move—when, where and in what amounts. We then take those requirements and try to fit them into a schedule that will satisfy the marketing people, and the limitations of the vessels" (Seventy Six, Jan.-Feb. 1986, p. 11).

Redacted has stated "[t]he reasons for utilizing a separate Redacted subsidiary to operate the vessels, rather than having Redacted operate the vessels directly, are the same as those which are involved in the utilization of an unrelated transportation company: the limitation of liability and the avoidance of complex labor problems which would be associated with direct operation (Letter, May 15, 1986, from Redacted).

The "A Redacted, " an oil tanker, is owned by Redacted Inc., a wholly-owned subsidiary of Redacted Company. It was purchased from Redacted Company on July 15, 1980.

The information available to us indicates the Redacted transported crude oil for hire for the period from March 1, 1981, through March 1, 1985, for several different oil companies, including 1) Redacted Company, 2) Redacted 3) Redacted 4) Redacted 5) Redacted 6) Redacted 7) Redacted. No information has been provided about the relative amount of time per shipper.

County Counsel, in a memorandum dated June 3, 1986, has stated that the information provided by Redacted persuasive regarding the issue of whether the exemption provided by Section 3 (1) of Article XIII applies to the S.S. Redacted and the S.S. S Redacted, but that a court may examine the facts in a property tax context and decide to disregard the separate corporate entity of the subsidiary. Such disregard of the separate nature of parent and subsidiary would defeat the claim for exemption. However, additional information on the Redacted was requested by County Counsel in a memorandum dated July 26, 1985, before making any determination about the applicability of the exemption to the Redacted.

#### Analysis

Section 3 (1) of Article XIII of the California Constitution exempts from property taxation:

Vessels of more than 50 tons burden in this State and engaged in the transportation of freight or passengers.

The phrase "engaged in the transportation of freight or passengers" has been construed by the California courts to mean the carrying of freight (property transported by a carrier from a consignor to a consignee) or passengers (travelers by some established conveyance) for hire (Dragich v. Los Angeles (1939) 30 Cal.App.2d 397). Thus, the question presented is whether these subsidiary corporations are independent corporations that ship the products of Union and the other petroleum companies for hire, or whether the subsidiary corporations are mere instrumentalities, conduits or agents for the parent corporations. If the corporate entity of the subsidiary corporation can be disregarded, the parent and subsidiary can be treated as one unit, thus defeating any claim that the vessels are transporting freight for hire.

The "alter ego" doctrine, the disregard of the corporate entity because the corporation is the alter ego of others, is applicable not only where the corporation is the alter ego of individuals forming or owning it, but also where a corporation is so organized and controlled, and its affairs so conducted, as to make it merely an instrument, agent, conduit or adjunct of another corporation (McLoughlin v. L. Blood Sons Co., Inc. (1962) 206 Cal.App.2d 848). "With increasing frequency, courts have demonstrated a readiness to disregard the corporate entity when a wholly-owned subsidiary is merely a conduit for, or is financially dependent on, a parent corporation (1B Ballantine & Sterling, Calif. Corp. Laws, ¶ 296.01, p. 14-33). Although the doctrine has been applied largely in tort and contract cases to assure a just and equitable results (Thomson v. L.C. Roney & Co. (1952) 112 Cal.App.2d 420; 1A Ballantine & Sterling, Calif. Corp. Laws, ¶295, p. 24-31), the doctrine has been found applicable to state tax matters to prevent the circumvention of revenue and tax laws (People v. Clauson (1964) 231 Cal.App.2d 374). Factors which courts have evaluated to determine if the separate existence of the subsidiary corporation should be disregarded are:

1. Presence in both corporations of the same officers or directors.
2. Joint accounting and payroll systems.
3. Subsidiary's lack of substantial business contacts with any save the parent.
4. Subsidiary operates solely with assets conveyed by parent.
5. Subsidiary is shown as a division on parent's financial statements.
6. Subsidiary's property is used by the parent as its own.
7. Subsidiary acts in interests of the parent.

(Annot. (1963) 7 A.L.R.3d 1343, 1355)

Based on the facts presented here, it is difficult to sustain the conclusion that the separate existence of Redacted and Redacted can be disregarded. Redacted formed a separate subsidiary corporation to operate the vessels for legitimate business purposes: to limit liability and to avoid complex labor problems which would be associated with direct operation. Redacted treated Mr.

Max Goodrich

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October 22, 1986

Redacted as a separate entity, as shown in the Redacted Charter Parties in which Redacted leased the two vessels from Redacted and in the Transportation Contracts in which Redacted agreed to ship Redacted products for a specified sum. Moreover, Redacted has two additional vessels about which we have no information, which may be utilized in ways that further support Redacted claim that Redacted is an entity separate from Redacted. Therefore, unless substantial additional evidence is provided to show that Redacted is a mere instrumentality of Redacted, such as the listing of Redacted as a division of Redacted rather than a subsidiary corporation on Redacted financial statements, or the parent used the assets of the subsidiary as its own without regard to corporate formalities, we believe there is insufficient evidence to treat Redacted is the alter ego of Redacted. Consequently, the exemption provided by Section 3(1) of Article XIII is applicable to the vessels S.S. Redacted and S.S.S Redacted. Moreover, the evidence you have presented regarding the subsidiary status of Redacted, Inc. also does not provide sufficient support for disregard of the corporate entity. The Redacted, Inc.'s vessel, the Redacted, transports the products of the several oil companies named above, including its parent Redacted, and appears to be engaged in the transport of freight for hire. Based on this little evidence we cannot state that the exemption is inapplicable to the Redacted.

I trust that the above information has been of service to you. If you have any further questions, please do not hesitate to contact me.

Very Truly Yours,

Barbara G. Elbrecht  
Tax Counsel

BGE/rz

cc:     Mr. Gordon P. Adelman  
          Mr. Robert Gustafson  
          Mr. Verne Walton

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