



Appeals of Eljer Company and  
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products of the single subsidiary not selling directly to the parent were sold to another subsidiary which also bought part of the production of the parent. The parent purchased the products manufactured by the subsidiaries at the price at which it sold the goods to its customers less a discount of three per cent during 1947 and 1948 and six per cent during 1949 and 1950.

The record in this appeal is somewhat sketchy as respects the management and general manner of operation of the group. It appears, however, that the officers of the parent and the California Company were the same individuals and that while the subsidiaries had considerable autonomy, general policy was set by the parent. The parent did substantially all of the advertising,

Appellants filed separate returns for each of the years here in question. The Franchise Tax Board subsequently determined that all of the related corporations were engaged in a single unitary business and that a portion of their combined net income should be allocated to California by use of the usual formula composed of the factors of property, payroll and sales. The first issue therefore is whether the parent and its subsidiaries were engaged in a unitary business.

In Edison California Stores v. McColgan, 30 Cal, 2d 472, the most recent opinion by the California Supreme Court dealing with this problem, it was stated that the test is whether the operation of the portion of the business done within the State is dependent upon or contributes to the operation of the business done elsewhere. The court held that the test was met where one portion of the business purchased goods and the other portion sold those goods. The same principle applies where one portion of the business manufactures goods and the other portion sells the goods so manufactured. See Altman & Keesling, Allocation of Income in State Taxation, 2d Ed. (1950), at page 101, where the authors state: "... the business of manufacturing or purchasing goods in one state and selling them in other states is clearly unitary." And see our decision in Appeal of The Youngstown Steel Products Co. of California, decided May 29, 1952. In our opinion, the manufacturing and selling operation here present, together with the centralized ownership and management, establishes the unitary nature of the business.

Appellants argue (1) that the provisions of the law governing the filing of consolidated returns have not been met because the parent paid fair prices for the products of the subsidiaries and (2) that the allocation formula produces an unreasonable result because costs in California were higher than they were elsewhere. The first point was

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considered in Edison California Stores, supra, at page 480, where the court stated that the power to allocate income by formula was "not derived from the [statutory] authority to" require the filing of consolidated returns ..." but was authorized by Section 10 of the Act (later Section 24301 and now Section 25101 of the Revenue and Taxation Code). The second point has been rejected in John Deere Plow Co. v. Franchise Tax Board, 38 Cal. 2d 214.

Appellants made two other contentions respecting the proposed assessments: (1) that sales solicited outside California were improperly included in the California portion of the sales factor and (2) that the formula was incorrectly applied in the years when corporations were entering or leaving the group. In so far as (1) is concerned, the Franchise Tax Board makes the uncontroverted reply that in its action on Appellants' protests the Franchise Tax Board eliminated from the numerator of the sales factor all sales solicited from out-of-State customers by salesmen working out of a California sales office. In so far as (2) is concerned, the Franchise Tax Board makes the uncontroverted reply that it made adjustments in the factors of the allocation formula to ensure that) for example, property of a particular corporation would not be included in the formula for months prior to the date when the corporation joined the group or for any period of time after the corporation ceased operations. This type of adjustment is provided for in Regulation 24301 (now 25101) Title 18, California Administrative Code. In the application of this adjustment to the year 1950, the Franchise Tax Board included only one-sixth of the value of the property of the California Company inasmuch as that corporation ceased operations on March 1, 1950. This adjustment would appear to be reasonable. It must be remembered that formula allocation is not expected to produce a precise result - rough approximation is all that can be expected, (John Deere Plow Co. v. Franchise Tax Board, supra.) Furthermore, a taxpayer must show, by "clear and cogent" evidence, that extraterritorial values have been taxed before the action of the administrative agency will be set aside. (Butler Brothers v. McColgan, 315 U.S. 501) This, Appellants have failed to do.

Appellants contend, finally, that the notices of proposed assessment against each of them for the income year 1947 were defective because the Franchise Tax Board used estimated figures therein With the following explanation:

"Arbitrary addition to income prior to the running of the Statute of Limitations. The adjustment reflected in this notice may be revised upon submission of the required information to complete the audit."

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Appellants cite the following language in Section 25662 of the Revenue and Taxation Code (formerly Section 25(a) of the Bank and Corporation Franchise Tax Act): "Each notice shall set forth the reasons for the proposed additional assessment and the details of the computation thereof." The Franchise Tax Board states that it had to use estimated figures because Appellants refused to execute waivers of the statute of limitations and did not furnish requested information prior to the time when the statute would have expired on the income year 1947.

We have previously considered and rejected arguments substantially identical to that of the Appellants. (Appeals of Raymond H. Osbrink, et al., decided November 7, 1958; Appeal of Robert E. Campbell, Executor, decided June 20, 1950.) It here appears that the notices set forth reasons for the arbitrary assessments and informed the Appellants that the amounts were subject to revision upon the submission of required information; information which the Appellants had failed to provide on prior request. The form of the notices did not in any degree deprive Appellants of opportunity to contest them.

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, pursuant to Section 25667 of the Revenue and Taxation Code, that the action of the Franchise Tax Board in denying the protests of Eljer Company and Eljer Company of California against the following proposed assessments of additional franchise taxes:

	<u>INCOME YEARS</u>			
	<u>1947</u>	<u>1948</u>	<u>1949</u>	<u>1950</u>
Eljer Company	\$1,246.12	\$ 630.75	\$1,061.37	\$ 608.34
Eljer Company of California	9,991.03	13,909.48	7,403.80	5,648.47

be and the same is hereby sustained.

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Done at Sacramento, California, this 16th day of  
December, 1958, by the State Board of Equalization.

George R. Reilly, Chairman

Paul R. Leake, Member

J. H. Quinn, Member

Robert E. McDavid, Member

Robert C. Kirkwood, Member

ATTEST: Dixwell L. Pierce, Secretary