67-SBE-015

BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
)
LEAR SIEGLER, INC. (FORMERLY)
THE SIEGLER CORPORATION))

Appearances:

For Appellant: Bennett W. Priest and
Clyde E. Tritt
Attorneys at Law

For Respondent: Peter S. Pierson
Associate Tax 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 protests of Lear Siegler, Inc., against proposed assessments of additional franchise tax in the amounts of $28,595.82, $40,761.81, and $29,289.72 for the income years 1956, 1957, and 1958, respectively.

The issue presented by this appeal is whether the whole of appellant's business activities constituted one unitary business requiring allocation of income attributable to California sources by means of a single allocation formula.

Appellant was incorporated under the laws of the State of Delaware and has qualified to do business in the State of California. Prior to the year 1955 it was a closely held family corporation with principal business offices located in Chicago, Illinois. In November 1954 there was a substantial public sale of appellant's stock and since that time its business operations have been greatly expanded primarily by acquisition of existing businesses. It now manufactures and sells many different products.

The newly acquired businesses were incorporated into several operating divisions created by appellant. During the income years 1956 and 1957 the operating divisions consisted of the Siegler Heater Division, principally located in Illinois, a manufacturer of commercial space heaters; the Hallamore Electronics Division located in Anaheim, California, a manufacturer of military and industrial communication systems; and the Holly-General Division located in Pasadena, California, a manufacturer of commercial wall heaters, floor furnaces, and related products. In income year 1958 appellant added the Olympic Division located principally in New York, a manufacturer of commercial radio and television sets; the Bogen-Presto Division principally located in New Jersey, a manufacturer of high fidelity sound systems and recording discs; and the Baby-Mate Division principally located in Los Angeles, California, a manufacturer of infants' furniture. Each of the divisions conducted interstate operations.

Each of appellant's operating divisions had its own staff of executives who were assigned responsibility for the business activity conducted by that division. Each division maintained separate purchasing, engineering, and marketing departments. There was no centralization of the accounting of the operating divisions and no interchange of key employees. Although the Holly-General Division did in one instance develop a product for the Lear Siegler Division, there was no significant interdivision transfer of goods or services. Each division had the right to participate in common profit sharing and health insurance plans, but was not required to do so.

For the income years 1956 and 1957 appellant's corporate office maintained a liaison with the operating divisions through two corporate officers who periodically visited the divisions for discussion and review of division business. They also made arrangements for any financial assistance required for division business.

During the income year 1958 appellant moved its corporate headquarters to Los Angeles, California, and established a separate corporate services division. This division assumed responsibility for providing financing and also provided certain overhead services for the operating divisions. The cost of operating the corporate services division was allocated among the operating divisions. The staff of the corporate services division was expanded from two to six people during 1958 and in subsequent years has grown to a total of 26.

The holding of periodic conferences between division heads and corporate officers became an established business practice during the income year 1958. In subsequent years this practice has been expanded to constitute regular quarterly

meetings with an agenda. Some key management personnel of the operating divisions have been appointed to corporate officer positions.

On appellant's franchise tax returns the income of each division was determined separately and a separate apportionment formula was used to allocate income from each division within and without California.

Respondent determined that appellant's entire business operation constituted one unitary business and reallocated the combined income within and without the state by use of a single apportionment formula. Deficiency assessments were issued for the income years 1956, 1957, and 1958.

It is appellant's contention that each of the divisions was a completely separate business with virtual autonomy in operation and management, and that the separate formula apportionment of income for each division accurately reflects income attributable to California sources. Respondent concedes that there was considerable operational "separateness." Nevertheless, it contends that its determination is sustained by a centralization of management and administrative functions and a high degree of financial control exercised by a central authority.

Business operations carried on at locations within and without the state under common ownership constitute a single unitary business when the operation carried on within the state is dependent upon or contributes to the operations conducted outside the state. (Edison California Stores, Inc. v. McColgan, 30 Cal. 2d 472 [183 P.2d 16].) The interdependence of the business activities is established where there is unity of ownership; unity of operation as evidenced by central purchasing, advertising, accounting, and management; and unity of use in a centralized executive force and general system of operations. (Butler Bros. v. McColgan, 17 Cal. 2d 664 [111 P.2d 334], aff'd, 315 U.S. 501 [86 L. Ed. 991]; Superior Oil Co. v. Franchise Tax Board, 60 Cal. 2d 406 [34 Cal. Rptr. 545; 386 P.2d 33]; Honolulu Oil Corp. v. Franchise Tax Board, 60 Cal. 2d 417 [34 Cal. Rptr. 552; 386 P.2d 40].) Where a business is unitary, the entire income must be combined and allocated by use of a single formula. (RKO Teleradio Pictures, Inc. v. Franchise Tax Board,* 246 Cal. App. 2d _____; John Deere Plow Co. v. Franchise Tax Board, 38 Cal. 2d 214 [238 P.2d 569], appeal dismissed, 343 U.S. 939 [96 L. Ed. 1345].)

With the rapid growth of appellant corporation, there has been a centralization of certain of its functions. However, after fully considering all of the evidence, we have concluded that the central performance of these functions has not

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* Advance Report Citation: 246 A.C.A. 948

significantly detracted from the accuracy of separately determining and allocating the income of each division. During the income years under review, the various divisions have in all material respects remained operationally separate. Each division had its own executives who retained a large area of responsibility for formulation and execution of business policy. There was no centralization of purchasing, accounting, or other pooling of business functions. Nor does it appear that any of the divisions derived a value from a unity of use. There was no interchange of employees or goods between the divisions and, with a single exception, no joint participation in the development, marketing and sale of products. The general system of operations called for each division to operate independently of the other divisions.

While the executives of the corporate services division have asserted a degree of control over the activities of each division this control has, during the period here under consideration, been limited primarily to the review of division budgets and the approval of significant expenditures for new products, new plants and new ventures. We have previously ruled that such overall "management" decisions, standing alone, would not establish separate and distinct types of businesses as a single unitary business. (Appeal of Allied Properties, Cal. St. Bd. of Equal., March 17, 1964.) Only in the realm of financing and the operation of a joint profit-sharing and health insurance plan was there presented an opportunity for contribution to a common income through the activities of the corporate services division.

For the income years 1956 and 1957 the authority to obtain loans of money was limited to certain designated corporate officers and this authority was retained within the corporate services division during income year 1958. There was some interchange of funds between the divisions. The borrowed funds, however, were not used to finance a common business activity and none of the operating divisions were involved in lending money. Under these circumstances, the single source of financing did not establish the divisions as parts of a single unitary business. (Appeal of Simco, Inc., Cal. St. Bd. of Equal., Oct. 27, 1964.)

The joint profit participation plan and the common purchasing of insurance that existed are features of a unitary nature. However, participation was not mandatory and there is evidence that widespread use of these features was not made until subsequent years. Thus, it would not appear that the savings effected by these common activities had any significant effect on the income of the group during the income years under review. A different determination may well be required for subsequent years when these unitary features are weighed with other

developing factors disclosed by the record, such as increased administrative control, coordination of research and development and of advertising, some common purchasing activity, continuous interchange of funds between the divisions and other common activities.

During the income years 1956, 1957, and 1958, however, we do not find any significant connection between the earnings or losses of one division as a result of activities carried on by another division or on behalf of the group as a whole. For this reason we must reverse respondent's determination that all of appellant's business activities constituted a single unitary business.

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 on the protests of Lear Siegler, Inc., against proposed assessments of additional franchise tax in the amounts of $28,595.82, $40,761.81, and $29,289.72 for the income years 1956, 1957, and 1958, respectively, be and the same is hereby reversed.

Done at Sacramento, California, this 24th day of April, 1967, by the State Board of Equalization.

Paul R. Leake, Chairman

Geo. R. Reilly, Member

Richard Nevins, Member

_____, Member

Geo. R. Reilly, Member

Attest: _____, Secretary