

BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of
ROSENBERG BROS. & CO., INC.

Appearances:

For Appellant: Richard E. Guggenhime and
Robert C. Harris, Attorneys at Law
For Respondent: Jack Rubin, Assistant Counsel

O P I N I O N

This appeal is made pursuant to Section 25667 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of Rosenberg Bros. & Co., Inc., to a proposed assessment of additional franchise tax in the amount of \$72,880.99 for the income and taxable year 1948.

Appellant was incorporated in Maryland on October 30, 1947, and qualified to do business in California on November 6, 1947. It maintained its records on a calendar year basis. Its sole shareholder was Mr. Nathan Cummings, who was a principal stockholder of Consolidated Grocers Corporation (now Consolidated Foods Corporation), Consolidated desired to acquire all of the stock or all of the assets of Rosenberg Bros. & Co., a California corporation (hereafter referred to as Rosenberg-California). Appellant was organized for the sole purpose of making the acquisition for Consolidated.

Within a few days after being organized, the first meeting of Appellant's board of directors was held in San Francisco. Bylaws were adopted, officers were elected and it was resolved to establish a bank account with Wells Fargo Bank and Union Trust Company of San Francisco.

✓ On November 26, 1947, Appellant entered into an agreement of purchase and sale with the Rosenberg-California stockholders, under which Appellant would purchase all, or substantially all, of the Rosenberg-California stock.

✓ On December 1, 1947, the second meeting of the board of directors was held in San Francisco. The directors approved an agreement under which Appellant would secure loans totaling \$16,054,688.00 from banks located in San Francisco, Chicago, New York and Boston. The directors also accepted an offer by

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Nathan Cummings to lend Appellant \$1,000,000.00 payable on demand. At this meeting the directors approved an agreement between Appellant and Consolidated whereby Appellant agreed to sell to Consolidated all of the Rosenberg-California stock or the Rosenberg-California assets should that corporation be liquidated. The sale was to take place on December 1, 1948. The price was established so that Appellant would receive the price which it was to pay to the Rosenberg-California stockholders. The agreement further provided that Appellant might retain dividends received from Rosenberg-California but that any excess over \$485,000.00 would proportionately reduce Consolidated's obligation. The agreement was formally executed on December 5, 1947.

In January, 1948, Appellant purchased all the shares of stock of Rosenberg-California pursuant to its agreement with the Rosenberg-California stockholders. Appellant then exercised its newly acquired voting rights in Rosenberg-California and elected a new board of directors for that corporation. On January 26, March 17, May 29 and August 28, 1948, Appellant received dividend payments from Rosenberg-California in the total sum of \$4,813,630.50.

Shortly before September-6, 1948, Cummings sold all of Appellant's stock to Consolidated and on September 6, 1948, the agreement between Appellant and Consolidated was formally canceled by mutual consent.

On October 21, 1948, Appellant liquidated Rosenberg-California and distributed all the assets to itself as sole stockholder. Since then Appellant has operated the business originally operated by Rosenberg-California.

The Franchise Tax Board's proposed assessment is based on its conclusion that Appellant began doing business in California in 1947. Thus Appellant's first taxable year would be for less than twelve months, and Appellant's net income for the year 1948 would measure its liability for the taxable years of 1948 and 1949. (Section 13(c) of the Bank and Corporation Franchise Tax Act, now Section 23222 of the Revenue and Taxation Code.) Appellant protests the proposed assessment on the theory that it did not commence doing business in California in 1947, that when it commenced to do business it was pursuant to a reorganization and that the Franchise Tax Board's action amounts to double taxation which was never intended by the Legislature.

Section 5 of the Bank and Corporation Franchise Tax Act (now Section 23101 of the Revenue and Taxation Code) defines "doing business" as "actively engaging in any transaction for

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the purpose of financial or pecuniary gain or **profit.**"

There can be no doubt that entering into the agreements to buy and sell stock constituted engaging in transactions. (Carson Estate Co, v. McColgan, 21 Cal. 2d 516.) Appellant contends, however, that the second half of the "doing business" definition was not met in that its activities were not "for the purpose of financial or pecuniary gain or **profit.**" Under Appellant's agreement with Consolidated, Appellant was to make a profit of \$485,000.00; but this was the amount of interest it had contracted to pay on its loans and, therefore, Appellant, after completing the entire transaction, would not have any profit.

We believe that Appellant assumes too narrow a view of the meaning of the statutory language. The activities of Appellant were undoubtedly for the purpose of financial or pecuniary gain or profit to Mr. Cummings as the sole stockholder of Appellant and a principal stockholder of Consolidated or, if he merely held Appellant's stock on behalf of Consolidated, then to Consolidated as the true stockholder. That such a purpose is within the scope of the statute is indicated by the decision in Hise v. McColgan, 24 Cal. 2d 147, 151, wherein the California Supreme Court stated:

"It should be clear that the commissioner in liquidating Marine was endeavoring to get the best price obtainable for its assets and to conduct its affairs in liquidation to the end that the most financial gain would be realized for its creditors and stockholders. The aim was pecuniary gain."

In Atlanta Labor Temple Assn., Inc. v. Williams, 105 S.E. 2d 406, it was held that a corporation was "organized for pecuniary gain or profit" where its charter provided that "The objects of said association are pecuniary gain to the stockholders thereof." Similarly, the court stated in In Re Wisconsin Co-Operative Milk Pool, 119 Fed. 2d 999, 1002, that "The sole motive is pecuniary gain" where the chief purpose of a cooperative corporation was the financial benefit of its members. In our opinion, a corporation is doing business when, as in this case, it engages in activities at the direction of its sole stockholder for the purpose of financial gain to him. See Roger J. Traynor and Frank M. Keesling, Recent Changes in the Bank and Corporation Franchise Tax Act, 21 Calif. L. Rev., 543, 547, 551.

Section 13(g) of the Act (now Section 23252 of the Code), and Section 13(j) of the Act (now Section 23251 of the Code),

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provide that a corporation which commences to do business in this State pursuant to a reorganization shall not be taxed as a commencing corporation, and define "reorganization" to include a distribution in liquidation by a corporation of all of its business or property to a corporation stockholder which continues the business.

As we have indicated, it is our opinion that Appellant commenced to do business long before the liquidation of Rosenberg-California. Even if we take the view most favorable to Appellant, ~~that its~~ activities in 1947 were part of a pre-conceived plan leading to the liquidation, we could not conclude that the activities were pursuant to a reorganization. In Appeal of Andrews Motor Car Company, decided May 19, 1954, we held that a corporation did not commence business pursuant to a reorganization where its purpose was to acquire the assets and business of another corporation and the purpose was carried out by first acquiring all the stock of the other corporation and thereafter liquidating the other corporation and distributing the assets and business to itself as the sole stockholder. We said:

"The only theory upon which Appellant's position may be supported is that the acquisition of Hollywood's stock and the subsequent liquidation of that corporation constituted separate transactions. The facts show clearly, however, that the acquisition of the Hollywood stock and the liquidation of that corporation were but closely related steps of a single transaction. In such a situation we feel compelled to follow the United States courts which, in applying similar Federal statutes, have adopted the view that substance not form controls tax liability and have held that such a transaction is a purchase of property and not a reorganization. Commissioner v. Ashland Oil & Refining Co., 99 Fed. 2d 588; Prairie Oil and Gas Co. v. Motter, 66 Fed. 2d 309; Kimbell-Diamond Milling Co., 14 T. C. 74, affirmed 187 Fed. 2d 718, certiorari denied 342 U.S. 827.

* * *

The case of San Joaquin Ginning Company v. McColgan, 20 Cal, 2d 254, cited by

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Appellant does not require a different conclusion than we have reached. In that decision the court adopted a liberal construction of the term 'reorganization' to include any transaction which does not affect a substantial change in the continuity of interest. The transaction here in question, however, resulted in a complete transfer of ownership of the assets of Hollywood."

The principle of the Federal cases cited in our prior opinion has recently been reaffirmed, (U. S. v. Mattison, 273 Fed. 2d 13; U. S. v. M. O. J. Corp., Fed. 2d 15 AFTR 2d 535], (C. A. 5, Jan. 19, 1960); North American Service Co., Inc., 33 T. C. No. 77.)

The remaining contention of Appellant is that the Franchise Tax Board's proposed assessment will result in "double taxation." Appellant's contention is based on the fact that Rosenberg-California paid a franchise tax for the privilege of doing business for a full year including the period of October 21, 1948, through December 31, 1948, when Appellant was operating what had formerly been the business of Rosenberg-California.

It should be noted that there was no double taxation of the same income in any sense, because the tax paid by Rosenberg-California was measured by the income of a preceding period. The case of one corporation transferring its business and assets to another "is not unique. In a situation of this kind the law provides that the transferor is entitled to a partial refund if it formally dissolves before the end of its taxable year. (Section 13(k) of the Act, now Section 23332 of the Code.) There is here no indication of a date when Rosenberg-California dissolved. In any event, its failure to claim a partial refund would not affect the tax liability of Appellant.

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,

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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 on the protest of Rosenberg Bros. & Co., Inc., to a proposed assessment of additional franchise tax in the amount of \$72,880.99 for the income and taxable year 1948, be and the same is hereby sustained,

Done at Los Angeles, California, this 4th day of April, 1960, by the State Board of Equalization,

John W. Lynch, Chairman

George R. Reilly, Member

Richard Nevins, Member

_____, Member

_____, Member

ATTEST: Dixwell L. Pierce, Secretary