

Appeal of U-Haul Co. of Van Nuys

Three questions are presented by this appeal: (1) Whether Amerco Lease Co. was engaged in a single unitary business with appellant and other members of appellant's combined group; (2) if so, whether the income of Amerco Lease Co. was business or nonbusiness income; and (3) whether respondent properly computed appellant's California property factor.

Appellant is a California corporation engaged in the business of renting various kinds of equipment, principally trucks and trailers, to the public. Appellant is wholly owned by AMERCO, Inc., a Nevada corporation, which also owns 100 percent of Amerco Lease Co. (Amerco Lease), U-Haul International, Inc. (U-Haul International), and various manufacturing companies.

Amerco Lease and various independent fleet owners purchase trucks, trailers, and supporting equipment from the manufacturing affiliates. Amerco Lease and the independent fleet owners lease that property to U-Haul International, an Oregon corporation. U-Haul International then makes the property available to local U-Haul marketing companies, such as appellant, for rent to the public. The gross rental income is divided among the fleet owners (including Amerco Lease), U-Haul International, the marketing companies, and independent dealers. This division of the gross rental income provides the total income for each of the corporations involved.

The Franchise Tax Board determined that, during the years at issue, Amerco Lease was engaged in a unitary business with its parent and affiliated corporations, because of its functional integration with the rest of the corporate group. Appellant argues that Amerco Lease was merely a passive investor in equipment and did not derive any income from California. Appellant appears to concede that the other affiliated companies were engaged in a single unitary business.

A taxpayer which derives income from sources both within and without California is required to measure its California franchise tax liability by its net income derived from or attributable to California sources. (Rev. & Tax. Code, § 25101.) Even if a taxpayer does business solely in California, its income is derived from or attributable to sources both within and without California when that taxpayer is engaged in a unitary business with affiliated corporations doing business outside California. In such a case, the amount of income

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attributable to California sources must be determined by applying an apportionment formula to the total income derived from the combined unitary operations of the affiliated corporations. (See Edison California Stores, Inc. v. McColgan, 30 Cal.2d 472 [183 P.2d 16] (1947).)

A unitary business may exist when there is unity of ownership, unity of operation, and unity of use (Butler Bros. v. McColgan, 17 Cal.2d 664, 678 [111 P.2d 334] (1941), affd., 315 U.S. 501 [86 L.Ed. 991] (1942)) or when the operation of the business within California contributes to or is dependent upon the operation of the business outside this state. (Edison California Stores, Inc. v. McColgan, supra, 30 Cal.2d at 481.) Respondent's determination that affiliated companies are engaged in a unitary business is presumptively correct, and the burden is on the appellant to show that such determination is erroneous. (Appeal of John Deere Plow Co. of Moline, Cal. St. Bd. of Equal., Dec. 13, 1961.)

We agree with the Franchise Tax Board's determination that Amerco Lease was part of the unitary business conducted by its parent and affiliates. It was obviously an integral link in the chain running from the manufacturing subsidiaries to the dealers who rented the equipment to the general public. Appellant has presented no evidence or argument to refute the Franchise Tax Board's determination that the companies were functionally integrated. Its argument regarding Amerco Lease's lack of income from or presence in California goes only to California's jurisdiction to tax it. In the context of determining whether it is part of a unitary business and includable in a combined report, its status as a California taxpayer is irrelevant. (See Appeal of Dasibi Environmental Corporation, Cal. St. Bd. of Equal., Nov. 19, 1986; Appeal of Beecham, Inc., Cal. St. Bd. of Equal., Mar. 2, 1977.)

Appellant argues next that, even if Amerco Lease is included in the unitary group, its income is nonbusiness income allocable entirely to Nevada, rather than apportionable business income. Since its adoption by California in 1966, the Uniform Division of Income for Tax Purposes Act (**UDITPA**) (Rev. & Tax. Code, §§ 25120-25139) has provided a comprehensive statutory scheme of **apportionment** and allocation rules to measure California's share of the income earned by a taxpayer engaged in a multistate or multinational unitary business. UDITPA distinguishes between "business income," which must be apportioned by formula, and "nonbusiness

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income," which is allocated to a specific jurisdiction according to the provisions of sections **25124** through 25127 of the Revenue and Taxation Code. Business and nonbusiness income are defined in Revenue and Taxation Code section 25120 as follows:

(a) "Business **income**" means income arising from transactions and activity in the regular course of the taxpayer's trade or business and includes income from tangible and intangible property if the acquisition, management, and disposition of the property constitute integral parts of the taxpayer's regular trade or business operations.

(d) "Nonbusiness income" means all income other than business income.

The statutory definition of business income provides two alternative tests for determining the character of income. The "transactional test" looks to whether the transaction **or** activity which gave rise to the income occurred in the regular course of the taxpayer's trade or business. The "functional test" provides that income is **business** income if the acquisition, management, and disposition of the property giving rise to the income were integral parts of the taxpayer's regular business operations, regardless of whether the income was derived from an occasional or extraordinary transaction. (Appeal of Fairchild Industries, Inc., Cal. St. Bd. of Equal., Aug. 1, 1980; Appeal of New York Football Giants, Inc., Cal. St. Bd. of Equal., Feb. 3, 1977; Appeal of Borden, Inc., Cal. St. Bd. of Equal.; Feb. 3, 1977.)

Appellant argues that the "taxpayer" here is **U-Haul** co. of Van Nuys, not Amerco Lease and, since Amerco Lease is not part of the taxpayer's trade or business, its income could not be business income under either the transactional or functional test. We need not address the issue of whether Amerco Lease was a "**taxpayer**" as defined in section 23037, because Amerco Lease is included in appellant's trade or business. The "trade **or** business" referred to is that of the unitary business and both appellant and Amerco Lease are part of the same unitary business. **Therefore**, it is the relationship between Amerco Lease's income-producing assets and the unitary business operations **which** determine whether the **income** is business or nonbusiness.

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We must agree with the Franchise **Tax Board** that **Amerco** Lease's purchase and lease of equipment are clearly activities which occurred in the regular course of the unitary business, thus, satisfying the transactional test. It is also clear that the acquisition, management, and disposition of the equipment were integral parts of the regular unitary business operations, satisfying the functional test as well. Therefore, we must conclude that **Amerco** Lease's income was properly determined by the Franchise Tax Board to have been apportionable business income.

Appellant has also objected to the Franchise Tax Board's calculation of the property factor of its apportionment formula. In this case, the property factor is one for all the California companies in the U-Haul system, because appellant elected to file a **single** tax return and pay the entire California tax due for all taxpayers included in the combined report. The property factor of the apportionment formula is defined in section 25.129 as

a fraction, the numerator of **which** is the average value of the taxpayer's real and tangible personal property owned or rented and used in this state during the income year and the denominator of which is the average value **of all** the taxpayer's real and tangible personal property owned **or** rented and used during the income year.

The value of mobile or **moveable** property to be included in the numerator of the property factor is ordinarily computed on the basis of total time the property is within the state during the income year. (Cal, Admin. Code, tit. 18, reg. 25129, **subd. (d)** (art. **2.5**.) However, appellant was unable to provide the data necessary for such a computation. The Franchise Tax Board, therefore, multiplied the California gross receipts factor by the value of all the **moveable** property to compute the portion of **moveable** property to be included in the numerator of the California property factor. In its Reply Brief, at pages 6-7, appellant has stated that it does not object to this method of computing the **numerator** of the property factor. What appellant **apparently** objects to is the inclusion in the property factor of the equipment owned by **Amerco** Lease valued at its original **cost** as provided in section 25130.

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Appellant had apparently included the **moveable** property in the property factor as **property** leased by **U-Haul** International, valuing it at eight times the annual rental rate. Appellant **argues** that the property cannot be included at its original cost, as property owned by the taxpayer, because it was owned by Amerco Lease and Amerco Lease was not a "taxpayer,." We disagree with appellant's conclusion, since **we** believe that Amerco Lease is clearly **a** taxpayer under the pertinent statutes and regulations.

Any corporation subject to the California franchise tax (chapter 2 of the **Bank** and Corporation Tax Law) or the California corporation income tax (chapter 3 of the Bank and Corporation Tax Law) is considered a **"taxpayer."** (Cal. Admin. Code, tit. 18, **reg.** 25121, subd. (a)(1) (art. 2.5); **Rev. & Tax. Code, § 23033**; Cal. Admin. Code, tit. 18, **reg.** 23037.1 Generally, a corporation is subject to the franchise tax if it is doing business in this state. (**Rev. & Tax, Code, § 23151**, subd. (a).) A corporation is subject to the corporation income tax if it has **income** derived from sources within the state. (**Rev. & Tax, Code. § 23501**, subd. **(a).**)

Appellant contends that, in order to include **Amerco** Lease's property in the numerator of the property factor, it must be determined that **Amerco** Lease was doing business in California. As we have indicated above, such a determination is not necessary. **All that must be** found is that Amerco Lease had income from sources within California. That Amerco Lease had income **from** sources within this state **is**, we believe, crystal **clear.**

"Income from sources within this State" includes income from, rentals of, **or** gains realized from the sale of real or tangible personal property **located** in this State, regardless of where the sale or transfer is consummated. **The term** also includes income from ownership, control or management of such property located in this State, even though the taxpayer is not carrying on a business in this State.

(Cal. Admin., Code, tit. 18, **reg.** 23040(a),)

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Amerco Lease received a designated percentage of the revenues generated by the rental to the public of **moveable** property which it owned. Therefore, the income which Amerco Lease received was directly related and attributable to the rental by the public of the **moveable** property owned by it and used in California as well as other states. Constitutionally **sufficient** nexus was also clearly present by virtue of Amerco Lease's regular and systematic pattern of channeling its **moveable** property into this state through its commonly controlled sister corporation, U-Haul International. Amerco Lease's exploitation of the California market for the purpose of earning income from the rental of its **moveable** property, together with the benefits and protections which California provides during the process, is sufficient to satisfy the requisites of due process, and **it makes** no difference that Amerco Lease chose to conduct rental activities through unitary sister corporations. (See Appeal of Dresser Industries, Inc., Opn. on Pet., for Rehg., Cal. St. Bd. of Equal., Oct. 26, t 983.)^{2/}

The foregoing leads us to the conclusion that the Franchise Tax Board properly included Amerco Lease in the combined report, properly treated the income of Amerco Lease as apportionable business income, and properly included and computed the value of the **moveable** *property owned by Amerco Lease in the property factor of the apportionment formula.^{3/} Therefore, the action of the Franchise Tax Board must be sustained.

2/ The situation regarding the property of Amerco Lease **is** in distinct contrast to that of the appellant in the Appeal of John H. Grace Co., decided by this board on October 28, 1980. **In the Grace** appeal, we concluded that the appellant did not **have income** attributable to sources within California where the quantity of its property present in California was minimal; the property was in the control of bailees of the appellant's lessees, who were completely unrelated to the appellant; the lessees paid flat monthly fees for the use of appellant's property; and the presence of appellant's property in this state was entirely **fortuitous**.

3/ In its original protest, appellant objected to the **inclusion** in the property factor of property owned by independent fleet owners. The Franchise Tax Board agreed that some of the property included in the property factor

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3/ (continued))

was owned by independent fleet owners and made a trial computation for the year 1977, eliminating that property from the factor. This trial computation resulted in a small increase in tax due. The Franchise Tax Board has agreed to recompute the tax due for each of the appeal years, if we so order. However, it appears to us that the property of the independent fleet owners should not be eliminated, since it is clearly property that was rented and used in this state, and should, therefore, be included in the property factor at eight times the net annual rental rate. (Rev. & Tax. Code, §§ 25129, 25130,) . Therefore, we see no need for any recomputation to eliminate that property from the property factor.

