Setting Up a Holding Company and Subsidiaries

A parent company over your operating companies can organize your affairs and contain your risks. It can also double your paperwork and trip a tax rule you never heard of.

Someone owns a business, then a rental, then a second business. Somebody tells them to put a holding company on top. It sounds like the grown-up thing to do, and sometimes it is. Other times it adds an entity, a bank account, and a tax return without protecting anything the owner was worried about.

This guide explains what a holding structure does and does not do, how to build one from scratch or around companies you already own, and where the tax law sets traps. It applies to limited liability companies and corporations, formed in any state.

What a Holding Structure Does

A holding company owns other companies. It usually runs no business of its own. Each subsidiary runs one business or holds one asset.

- **Liability separation.** A claim against one subsidiary generally reaches that subsidiary's assets, not its siblings'. A tenant suing your rental company should not be able to reach your consulting company's receivables.
- **Administration.** One parent can hold the ownership records, receive distributions, and make decisions for every subsidiary. Adding or selling a business means adding or selling a subsidiary, not reworking your personal ownership.
- **Privacy.** When a subsidiary's public filings list the parent as its owner or manager, your name may not appear on that subsidiary's record. How much the parent's own filings disclose depends on the state where it is formed.

What It Does Not Do

- **It does not protect you from your own conduct.** If you personally sign a guarantee, commit a wrong, or ignore the separation between companies, no number of layers stands between you and the claim.
- **It does not protect the parent's equity.** The holding company owns every subsidiary. A creditor of the holding company, or of you personally, looks at what the holding company owns.
- **It does not make you anonymous.** Your bank, the IRS, a court, and anyone who can issue a subpoena can learn who owns the parent. The structure changes what the public record shows, nothing more.
- **It does not undo the past.** Once your name is on a public record, it generally stays there. Moving an existing company under a new parent changes future filings. Archived filings,

deeds, and data aggregators keep the old ones.
- **It does not lower taxes by itself.** A holding structure is mostly a liability and administrative tool. The tax result depends on how each entity is classified, and a poor choice can cost money.

When It Is Overkill

One business with modest risk usually needs one company, good insurance, and clean records. A holding structure starts to earn its cost when you have two or more businesses or assets with different risk profiles, when you expect to add or sell pieces separately, or when co-owners differ from one venture to the next. Each additional entity means its own filings, fees, bank account, books, and possibly a tax return, every year, whether or not anything happens. Insurance sized to the risk often does more for less.

Building from Scratch

- **Form the parent first.** Choose the entity type with the tax result in view (see below). Pick a formation state for practical reasons: where you live, what the state charges each year, what its filings make public. A state chosen for its reputation still leaves you registering and paying in the states where you actually operate.
- **Form each subsidiary where it makes sense.** A company that operates, employs people, or owns real estate in a state will usually have to register there even if formed elsewhere. Forming it in that state often avoids paying two states.
- **Make the parent the owner on paper.** The parent is the sole member of each LLC subsidiary or the sole shareholder of each corporate subsidiary. Each subsidiary's operating agreement or bylaws should say who manages it and who may sign for it.
- **Get an EIN and a bank account for every entity.** No shared accounts. A subsidiary with no account of its own has no practical separation from its siblings.
- **Plan succession at the top.** If you want your ownership to pass to a trust or to family at your death, address it in the parent's governing documents or your estate plan, coordinated with each other.

Moving Existing Companies under a New Parent

An existing company becomes a subsidiary when its owners transfer their ownership to the parent. The company itself keeps its name, its contracts, and usually its EIN. Get a tax review before you sign anything (next section). Then:

- **Read the existing documents.** The operating agreement, bylaws, or shareholder agreement may restrict transfers or require consent of the other owners. Get every required consent in writing first.
- **Sign the transfer.** An assignment of membership interest for an LLC, or a stock assignment (with any certificates endorsed or cancelled and reissued) for a corporation. Date it. That date is your evidence of when the parent took over.
- **Update the records.** The ownership ledger or stock ledger, the operating agreement schedule, and any state filing that lists owners or managers.

- **Give notice where the change matters.** Lenders and landlords often treat a change of ownership as a default or require consent. Insurers need to know who the owner is. Licensing bodies, franchisors, and some government contracts require notice or approval of ownership changes.
- **Fix the banking.** The bank will want the new ownership information and may require new signature cards. Keep the subsidiary's own account; open a separate one for the parent.
- **Mind partial ownership.** If only some owners move their interests into a holding company, the subsidiary ends up owned by a mix of individuals and companies. That is workable, but the other owners must agree, and the governing documents should say how the arrangement works from then on.

The Tax Effects, by Structure

This is where holding structures go wrong most often, because the changes happen automatically when ownership changes.

- **A multi-member LLC that becomes wholly owned by the parent.** It stops being a partnership for tax purposes and becomes a disregarded entity: its income and expenses show up on the parent's return. The old partnership files a final partnership return for the year of the change, and the K-1s stop. How the parent picks up the partnership's history is a question for the tax review.
- **An S corporation under the wrong parent.** Only individuals, estates, certain trusts, and certain exempt organizations may own S corporation stock. An LLC taxed as a partnership cannot. A C corporation cannot. Transfer the stock to either one and the S election ends on the day of the transfer, often without anyone noticing until the next return. (An LLC with one individual owner that is disregarded for tax purposes is treated as that individual and generally can hold S corporation stock.)
- **An S corporation parent over a corporate subsidiary.** When an S corporation owns 100% of a corporation, it may elect to treat the subsidiary as a qualified subchapter S subsidiary (a QSub) by filing Form 8869. The subsidiary then disappears for federal tax purposes and reports through the parent. Without the election, owning the subsidiary's stock does not by itself end the parent's S status, but the subsidiary is a separate C corporation paying its own tax. Moving an existing S corporation under a new S corporation parent is usually done as a specific reorganization sequence designed to keep the original S election alive. Order and timing matter.
- **A C corporation parent.** A C corporation that owns at least 80% of the vote and value of other corporations can file one consolidated federal return for the group, offsetting one subsidiary's losses against another's income. Dividends between members of the group are generally eliminated. State treatment varies. Profits that leave the group for you are still taxed twice: once at the corporate level and again as dividends.
- **An LLC parent taxed as a partnership.** Flexible for LLC subsidiaries, which become disregarded and report through the parent's partnership return. Incompatible with S corporation subsidiaries, as above.
- **Contributing property to a corporation.** Transfers to a corporation are generally

tax-free only if the transferors control at least 80% of it immediately afterward and the property is not carrying more debt than its basis. Getting appreciated property back out of a corporation later is generally taxable.

If you own an S corporation, get a tax review before it moves under a holding company. A terminated S election generally cannot be re-elected for five years without IRS consent, and the mistake is easy to make and expensive to fix.

Money Flows through the Parent

A structure is only as good as the discipline behind it. Courts look past companies whose owners treat them as one pot of money.

- **Contributions go down through the parent.** You contribute to the holding company. The holding company contributes to the subsidiary. Document each step with a written consent or resolution.
- **Distributions come up through the parent.** The subsidiary distributes to the holding company. The holding company distributes to you. Document each step.
- **Money between subsidiaries is a loan or a payment for something.** If one subsidiary funds another, sign a promissory note with interest and a repayment schedule, or route the money through the parent as a distribution and a contribution.
- **Shared assets need agreements.** If one subsidiary uses another's building, equipment, or staff, put a lease, a services agreement, or a cost-sharing agreement in writing, at a price a stranger would pay, and actually pay it.
- **Separate books and accounts for every entity.** Never pay a subsidiary's bills from your personal account or from a sibling's account.

A Note on Privacy

If privacy is a goal, plan it before the first filing. Once your name appears on a company's public record, a deed, or a lien, assume it stays findable. A new parent can keep your name off future subsidiaries' records. It will not scrub the old ones. And whatever the public sees, banks verify who owns every company they open accounts for.

Related reading at bjoffrionconsult.com/blog: "What a holding company does, and what it doesn't" and "How many LLCs do you actually need for rental property?"

If You Want This Structured for Your Companies

Multi-State or Holding Company Plan — from $2,600. Which entities to form or keep, which owns what, where each must register, how money moves among them, and a written account of what the structure does not protect against.

Restructuring Tax Analysis — from $1,500. The tax result of moving existing companies under a parent, including S elections, final partnership returns, QSub and consolidated return options, and the order of steps that avoids an unplanned tax.

Entity Structure Audit — from $850. A written review of the companies you already have: what each does, where filings, ownership records, and tax classifications disagree with reality, and what to fix in what order.

The fee for a consultation is credited in full toward any written work you commission within 30 days.

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1500 N Grant St Ste N, Denver, CO 80203 · brandi@bjoffrionconsult.com · www.bjoffrionconsult.com
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