



BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

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Appeals and Review Office
FRANCHISE TAX BOARD

In the Matter of the Appeal of)
AVON PRODUCTS, INC.)

For Appellant: L. W. Jaeger, Treasurer

For Respondent: Burl D. Lack, Chief Counsel;
Crawford H. Thomas, 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 protest of Avon Products, Inc., against a proposed assessment of additional franchise tax in the amount of \$703.62 for the income year 1954.

Appellant is engaged in the manufacture and sale of cosmetics. Appellant is a New York corporation; its principal place of business and its commercial domicile are in New York. It was the sole owner of Hinze Ambrosia, Inc. (hereafter referred to as Ambrosia), also a New York corporation.

Ambrosia was merely a distribution channel through which Appellant's products were sold using conventional merchandising methods rather than Appellant's direct selling technique. Appellant was Ambrosia's sole supplier. Ambrosia had no employees or fixed assets; it relied solely upon the facilities of Appellant, for which it paid a fee. Both corporations had the same officers and directors.

Appellant does business in California and Ambrosia also did business here. The Franchise Tax Board determined that Appellant and its subsidiaries, including Ambrosia, were conducting a unitary business both within and without this State and required the filing of combined income reports. These combined reports, filed for the years 1950 to 1953, indicated that Ambrosia suffered operating losses which reduced the allocable combined income. Appellant sustained a loss of \$171,680.14 in 1954 as a result of the liquidation of Ambrosia and this amount was deducted from the allocable income. The Franchise Tax Board disallowed the deduction of this loss and recomputed the income allocable to this State accordingly,

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Appellant contends that Ambrosia was a mere adjunct, agency or instrumentality which it used in the conduct of the unitary business. Relying principally on Holly Sugar Corp. v. Johnson, 18 Cal. 2d 218, it urges that since Ambrosia was an integral part of the unitary business, the loss sustained on liquidation must be included in the tax base used to determine the amount of net income properly allocable to California.

We think Appellant's reliance is misplaced. The facts in the Holly Sugar case were that a New York corporation doing a substantial portion of its business in California, but with its principal office in Colorado, acquired 70 percent of the shares of a California corporation engaged in the same type of business wholly within this State. The court held that by economic integration with the owning company's operation within California the shares of stock had become sufficiently localized to acquire a business situs here. Appellant's situation is not comparable. We are not dealing here with a subsidiary whose legal and commercial domiciles were in California and whose entire activities were localized in this State. From what appears in the record, Ambrosia's legal and commercial domiciles were in New York and its activities spread over a number of states.

To give effect to Appellant's contention would require the establishment of a novel concept. It is well recognized that the source of income from stock ownership is in the shares of stock owned and that the income is taxable at the situs of that stock. (Miller v. McCorgan, 17 Cal. 2d 432; Southern Pacific Co. v. McCorgan, 68 Cal. App. 2d 48.) Thus Appellant's position necessarily implies that the situs of the shares of stock it held in Ambrosia was spread among the various states in which Ambrosia did business. As we said in the Appeal of Dohrmann Commercial Co., Cal. St. Bd. of Equal., Feb. 29, 1956 2 CCH Cal. Tax Cas. Par. 200-504, 2 P-H State & Local Tax Serv. Cal. Par. 13152, wherein we considered and rejected essentially the same proposal:

Since the percentage of the unitary income attributable to sources in each State is subject to fluctuation from year to year, the situs of the shares of stock would apparently shift from one state to another annually on the basis of income derived from each state, without regard to the legal or commercial domicile of either the owning or issuing corporation. This concept of situs is not supported by the authorities and is contrary to well settled principles of law.

* * *

While it is true that the court [in Holly Sugar Corp. v. Johnson, supra] relied on the unity of operations of the two companies as

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the basis for its conclusion that the shares of stock there in question had become localized as an integral part of the foreign corporation's activities within the State, Appellant's interpretation of the decision overlooks the fact that the stock owned by Holly Sugar Company was used to control a corporation having its legal and commercial **domicil** within this State and whose activities were localized here. Since the question was not in issue, the decision is certainly not authority for the arbitrary assignment of a business **situs** of a fragmentary portion of stock to each state in which a multi-state subsidiary conducts a portion of the unitary business.

Since Appellant was not domiciled in California and the facts do not establish that the stock in Ambrosia had a business **situs** here, no part of the loss arising from the stock was attributable to California. (Southern Pacific Co. v. McColgan, supra; Appeal of Safeway Stores, Inc., Cal. St. Bd. of Equal., March 2, 1962, 3 CCH Cal. Tax Cas. Par, 201-897, 2 P-H State & Local Tax Serv. Cal. Par. 13272.)

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 protest of Avon Products, Inc., against a proposed assessment of additional franchise tax in the amount of \$703.62 for the income year 1954 be and the same is hereby sustained.

Done at Sacramento, California, this 7th day of June, 1962, by the State Board of Equalization.

<u>George R. Reilly</u>	, Chairman
<u>John W. Lynch</u>	, Member
<u>Alan Cranston</u>	, Member
<u>Richard Nevins</u>	, Member
_____	, Member

ATTEST: R. G. Hamlin, Acting Secretary