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Memorandum

To: Mr. Trow Hendrick   Date: September 8, 1977
      Collections

From: Susan M. Wengel
        Legal

Subject: Parent's Liability for Subsidiary's Tax

You have asked for a brief analysis of when a subsidiary's tax liability can be passed on to the parent corporation.

When a parent corporation and its subsidiary are true corporations conducting their respective business as a holding company and as an operating company, their transactions must be given recognition unless they are in some way tainted.

In the case of In re Prizant & Co., 24 AFTR 2d 69-5623 (DCND Ill. 1969) the court found that a parent corporation was liable in bankruptcy proceedings for taxes due from the subsidiary. This liability was based on the theory that the companies were so clearly related that they shared a single identity. (This "identity theory" is one method of setting aside the legal protections afforded a corporate entity.)

The following are factors which the Prizant court considered:

1.   The parent owned the stock of the subsidiary.

2.   They shared the same officers and facilities.

3.   They functioned as a single unit. (In this case the parent employed all the administrative sales and clerical help; one subsidiary employed only labor; and the second subsidiary employed only draftsmen. All together they functioned as a unit constructing and installing commercial heating and cooling systems.)

4.   The subsidiaries dealt only with the parent company.

5.   There were minimum amounts of paid-in capital. (For example, a sub may have no cash surplus and will rely only on inter-company transfers of funds to meet its obligations. This indicates that the parent has control. Consequently if the parent did not transfer funds to the sub, it could not pay its tax obligations.)

Other factors which may be considered are:

6.   Parent owns the building and the furniture.

7.   Both employ the same attorney.

        [Witkin, Summary of California Law § 11 (8th ed 1974).]

If you have any further questions please feel free to call me at 5-6366.

SMW/at