BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO

In the Matter of the Protest of [Redacted], Petitioner.	))))))	DOCKET NO. 16497 DECISION

On March 15, 2002, the Income Tax Audit Bureau of the Idaho State Tax Commission issued a Notice of Deficiency Determination to [Redacted] (taxpayer), proposing additional income tax, penalty, and interest for each of the tax years ending 09/30/89 through 09/30/97,[1] inclusive, and the short tax year ending 06/30/98, in the total amount of $1,299,022.

On April 2, 2002, a timely protest and petition for redetermination was filed by the taxpayer. An informal conference was requested by the taxpayer and held on October 22, 2002.

The Tax Commission has reviewed the file, is advised of its contents, and hereby issues its decision affirming the Notice of Deficiency Determination. The issue for decision is whether the taxpayer and its affiliates constituted a unitary business that is subject to combined reporting. The Tax Commission holds that the taxpayer has not presented evidence sufficient to disprove the auditors' findings that a unitary business existed.

Facts

Effect of unity among subsidiaries of ultimate foreign parent;

sources of information

This is a foreign parent unitary case. The unitary group asserted by the Tax Commission only includes the highest [Redacted] and all of its U.S. and foreign subsidiaries, and does not include the ultimate foreign parent or foreign subsidiaries of that foreign parent. The taxpayer

[1] Tax liability was zero for years through 09/30/94.

does not argue for a unitary group larger than that asserted in the Notice of Deficiency Determination.

The constitutional definition of a unitary business is blind to the place of incorporation. *Barclays Bank PLC v. Franchise Tax Bd.*, 512 U.S. 298 (1994). Facts showing interaction between the various U.S. businesses, on the one hand, and the foreign parent and/or its foreign subsidiaries, on the other hand, are relevant in establishing unity within the subgroup of U.S. companies.

Facts in this discussion are generally taken from published press reports, the taxpayer's board minutes, and the foreign parent's annual reports and Securities and Exchange Commission (SEC) filings. The facts are grouped first by general topics, and within those topics are recited chronologically. For ease of understanding after redaction, generic words and pseudonyms are used here to designate companies, people, states, and foreign countries. Years are either calendar years (1993, 1994, etc.) or fiscal years (09/93, 09/94, etc.). Some quotations are edited to conform to American usage.

Organizational overview

The taxpayer manufactures packaged foods for consumers and institutions. It is headquartered outside Idaho in State X. Its Idaho operations consist of [Redacted] During the audit period, the taxpayer was wholly owned by a foreign parent whose primary business is beverages.

In 1987, the foreign parent "determined that our core skills—brand marketing and the management of worldwide operations—were most valuable when applied to businesses which were large, international, and complementary."[2] The foreign parent began divesting diverse

[2] Foreign parent's SEC Form 20-F, 09/93, page 5.

businesses in its home country, keeping its core beverage business. The foreign parent acquired a U.S. pet food company and a U.S. beverage company. The U.S. beverage company acts as the U.S. distributor of the foreign parent's beverage brands.

In 1989, the foreign parent acquired the taxpayer and its subsidiaries, which included a U.S. restaurant chain and a dessert company. The foreign parent acquired a restaurant chain in its home country and then converted those outlets to the brand of the U.S. restaurants. The foreign parent organized the U.S. restaurant chain and a U.S. specialty retailer, together with beverage restaurants in its home country, under a branded retailing division.

The foreign parent's 09/89 annual report states at pages 4 and 5:

> The future success of [the foreign parent] is founded on our appreciation of one key fact, that our brands, whether they be in food, drinks or retailing, are bought by discerning customers with similar tastes and lifestyles in [various parts of the world]. ...
>
> The brand building approach on which [the beverage business's] continuing success is based has also been a key feature in the restructuring of [the taxpayer] and [the U.S. restaurant company] to meet the needs of the 1990s. .... Over the next decade we will continue to build our food interests and reinforce our market position by using our proven skills in the development, marketing and distribution of major brands.
>
> Since January 1989 there has been intense activity in integrating and repositioning [the taxpayer]. Steps taken include: a significant rationalization of organization, increasing accountability down the line and reducing bureaucracy; the disposal of non-strategic businesses; major reviews of production, distribution and systems to streamline costs and bring efficiency to best competitive standards; and intensification of new product development and brand building....
>
> The development of branded retailing continues to be a focus of attention. There are very few truly international or pan-[foreign area] retail brands. We have a worldwide brand in [U.S. restaurant company] and a potential world brand in ... our [specialty retailer]. ... Over the next decade we expect to see an emergence of strong, international retail brands where major benefits will be derived from the pooling of property expertise, marketing skills, systems, procurement and, most

importantly, people. We see our branded retailing operations as a major area of long term opportunity for the group.

The taxpayer's 09/92 SEC filing states at page 9:

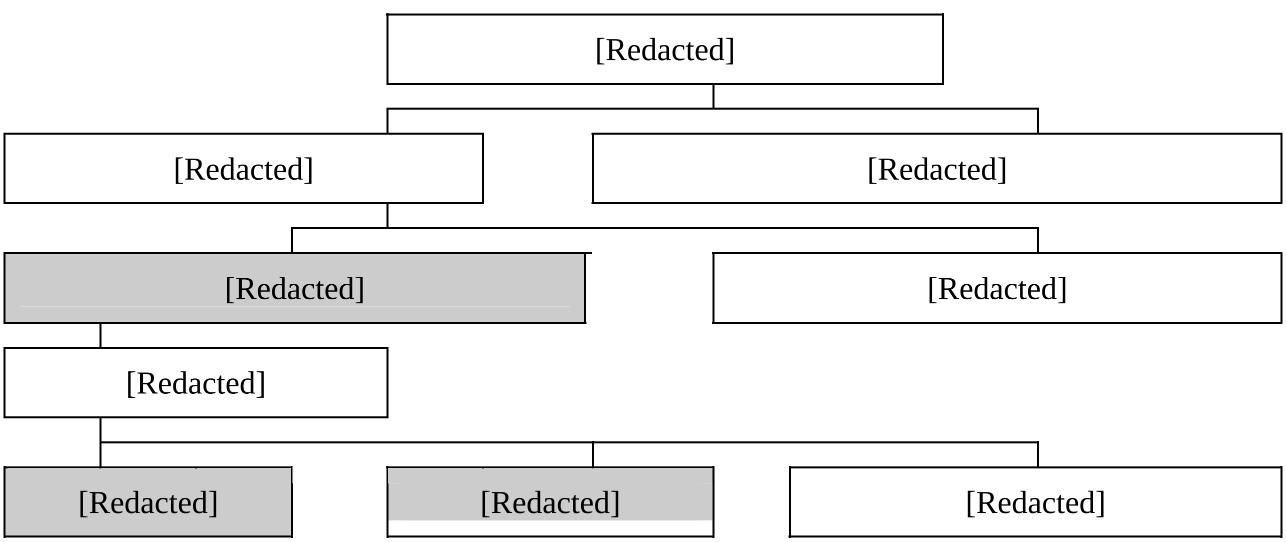
> The [branded retailing division] operates in businesses in which its experience with multi-unit retailing, property management, information and control systems, franchising, distribution and marketing can be applied. ....

The 09/93 annual report explains the synergy between food and beverages at page 7:

> [Our] focus comes from the fact that both the Food and Drinks sectors are targeted at similarly motivated consumers. These consumers eat and drink, are international, and above all are selective and choose added value food and drinks brands. ... There is now a clear cut synergy of management purpose aimed at marketing added value food and drinks brands to similar consumers who in turn are largely reached through the same trade customers.

The foreign parent in 09/94 sold its home country beverage restaurants and in 09/95 sold the U.S. pet food business, leaving the foreign parent and its global subsidiaries in the food, restaurant, and beverage businesses, along with a specialty retail business in the U.S.

Since acquiring the taxpayer in 1989, the foreign parent has conducted its [Redacted] The organization of the foreign parent's holdings in the U.S. as of early 1996 can be diagrammed as follows (ownership percentages are all 100%):



[Redacted] is the indirect parent of the following three major U.S. lines of business:

- The taxpayer, based in State X,
- The restaurant chain, based in State Y, and
- The beverage business, based in State Z.

The taxpayer contends that the beverage business and the holding companies are not unitary with the taxpayer and the restaurant chain. The taxpayer, the dessert company, and the restaurant chain (shaded in the chart) were included in the taxpayer's combined Idaho returns. The beverage companies filed separate returns starting with year 09/94, when Idaho law was amended to require them to maintain inventories in Idaho.

In 1996, the taxpayer sold the U.S. specialty retailer. The U.S. restaurant chain acquired a chain of restaurants in a foreign country where it had not previously operated, with the intent of converting the acquired outlets to the U.S. brand.

Effective late in 1997, the foreign parent merged with a foreign beverage company, took a new name, and changed its fiscal year end to June 30. The subsidiaries of the merged parent now consisted of four main businesses: Two beverage businesses, a restaurant chain, and the taxpayer's food business. For Idaho purposes, the auditors have not added subsidiaries of the foreign beverage company to the previous unitary group of subsidiaries of the pre-merger foreign parent of the taxpayer.

<u>Changes in reporting and divisional structures over time;</u>

<u>unitary ties between the U.S. companies and non-U.S. companies</u>

The foreign parent has repeatedly reorganized the reporting structures of its subsidiaries. The foreign parent's 09/89 annual report shows a foreign foods group, comprising the taxpayer's foreign operations along with a foreign subsidiary of the foreign parent. "These recently acquired businesses [of the taxpayer] and those transferred from [existing foreign subsidiaries of the foreign parent] are all trading successfully."[3]

A 1989 press report states that the taxpayer's information systems department, neglected before the foreign parent acquired the taxpayer, was "integrated into all the [foreign parent's information systems] operations so that the [taxpayer's] staff could provide the right information at the right time." In documenting claims for Idaho investment tax credits, the taxpayer provided two forms entitled, "[Redacted]," dated mid-1989. The first form authorizes replacement of computers at Idaho food plants. It states, "Final approval given by [the executive referred to below by the pseudonym [Redacted], then still with the foreign parent] June 7, 1989." The second form also deals with computers. It states, "Project approved by [foreign parent] 6/15/89." Both of these forms state, "This project is included in the [foreign parent] approved three year [Redacted] strategic plan." The foreign parent's 09/89 annual report states that a common electronic mail system "is improving communication links between office locations [in foreign countries] and the U.S. and providing a readily accessible information base for office staff. New 'electronic notice boards' have been successfully tested and the system regularly transmits over 40,000 mail items monthly between its 1,600 users."[4]

The foreign parent's 09/89 annual report at page 8 displays a photograph of the foreign parent's board of directors meeting at the taxpayer's headquarters in State X in November, probably in 1989.

The foreign parent has a real estate division that manages commercial properties that are owned and operated by the foreign parent and its subsidiaries in the foreign parent's home

[3] Foreign parent's annual report, 09/89, page 13.

[4] Foreign parent's annual report, 09/89, page 35.

country. According to the foreign parent's 09/92 SEC filing at page 11, the foreign parent's real estate division "provides advice and assistance on property matters to Group companies in North America and [elsewhere] ...."

In 09/93, the taxpayer, the U.S. pet food and dessert companies, but not the U.S. restaurant chain, were placed within a division known as [foreign parent] [Redacted], based in State X. A division known as [foreign parent] [Redacted] comprised the taxpayer's brands and the dessert company's brand in another continent along with brands derived from other subsidiaries of the foreign parent. All of these, together with the U.S. restaurant chain and the U.S. specialty retailer, comprised the foreign parent's foods sector.

In 09/94, the foreign parent withdrew the taxpayer's brands from parts of Europe. [Foreign parent] [Redacted] was renamed with the taxpayer's name. The foreign parent centralized its internal audit function and consolidated its treasury function in the foreign parent's home country.[5] "Capital expenditure was tightly controlled, and decreased ...." [6] [The company] performs detailed post investment appraisals of the results of acquisitions and major capital expenditure projects."[7] The 09/94 annual report at page 38 states that policy manuals on internal controls "apply to all business units." In 09/94, "in an exciting cross sector initiative, [two beverage] flavors of [dessert] ... entered the U.S. market."[8]

In 09/95, the dessert company's North American operations and a food company acquired by the taxpayer in that year became a division of the taxpayer. The foreign parent

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[5] Foreign parent's annual report, 09/94, page 28.

[6] Foreign parent's annual report, 09/94, pages 28 and 39.

[7] Foreign parent's annual report, 09/94, page 39.

[8] Foreign parent's annual report, 09/94, page 7.

negotiated an ocean freight agreement with trans-Atlantic shipping companies under which it received volume discounts by combining beverages and foods under the same service contract. The foreign parent also issued preferred stock in the U.S. for the first time.

In 09/96, the foreign parent eliminated its food division, so that the heads of the U.S. businesses reported directly to a group chief executive in the foreign parent. [Foreign parent] Foods [foreign area] was renamed [Taxpayer] [foreign area], the smaller brands were put up for sale, and the marketing focus in the other continent was concentrated on the taxpayer's brands. The foreign parent promoted an individual from the foreign beverage business to be group marketing director for the entire unitary business, with a mission to develop coherent marketing across all of the company's brands in all countries, including beverages, foods, and restaurants. He reported to the chief executive of the foreign parent. He retired in 1997.

Minutes of the taxpayer's board of directors' committee on organization development for February 15, 1996 discuss stock ownership plans for U.S. employees and redesign of pension plans, and say, "Discussion of possible alternatives should be initiated with [the foreign parent]." Minutes for April 9 and 10, 1996, of the taxpayer's board of directors discuss a report of the board's audit and compliance committee, and state that the board asked a named senior vice president "to coordinate and work with [a named individual] for [the foreign area foods division] operations and audit and risk management issues." The same minutes report that the taxpayer's senior vice president of human resources "advised the board of the upcoming ... review in [foreign parent's headquarters city]." On May 21, 1996, the taxpayer's board of directors elected the chief executive officer of the foreign parent as the taxpayer's "chairman emeritus," an advisory role. On September 17, 1996, the board's organization development and compensation committee reported that the taxpayer's senior vice president of human resources "was meeting with [the foreign parent's] Human Resource personnel to review and recommend implementation of a new restricted stock program."

On September 17-19, 1996, the operating committee of the taxpayer's board met to discuss standardized formats and processes required by the foreign parent for strategic planning. Certain of the taxpayer's directors were to review planning criteria for a presentation to the foreign parent. Minutes for November 19, 1996 of the audit and risk management committee of the board discuss a report by a named individual on risk management, and on the [foreign parent's] "global property program."

In the year ended 09/97, the foreign parent tapped a New York advertising agency to handle buying of print advertising in the U.S. for both the beverage and food lines of business.

On March 10, 1997, the foreign parent's executive committee was to visit the taxpayer's headquarters city in the U.S. to review the taxpayer's strategic plan, presented by the taxpayer's directors and officers. On February 20, 1998, the minutes of the business operations committee of the taxpayer's board of directors discuss a risk assessment of the taxpayer by the foreign parent's internal audit group.

Minutes of the business operations committee of the taxpayer's board of directors for April 14, 1998 discuss "proposed new incentive and compensation initiatives which more closely align [the taxpayer's] management with its shareholder, [the newly merged foreign parent. A named individual] indicated that ... it was likely that the [foreign parent] board would approve these plans in some form in the near future."

The taxpayer answered a unitary questionnaire for the audit. It is not clear from the questionnaire whether the facts stated were constant throughout the audit period or have evolved during that period, or whether the present tense used in the replies to the questionnaire means that the answers given relate back throughout the audit period.

According to the unitary questionnaire, U.S. employees are allowed to participate in tax-qualified plans to purchase American depositary shares of the foreign parent. The questionnaire reports that there are no limits imposed by [Redacted] or the foreign parent on the U.S. companies' contracts, daily operations, employee compensation, hiring and firing, budgets, or capital investments. However, another part of the questionnaire states that capital projects in excess of $15 million "require approval of the [foreign parent] executive committee." The minutes for January 10, 1997, of the business operations committee of the taxpayer's board of directors discuss a capital spending proposal for a food packing line costing $52 million. The committee approved the proposal and chose its location from among three alternatives. Approval from the foreign parent would be sought in March of 1997.

According to the questionnaire, each U.S. business unit prepares a quarterly summary of year-to-date earnings and cash flow and a forecast of earnings and cash flow for the remainder of the year. These quarterly reports are submitted to the foreign parent.

<u>Foreign parent executives' involvement in U.S. businesses</u>

When the foreign parent acquired the U.S. beverage business in 1987, the foreign parent sent an individual, referred to here by the [Redacted], from the foreign parent's board to run the U.S. beverage business. When the foreign parent acquired the taxpayer and the restaurant company in 1989, [Redacted] moved to State X as the taxpayer's chairman, where he drastically downsized the corporate staffs of the taxpayer and the restaurant company. "Following the acquisition of [the taxpayer, the foreign parent] began streamlining [the taxpayer]'s operations, resulting in cost savings and increased efficiencies. These streamlining activities included a reduction in the number of employees and the consolidation of production and distribution facilities."[9] The foreign parent committed itself to diversity in the U.S. work force, rolled out a new and expanded diversity training program, and then adopted a similar program in its home country, with the U.S. program as a model. [Redacted] also chaired the restaurant company and [Redacted] and held the post of Chief Executive, Food Sector with the foreign parent. [Redacted] returned to the foreign parent in 1991 as its chief operating officer.

The foreign parent's 09/89 annual report states that the foreign parent's senior management training program with a university in the parent's home country "has been extended to the United States using [a U.S. university]. Both programs are open to [managers] worldwide."

Another officer of the foreign parent, [Redacted], was sent in 1991 to the taxpayer as chief operating officer, and then became chief executive of the taxpayer in 1992. In 1992, a board member of the foreign parent and chief of its beverage business became the taxpayer's chairman and chief of the foreign parent's food sector. In 1995, [Redacted] also became additionally responsible for European food operations of the foreign parent while remaining posted in State X.

The U.S. restaurant company had a succession of chief executives, most sent by the foreign parent. A foreign parent executive, [Redacted], formerly responsible for foreign restaurants, joined the U.S. restaurant company as CEO from 1989 to 1991, and as chairman from 1991 to 1993, replacing [Redacted]. "Following its acquisition [by the foreign parent] as part of [the taxpayer] in 1989, significant changes were initiated at [the restaurant company]. A number of redundant tiers of management were removed and store level operations underwent a

[9] Foreign parent's SEC Form 20-F, 09/92, page 4.

major review, focused on improving staff training, incentives and recruitment. Efforts were also made to improve ... restaurant operations."

[Redacted] was succeeded by an individual recruited from outside the unitary group, who only stayed briefly. Then the foreign parent sent an individual, [Redacted], the head of the food division of the foreign parent since 1993, as interim chief executive. [Redacted] traveled frequently between the foreign parent's headquarters and the restaurant chain's headquarters in State Y. An individual, [Redacted], was transferred in 1995 from the foreign parent to the U.S. restaurant company as CEO, succeeding [Redacted] He then was promoted to the foreign parent's executive committee.

In 1997, an individual, [Redacted], was transferred from the foreign parent's beverage division to the U.S. restaurant company to replace [Redacted]. Another foreign parent officer, [Redacted], became chairman of the restaurant company. The stated goal was to expand the restaurant chain faster outside the U.S.

<u>Holding companies and US Investment Co.</u>

The three U.S. holding companies--[Redacted] are all based in State X in the same city as the taxpayer. The Tax Commission has not explored in detail the function of these four companies nor the sources and destinations of any intercompany flows of funds or services involving them.

The taxpayer provided the income by company behind the federal consolidated return for years ending 09/91 through 09/98, and pro forma separate forms 1120 for the four companies for the periods ending 09/93 through 06/98, inclusive. The tax returns show the following amounts of taxable income (line 28) for the four companies (in $ millions):

	USHC1	USHC2	USHC3	US Investment Co.	Total after eliminations
09/91	-10	9	139	1	139
09/92	5	9	114	1	129
09/93	-3	10	0	101	108
09/94	0	13	81	-447	-353
09/95	-16	31	58	104	177
09/96	-12	316		61	365
09/97	0	28		63	92
06/98	-163	26		49	-88

The cumulative taxable income of these four companies for the years shown is $569 million.

[Redacted] income is primarily from dividends, and it appears to have a full complement of operating expenses. [Redacted] large loss in 06/98 is caused by "other deductions," which have not been investigated.

[Redacted] income is primarily from dividends, except in 09/96, when it also had large capital gains, possibly from the sale of the U.S. specialty retailer. [Redacted] has a few small operating expenses. [Redacted] has interest income and minimal expenses and was liquidated in 09/95.

[Redacted]. has large amounts of interest income and interest expense, with the two amounts offsetting each other in varying degrees in all years except 09/94, when it had large dividend income with even larger interest expense. [Redacted] issues commercial paper, notes, and bonds in the U.S. on behalf of the foreign parent. The [Redacted] first issue of bonds in 1991 was guaranteed by the foreign parent. With that issue, the foreign parent began filing disclosure documents with the Securities and Exchange Commission.

According to the unitary questionnaire, the [Redacted] "acts as the corporate banker for all the operating companies. [It] lends money to the operating companies for their expansion and working capital. [It] performs a daily cash sweep of the cash raised by each of the businesses."

<u>Interlocking officers and directors in the U.S. businesses</u>

As of 09/92, [Redacted] was chairman of [Redacted].

As of 09/94, a group chief executive of the foreign parent was chairman of the taxpayer. The CEO of [Redacted]was also CEO of the [Redacted]. The CFO of [Redacted] was also CFO of the taxpayer and an officer of US Investment Co. The treasurer of [Redacted] was also treasurer of [Redacted]. The general counsel of [Redacted] held the same office in the taxpayer, and was also a senior vice president of USHC2, US Investment Co., and USHC3. The chairman of [Redacted] was also president of [Redacted] An individual was an officer of [Redacted], the taxpayer, the restaurant company, and the beverage company. Five individuals had the same officer positions in both [Redacted]; one of these was also an officer of the taxpayer; and another of these was an officer of the restaurant company. A senior executive vice president of the taxpayer, [Redacted] above, was also president of [Redacted]. Interlocks among directors were similar in scope but are not detailed here.

<u>Unitary facts within the U.S. operating businesses</u>

The unitary questionnaire states that the three U.S. lines of business had zero sales of goods and services between them.

The questionnaire states that the three U.S. lines of business have chief executives appointed by the foreign parent. Below that level, each company appoints its own officers. The three U.S. lines of business share common departments (and some officers) for tax, treasury, corporate accounting and consolidation, and investor relations. According to minutes of

December 4, 1996, an individual resigned as a director and/or officer of 23 affiliated corporations, including the taxpayer and several of its food subsidiaries, [Redacted] and the dessert company. According to the questionnaire, in 1997, the restaurant company began running its enterprise software on the taxpayer's mainframe computer.

Board of directors' minutes for February 28, 1997 state that the taxpayer's pension management group would be taking over management of the pension plan for the [Redacted]

The questionnaire states that the three U.S. lines of business do not share common physical facilities or offices, legal counsel, communications facilities or equipment, manuals or brochures, insurance programs, or pension and other employee benefit plans, with the exception of the stock purchase plans mentioned above. Also separate among the three U.S. lines of business are departments such as accounting, sales, purchasing, human resources, marketing, advertising, budgeting, research, and management services. The taxpayer states that no individual traveled outside his or her company to visit any other affiliate.

Law and analysis

Idaho Code § 63-3027(t) provides that two or more corporations may be considered a single corporation for income tax purposes, provided more than 50% of the voting stock of each of them is owned directly or indirectly by a common owner or owners, and such treatment is necessary to accurately reflect income. The Idaho Supreme Court has interpreted this statute to require combined reporting by a unitary business. *E.g., Albertson's, Inc. v. State, Dept. of Rev.*, 109 Idaho 810 (1984). The taxpayer does not dispute that the ownership requirement is satisfied here.

Unitary business is a concept of constitutional law under the Commerce and Due Process Clauses. A state may tax the multistate income of a nondomiciliary corporation if there is both a "minimal connection" between the interstate activities and the taxing state, and a rational relationship between the income attributed to the taxing state and the in-state value of the corporate business. A state need not attempt to isolate the in-state income producing activities from the rest of the business. The state may tax an apportioned share of the multistate business if the business is unitary. But the state may not tax the business' income that is "derived from unrelated business activity" or a "discrete business enterprise." *Allied-Signal, Inc. v. Director, Div. of Tax.,* 504 U.S. 768, 772-773 (1992)(citations and internal quotation marks omitted); *Albertson's, supra,* 106 Idaho at 815 n.4.

In 1965, Idaho adopted with slight modification the Uniform Division of Income for Tax Purposes Act (UDITPA), Idaho Code § 63-3027. The Act contains a formula for determining the portion of a corporation's total income from a multistate business which is attributable to Idaho and therefore subject to Idaho's income tax.

Combined reporting is a refinement of the apportionment principle. Its purpose is to permit application of the UDITPA apportionment formula to a single business enterprise that is conducted by means of separately incorporated entities. In an economic sense, such a business is no different from a similar business composed of a single corporation with several separate divisions. For tax reporting, such businesses should be treated the same. Combined reporting can be required only in the case of a unitary business. When the Tax Commission has found that a subsidiary is part of the taxpayer's unitary business, then the taxpayer has the burden of proving that the finding is incorrect. *Albertson's, supra,* 106 Idaho at 814-815. Here, the auditors have so found, and the taxpayer has the burden of disproving the finding.

Among the tests of unity is whether "the operation of the portion of the business done within the state is dependent upon or contributes to the operation of the business without the state [; if it does], the operations are unitary." *Edison Cal. Stores v. McColgan,* 30 Cal. 2d 472, 481, 183 P.2d

16, 21 (1947), *quoted at* 106 Idaho at 815. In general, the U.S. companies, including the taxpayer, depend on the foreign parent's proven skills in the development, marketing, and distribution of major brands. The [Redacted] depends on the foreign beverage business for supply, and the foreign beverage company depends on the [Redacted] for distribution. The foreign restaurant chain shares the brand name of the [Redacted], showing the latter's contribution to the former.

Another test asks "whether contributions to income result from functional integration, centralization of management, and economies of scale." *F. W. Woolworth Co. v. Taxation & Rev. Dept.*, 458 U.S. 354, 364 (1982), *quoted at* 106 Idaho at 816. Both the Food and Drinks sectors are targeted at similarly motivated consumers. There is a clear cut synergy of management purpose aimed at marketing value added food and drinks brands to similar consumers who in turn are largely reached through the same trade customers. In branded retailing, the foreign parent's strategy is to pool its expertise in property, its marketing skills, systems, procurement and, most importantly, people. The foreign parent's real estate division advises subsidiaries in North America. The foreign parent placed the taxpayer's foreign area marketing organization in the same structure with the foreign parent's prior food marketing arm. In 09/94, the foreign beverage unit began providing key ingredients to the U.S. dessert company. The foreign parent used the U.S. Investment Co. to issue bonds on behalf of, and guaranteed by, the foreign parent.

Upon acquiring the taxpayer, the foreign parent integrated the taxpayer's information systems, including a common electronic mail system, with its own, upgrading the computer facilities of the Idaho plants in accordance with a central plan. The foreign parent in 09/94 centralized the internal audit function and consolidated its treasury function in the foreign parent's home country. U.S. employees can buy American depositary shares in the foreign parent. The foreign parent in its home country adopted diversity programs from the U.S. companies.

The foreign parent has exercised its strong central management by repeatedly shuffling the reporting relationships of the U.S. companies with its own hierarchy. It has sent a series of top executives from its home country to run the taxpayer and the U.S. restaurant chain. Those individuals imposed draconian cost-cutting measures on the U.S. offices and plants. Capital expenditure "was tightly controlled," in the words of the 09/94 annual report. Policy manuals apply to all business units. The available U.S. board minutes are replete with references to reviews by and coordination with various levels of foreign parent management. The officers and directors of the three [Redacted] are tightly interlocked.

As for economies of scale, the foreign parent arranged a transatlantic freight contract to combine food and beverages for volume discounts. The foreign parent also arranged for a common advertising agency for the U.S. food and beverage lines of business. University management training programs in both the U.S. and the foreign parent's home country are open to managers worldwide. The [Redacted], which along with the three [Redacted] companies centrally accumulated $569 million in profits from the operating [Redacted] over eight years. The pension plan of the [Redacted] business is managed by the taxpayer's pension staff. The restaurant chain runs its enterprise software on the taxpayer's mainframe computer.

Accordingly, the Tax Commission finds that the taxpayer was engaged in a unitary business during the years in issue, and it is therefore required to file a combined report as computed in the Notice of Deficiency Determination.

The 10% penalty for substantial understatement of tax, Idaho Code § 63-3046(d), is affirmed because the taxpayer's filing position with respect to unity was not separately disclosed in the return, and was not supported by substantial authority.

Conclusion

WHEREFORE, the Notice of Deficiency Determination dated March 15, 2002, is hereby APPROVED, AFFIRMED, and MADE FINAL.

IT IS ORDERED and THIS DOES ORDER that the taxpayer pay the following tax, penalty, and interest (computed through 06/04/03)(interest runs at $120.92 per day):

YEAR	TAX	PENALTY	INTEREST	TOTAL
09/30/95	$192,178	$19,218	$109,146	$320,542
09/30/96	198,308	19,831	96,684	314,823
09/30/97	224,993	22,499	89,535	337,027
06/30/98	267,235	26,724	90,354	384,313
			TOTAL DUE	$1,356,705

DEMAND for immediate payment of the foregoing amount is hereby made and given.

An explanation of the taxpayer's right to appeal this decision is enclosed with this decision.

DATED this _____ day of ____________________, 2003.

IDAHO STATE TAX COMMISSION

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COMMISSIONER

CERTIFICATE OF SERVICE

I hereby certify that on this ____ day of _______________, 2003, a copy of the within and foregoing DECISION was served by sending the same by United States mail, postage prepaid, in an envelope addressed to:

[REDACTED] Receipt No.

____