



BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
L & B MANUFACTURING COMPANY)

For Appellant: Arthur J. Dellinger
Certified Public Accountant

For Respondent: Paul J. Petrozzi
Counsel

O P I N I O N

This appeal is made pursuant to section 25666 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of L & B Manufacturing Company against proposed assessments of additional franchise tax in the amounts of **\$4,950.36, \$4,243.05, \$3,860.08** and **\$3,814.09** for the income years ended January 31, 1969, 1970, 1971 and 1972, respectively.

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The issue for determination is whether appellant and its affiliated corporations were **engaged in** a single unitary business during the years on appeal.

Appellant is one of a nationwide group of six wholly owned subsidiaries of L & B Products Co. (hereinafter referred to as "Products"), a New York corporation. The affiliated group is involved in the manufacture, assembly, installation, sale, and resale, of restaurant and hotel furniture and furnishings. Products, appellant, and **appellant's** wholly owned subsidiary, Bentley Products and Engineering Corporation (hereinafter referred to as "Bentley") conduct **advertising** operations for the entire corporate group. Advertising is conducted through the publication of catalogs and price lists. The catalogs reveal that each member of the affiliated group merchandises virtually identical products.

Products was founded in New York on January 30, 1946, and is principally owned by Leo Seifer, Leo Zelinger and Joseph **Zelinger**. As of 1972, these three individuals continued to own 83.61 percent of the parent. During the appeal years, all five of Product's directors were also directors of at least one of the subsidiaries, and two of Product's directors were directors of all the subsidiaries. All of appellant's directors were also directors of Products, and two of them were also directors of all the other members of the affiliated group. In **addition**, all of appellant's officers were also officers of Products, and three of Product's five officers were officers of virtually all the subsidiaries.

During the appeal years, appellant acquired an average of approximately 13 percent of its total purchases from Products. Products purchased less than one percent of its merchandise from appellant, resulting in total purchases of \$152,000. The record **indicates** that Products purchases all of the items it later sells from its subsidiaries. Borrowing and financing are arranged by the parent corporation for its subsidiaries. Specifically, information supplied by appellant indicates that Products stands behind letters of credit or sight drafts drawn on Products on behalf of some or all of its subsidiaries. The parent corporation also occasionally finances direct purchases of materials by its subsidiaries. Furthermore, the record reveals **that appellant** is indebted to Products for **a sum** in excess of \$100,000 and that Products made purchases on behalf of Bentley

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during each year in issue and for appellant during the income year ended January 31, 1971. Products was immediately repaid for the sums advanced for these purchases.

When a taxpayer derives income from sources both within and without California, it is required to measure its California franchise tax liability by its net income derived from or attributable to sources within this state. (Rev. & Tax. Code, § 25101.) If the taxpayer is engaged in a unitary business with affiliated corporations, its California tax liability must be determined by applying an apportionment formula to the total business income derived from the combined unitary operations of the affiliated companies. (See Edison California Stores, Inc. v. McColgan, 30 Cal.2d 472 [183 P.2d 16] (1947); John Deere Plow Co. v. Franchise Tax Board, 38 Cal.2d 214 [2338 P.2d 569] (1951), app. dismissed, 343 U.S. 939 [96 L.Ed. 1345] (1952).)

The California Supreme Court has determined that a unitary business is definitely established by the existence of: (1) unity of ownership; (2) unity of operation as evidenced by central purchasing, advertising, accounting, and management divisions; and (3) unity of use in a centralized executive force and general system of operation. (Butler Bros. v. McColgan, 7 Cal. 2d 664 [111 P.2d 334] (1941), aff'd., 315 U.S. 501 [86 L.Ed. 991] (1942).) The court has also held that a business is unitary when the operation of the business within California contributes to or is dependent upon the operation of the business outside the state. (Edison California Stores, Inc. v. McColgan, supra.) These principles have been reaffirmed in more recent cases. (Superior Oil Co. v. Franchise Tax Board, 60 Cal.2d 406 [34 Cal.Rptr. 545, 386 P.2d 331] (1963); Honolulu Oil Corp. v. Franchise Tax Board, 60 Cal.2d 417 [34 Cal.Rptr. 552, 386 P.2d 40] (1963).) The existence of a unitary business may be established if either the three unities or the contribution or dependency test is satisfied. (Appeals of Browning Manufacturing Co., et al., Cal. St. Bd. of Equal., Sept. 14, 1972; Appeal of F. W. Woolworth Co., Cal. St. Bd. of Equal., July 31, 1972.)

In concluding that appellant and the rest of the affiliated group were engaged in a single unitary business under either the contribution or dependency test or the three unities test, respondent relied principally on the following factors: total ownership of

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the subsidiaries, including appellant, by Products: an integrated executive force which controlled appellant's major policy decisions'; the operation of similar businesses by appellant and the remainder of the affiliated group and the sharing of know-how among members of the group: intercompany financing: intercompany product flow; and other centralized functions (e.g., common advertising).

In numerous prior cases, the unitary features relied upon by respondent, when viewed in the aggregate, have demonstrated a degree of mutual dependency and contribution sufficient to compel the conclusion that a unitary business existed. (See, e.g., Chase Brass & Copper Co. v. Franchise Tax Board, 10 Cal.App.3d 496 [87 Cal.Rptr. 2391 app. **dism.** and cert. den., 400 U.S. 961 [27 L.Ed.2d 381] (1970); Appeal of Harbison-Walker Refractories Company, (on rehearing), Cal. St. Bd. of Equal., Feb. 15, 1972; Appeal of Williams Furnace Co., Cal. St. Bd. of Equal., Aug. 7, 1969; and Appeal of Anchor Hocking Glass Corporation, Cal. St. Bd. of Equal., Aug. 7, 1967.) Respondent's determination that appellant is engaged in a **unitary** business with its affiliates is presumptively correct, and the burden to show that such determination is erroneous is upon appellant. (Appeal of John Deere Plow Co. of Moline, Cal. St. Bd. of Equal., Dec. 13, 1961.)

We believe that the unitary features relied upon by respondent satisfy the 'three unities test and that those same features, when viewed in the aggregate, demonstrate a degree of mutual dependency and contribution sufficient to establish the existence of a unitary business operation by appellant and its affiliated corporations.

Appellant contends that it is not involved in a unitary business with its **affiliated corporations** and challenges the assessments on the 'basis that **two** of the three elements of the three unities test (i.e., the unities of use and operation) are not present in the activities of the affiliated group.' Appellant, however, has offered no factual evidence to support its contention; it simply asserts that the only unity present is that of ownership. Thus., in the absence of some compelling reason to invalidate respondent's determination, we **must conclude** that appellant has failed to carry its burden of proof and that respondent's action in this matter was correct.

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It should also be noted that appellant has argued only that the three unities test has not been satisfied and has completely ignored respondent's reliance upon the contribution or dependency test to establish that appellant and its affiliated corporations were engaged in -a single unitary business during the years on appeal. As noted above, a business is unitary when the operation of the business within California contributes to or is dependent upon the operation of the business outside the state. (Edison California Stores, Inc. v. McColgan, supra.) A showing that the contribution or dependency test has been satisfied is, on its own, sufficient to show the existence of a unitary business. (Appeal of F. W. Woolworth Co., supra.) Consequently, even if appellant had carried its burden of showing that the three unities test had not been satisfied, its failure to carry its burden of proof as to the contribution or dependency test would alone be fatal to its position.

