

Appeal of United States Plywood Corporation

Appellant then set up separate allocation formulas for each class of business. The sales, payroll and property of the home office and sales branches were divided on the same basis as that used for dividing the net income. The sales, payroll and property of the manufacturing plants were allocated entirely to the "**goods manufactured**" category. The two allocation ratios thus computed were applied to their respective portions of the total net income in order to arrive at **the income** attributable to **California for** each type of activity. These last two amounts were combined and reported as the net income derived from sources within this State.

The Franchise Tax Board disallowed Appellant's allocation method and, instead, applied a single allocation formula to the entire net income on the **ground that** Appellant is engaged in but a single unitary business.

Appellant contends that it is engaged in two separate, distinct businesses. It argues that the inclusion of its large California manufacturing properties in the formula used to allocate the net income from the distribution of non-manufactured products does not reach a fair result. Appellant raises the identical issues decided by us in the Appeal of RKO Radio Pictures, Inc., Cal. St. Bd. of Equal., Dec. 17, 1957, 2 CCH Cal. Tax Cas. Par. 200-767, 2 P-H State & Local Tax Serv. Cal. Par. 13173. That appeal concerned a taxpayer who was engaged in producing and distributing its own films and in distributing films produced by others. We upheld the Franchise Tax Board's action in disallowing the taxpayer's method of separately allocating the income from independently produced films and in applying instead a single formula of property, payroll and sales to all of the income.

As in the RKO appeal, Appellant has failed in its attempt to establish the separate character of a portion of its business. Since the same facilities and personnel are used in the distribution of all of the products handled by Appellant, it is readily apparent that there is a mutual dependence and contribution between the distribution of Appellant's own products and distribution of the goods purchased from others. We conclude that **Appellant's** entire operation was properly treated as a single unitary business.

In RKO, we noted that the taxpayer had failed to show the basis upon **which** it initially segregated the net income derived from distribution of independently produced films from the net income attributable to its own pictures. Since all subsequent calculations were based upon this initial step, it was apparent that the taxpayer had failed to prove an essential element of its case. In contra-distinction, Appellant in the instant appeal makes the basis of its initial segregation clear; it divided its income in proportion to the relative costs of the two classes of merchandise it sold.

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The Franchise Tax Board argues that such a basis for separating income is wholly arbitrary and objectionable in its application to a unitary business. It points out that the cost of goods purchased from outside sources contains an element of profit for the producer while the cost of goods manufactured by Appellant does not contain such an element of profit. Thus Appellant's method of apportionment makes no allowance for a profit from its own manufacturing process and unjustifiably weights the income attributable to the non-manufactured goods. Respondent urges that since California accounts for a large share of Appellant's manufacturing activities, this State must reject any method of allocation which does not attribute a fair share of net income to the manufacturing process. We agree.

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 protest of United States Plywood Corporation against a proposed assessment of additional franchise tax in the amount of \$8,149.77 for its income year ended April 30, 1954, be and the same is hereby sustained.

Done at Sacramento, California, this 17th day of May, 1962, by the State Board of Equalization.

Geo. R. Reilly, Chairman
Richard Nevins, Member
Paul R. Leake, Member
John W. Lynch, Member
_____, Member

ATTEST: Dixwell L. Pierce, Secretary