BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of	)	
	)	No. 91A-0467-MC
FABERGÉ, INCORPORATED, ET AL.	)	
	)	

For Appellant:	David Steinberg Tax Manager
For Respondent:	Michael J. Breining Counsel

O P I N I O N

This appeal is made pursuant to section 25666[1/] of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of Fabergé, Incorporated, et al., against proposed assessments of additional franchise tax in the amounts and for the income years as follows:

[1/] Unless otherwise specified, all section references are to sections of the Revenue and Taxation Code as in effect for the income year in issue.

Appellants	Income Years	Proposed Assessments
Fabergé Incorporated	1982	$27,165
	1983	24,072
Zizanie De Fragonard, Inc. 0639491, Taxpayer, and Fabergé, Incorporated, 0516266, Assumer and/or Transferee	1983	200[2/]

The question presented in this appeal is whether appellant and its majority-owned subsidiary were engaged in a single unitary business.

Appellant is in the world-wide business of developing, testing, manufacturing, and selling cosmetics, fragrances, toiletries, hair care products, and accessories. In March of 1980, appellant entered into an agreement to acquire up to 80 percent of Arden Industries, Inc., which then changed its name to B.C.S.I. Laboratories, Inc. (BCSI). In March of 1981, appellant acquired approximately 60 percent of BCSI's shares.

Prior to being acquired by appellant, BCSI had developed and patented a breast cancer screening device (hereinafter referred to as the "screening device") that utilized chemical heat sensors to measure the underlying breast temperature in order to detect any breast pathology. This was a noninvasive, nontoxic device which could be used by a woman in her home. If there were significant temperature differences, the woman would be alerted to the need to consult with her physician.

Appellant reached an agreement with BCSI "for the clinical study, development, and commercial exploitation of the" screening device. (Resp. Ex. C., [appellant's Annual Report, 1980].) During 1980, the screening device was clinically tested under the direction of Dr. Karpman, Director of Medical Research at appellant. (Resp. Ex. C., [appellant's Annual Report, 1980].) The testing continued during 1981, and in 1981 the results of the testing were submitted to the Federal Food and Drug Administration for its approval. (Resp. Ex. I., [appellant's Annual Report, 1981].) The FDA asked for additional information, in response to which appellant undertook additional testing, and in February of 1982 its application was resubmitted to the FDA. Eventually, appellant apparently concluded that the screening device was unmarketable, and BCSI was sold in March of 1984.[3/]

[2/] Respondent now concedes that the $200 assessment for 1983 was erroneously issued. Consequently, only the assessment for 1982 and the $24,072 assessment for 1983 remain in issue.

[3/] Appellant was acquired by McGregor Corporation in early 1984, and McGregor determined to sell BCSI.

Appellant filed its franchise returns treating BCSI as part of its unitary business. Respondent examined the returns, and determined that BCSI was not unitary with appellant. Appellant protested, and this appeal follows.

This board has stated the relevant law applicable to the issue of unity many times, most recently in Appeal of Hearst Corporation, 92-SBE-015, decided June 18, 1992. Basically, separate corporations will be considered part of a unitary business if either the three unities test or the contribution or dependency test is satisfied. An important aspect to finding a unitary business is that the separate businesses are an integrated economic enterprise whose parts are characterized by substantial mutual interdependence and a flow of value.

Appellant contends that when it bought BCSI, all BCSI had was a patent. Appellant contends that its personnel performed all of BCSI's administrative functions, such as security, accounting, budgeting, legal, financial, and insurance. Appellant contends that all scientific work was performed by its personnel. It contends that BCSI had virtually no ability to continue development of the screening device and that appellant was completely responsible for such development. Appellant also loaned BCSI approximately $1,500,000. Appellant then cites California Code of Regulations, title 18, regulation 25120, subdivision (b)(3), and concludes that it is therefore unitary.

Respondent contends otherwise, pointing to various documents of appellant's that it contends show that BCSI was a separate company from appellant. Respondent also contends that there is no evidence to support appellant's factual conclusions, and that appellant's own documentation is inconsistent with appellant's factual contentions.

We conclude that, based on the evidence provided, appellant did perform all of the administrative functions of BCSI and that the officers and directors of appellant played a regular role in the operations of BCSI. Therefore, under regulation 25120, subdivision (b)(3), we conclude that appellant was unitary with BCSI.

First, appellant issued a press release in July of 1982 that as of June 16, 1982, appellant's "management personnel has taken control over the operations of BCSI." We believe a statement of a publicly traded company made contemporaneously with the events carries with it some inherent credibility. Second, appellant has submitted an affidavit of its associate corporate counsel indicating that BCSI had no resources and it was the financial and operational resources of appellant which allowed BCSI to submit the screening device to the FDA for approval.

Respondent dismisses the press release as being inconsistent with the other evidence it provided. However, all of respondent's evidence comes from the annual reports of appellant for years 1979, 1980, and 1981. The years in question are 1982 and 1983. We do not find the press release inconsistent with the annual reports. Up until June of 1982, there may have been the very independence respondent claims. However, the press release makes it clear that appellant was then running BCSI - operationally and otherwise. We think appellant has presented sufficient evidence of strong centralized management and centralized administrative functions such that the presumption of unity provided for in

regulation 25120, subdivision (b)(3), applies. We conclude that beginning June 16, 1982, appellant and BCSI were engaged in 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 protest of Fabergé, Incorporated, et al., against proposed assessments of additional franchise tax in the amounts of $27,165, $24,072, and $200 for the income years 1982, 1983, and 1983, respectively, be and the same is hereby modified in accordance with our opinion herein and with respondent's concession regarding the $200 assessment for income year 1983. In all other respects, the action of the Franchise Tax Board is sustained.

Done at Sacramento, California, this 29th day of October, 1992, by the State Board of Equalization, with Board Members Mr. Sherman, Mr. Dronenburg, Mr. Fong and Ms. Scott present.

Brad Sherman, Chairman

Ernest J. Dronenburg, Jr., Member

Matthew K. Fong, Member

Windie Scott*, Member

_____, Member

*For Gray Davis, per Government Code section 7.9
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