COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

B-170536

SEP 21 1972

Ernst-Theodore Arndt, Esquire
1211 Autre Court
Rockville, Maryland 20851

Dear Mr. Arndt:

Reference is made to your letter of May 30, 1971, requesting reconsideration of our decision of March 15, 1971, B-170536, 50 Comp. Gen. 627; your supplemental letter of December 16, 1971, and; your "Summation, Appeal for Review" forwarded here by your letter of July 16, 1972, all dealing with the same matter. This last mentioned document is largely a summary of the issues raised and discussed in your letters of March 15 and December 16, 1971, together with related exhibits and an attachment thereto that sets out your account of the discussion which took place regarding those issues during the conference with representatives of our Office on January 25, 1972.

Primarily, you are concerned with the conclusion reached in that decision with regard to allegations by Apache Flooring Company (Apache) that Armstrong Cork Company (Armstrong) had been given preferential treatment over Apache under a tile supply contract. It is contended that Armstrong was accorded preferential treatment in that Armstrong has not been required to comply with the equal employment opportunity provisions of Executive Order 11246 and the regulations issued thereunder (41 CFR 60-1.40(c)) requiring the submission of an affirmative action plan for each of its establishments within 120 days from the commencement of its contract.

Concerning this matter, Executive Order 11246, September 24, 1965, as amended, sets forth policies regarding equal employment opportunity (EEO) requirements. Under section 201 of the Order the Secretary of Labor is required to adopt rules and regulations and issue such orders as he deems necessary and appropriate to achieve the purposes of the Order in Government contracts.

The facts concerned in this case are fully set forth in our earlier decision and, therefore, will not be repeated in detail here. It may be noted, however, that the guidelines established by the Department of Labor for determining whether a parent and subsidiary are to be considered as

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a single entity for the purpose of the Executive Order and 41 CFR 60-1.40(a) which requires each prime contractor to "develop a written affirmative action compliance program for each of its establishments" were stated in letter of February 26, 1971, addressed to you by the Solicitor, Department of Labor, to be as follows: (1) common ownership (2) common directors and/or officers (3) de facto exercise of control (4) unity of personnel policies emanating from a common source and (5) the dependency of operations.

The General Services Administration (GSA), being the contracting agency, was primarily responsible for determining whether Armstrong had defaulted under its contract by reason of the fact that it had not complied with 41 CFR 60-1.40(a) in that it had not submitted an affirmative action compliance program for its subsidiary the Thomasville Furniture Industries, Inc. (Thomasville).

The above criteria were considered by GSA in its legal memorandum of January 28, 1971, and it was concluded that Armstrong, although it had potential control over Thomasville, did not exercise de facto day-to-day control over the subsidiary. As stated in our earlier decision, the Department of Labor did not find such conclusion to be erroneous nor did we, upon review of the evidence and arguments considered by GSA, find its conclusions and interpretation of Labor's guidelines to be arbitrary or capricious or not supported by substantial evidence. Accordingly, and since, as stated above, the regulations here involved were issued pursuant to the Executive Order and section 60-1.44 of those regulations provides that rulings under or interpretation of, such regulations shall be made by the Secretary, we concluded that there existed no valid basis for us to object to GSA's refusal to require Armstrong to submit an affirmative action program for its subsidiary, Thomasville.

In asking that we reconsider our earlier decision you list in your letter of May 30, 1971, what you believe constitutes seven errors therein. Such errors are set out and discussed separately below, although there will be some overlapping in discussing several of the alleged errors.

Error No. (1) Arbitrary addition of "day-to-day" control.

As set forth above, the Department of Labor guidelines provide only for de facto exercise of control and you urge that the additional criterion of de facto "day-to-day" control by GSA is a wholly arbitrary one.

In commenting on the five elements contained in the guidelines set out above, the Acting Solicitor, Alfred G. Albert, Department of Labor,

in a letter to us dated September 27, 1971, noted that those elements closely parallel those used by the National Labor Relations Board in deciding similar questions.

With particular reference to de facto control he stated that:

"When this Department established these criteria, it turned to existing law in the area. De facto control is a dominant factor in determining corporate liability, and it is defined as actual control rather than the potential control present where there is common ownership. In the field of labor law, the NLRB and the courts have required the existence of actual control by one business over another in order to consider the businesses a single employer for purposes of the Board's remedial orders. See Roy & Sons Co. v. NLRB , 251 F. 2d 771 (1st Cir. 1958); Bachman Machine Company v. NLRB, 266 F. 2d 599 (8th Cir. 1959); Majestic Molded Products, Inc. v. NLRB, 330 F. 2d 603 (2d Cir. 1964); NLRB v. Supreme Dyeing and Finishing Corp., 340 F. 2d 493 (1st Cir. 1965).

"In the area of the liability of a parent corporation for the torts of its subsidiaries, the courts also have held that mere common ownership is not sufficient to justify imposing liability on the parent. There must be common, actual control as well. Where this element is absent, courts have refused to hold the parent responsible for the torts of its subsidiary. As in the above-cited labor cases, common ownership would normally presuppose a potential ability to control, but the courts have held that actual control is required in order to impose liability on the parent corporation. See Baim & Blank, Inc. v. Philco Corp., 148 F. Supp. 541 (E.D. N.Y. 1957); Garret v. Southern R. Co., 173 F. Supp. 915 (E.D. Tenn. 1959), aff'd., 278 F. 2d 424 (6th Cir. 1960), cert. denied, 364 U.S. 833 (1960); Miller v. Bethlehem Steel Corp., 189 F. Supp. 916 (S.D. W.Va. 1960).

"The GSA memorandum prepared as a result of Apache Flooring Company's challenge to a bid award to Armstrong Cork Co. indicates that de facto control is to be interpreted as day-to-day control. That memorandum concludes that the compliance status under Executive Order 11246 of Thomasville Furniture Co., a wholly owned subsidiary of Armstrong Cork Co., should not affect Armstrong's status

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as a responsible bidder on government contracts covered by the Executive Order. Although this Department agrees with the conclusions of that memorandum, it has not taken the position that day-to-day control is required to consider the parent and subsidiary as a single entity for the purpose of coverage. Nash, Affirmative Action Under Executive Order 11246, 46 N.Y.U.L. Rev. 225, 250-51 (1971). From our review of the challenge, we found no evidence to reverse GSA's determination that there was no de facto, or actual, control, as defined in the above-cited cases, by Armstrong over the operations of Thomasville. Consequently, GSA's interpretation of de facto control as day-to-day control is not necessary to the ultimate decision that was reached."

You will note from the above that the Department of Labor in its review of GSA's findings found no evidence to reverse GSA's findings even though GSA had injected the term "day-to-day" into the criterion. Nor have you indicated why a different result would have been reached in this particular case if such term had not been added thereto. Consequently, while the addition of that term may have been in error, it is our view that, in this particular case, it was a harmless one and no change in the ultimate conclusion is thereby required.

Error No. (2) Capricious Interpretation of Criteria.

In his letter to you of February 26, 1971, referred to above, the Solicitor, after setting out the criteria for determining whether a parent and subsidiary corporation are to be considered as a single entity for the purposes of Executive Order 11246, stated that:

"* * * This has been the legal position of the Office of Federal Contract Compliance under Executive Order 11246 which I have reconfirmed with the Director of that Office. If, for good and sufficient business reasons, a parent corporation chooses not to exercise actual control over its subsidiary, the subsidiary will not be considered to be part of the parent corporation for purposes of Executive Order 11246. If the business is organized this way to escape its equal employment opportunity obligations, it would be another matter. However, there is no indication that this is the case

with the Armstrong Cork Company and Thomasville Furniture Industries, Inc."

Relative to this matter you state in part that:

"What sense does it make to prove conclusively the presence of all the criteria or guidelines if, in spite of this proof, a subsidiary will not be considered to be part of the parent corporation for purposes of Executive Order 11246, if, for so-called 'good and sufficient business reasons', a parent corporation is permitted to choose not to exercise control over its subsidiary?

"Such a wanton departure from the established guidelines, however motivated, being an obvious contradictio in adjecto, can only be deemed 'capricious'."

Where a parent corporation has potential control over a subsidiary the question as to whether or not it will actually exercise that control, must, of course, be a matter of choice on its part. Consequently, we do not agree that the Solicitor's statement concerning choice by the parent corporation constitutes a departure from the established guidelines. Also, we believe it significant that the Solicitor added that the choice not to exercise control must be for good and sufficient business reasons and that it would be a different matter if the business is organized this way to escape its equal employment opportunity obligations. According to GSA, Thomasville, after its acquisition by Armstrong, remained separate and distinct in its functions and operations, and its personnel and labor relations programs are the same as they were prior to such acquisition. Further, there is no evidence of record that there was here involved any action taken by Armstrong based upon a "choice" of any kind to evade its EEO obligations.

Error No. (3) Disregard of Mohasco Precedent.

The Mohasco case is said in your letter to be analogous to the Armstrong case. However, in that case you state that the Government insisted on proof of corporate-wide EEO compliance prior to award of the contract involved. The facts there involved are described in your letter as follows:

"* * * Mohasco, the parent corporation, a long-time holder of Federal Supply Contracts for carpets,

saw no reason to extend its EEO liability to its wholly-owned subsidiaries, mostly furniture plants, e.g. Futorian, Barcalo, Chromcraft, which had no connection with the carpet supply contract, Mohasco contending that its subsidiaries were separate corporate entities and were autonomously managed. Notwithstanding the President's Committee on Equal Employment Opportunity issued on July 30, 1965 Order No. (C-13) to all Government Departments, proscribing Mohasco from further contracts pending the submission of a 'corporate-wide program of affirmative action.'"

In view of the foregoing, you state that:

"It would appear to be incompatible with the ruling of the President's Committee on Equal Employment Opportunity, whose functions were subsequently transferred to the Labor Department, to bar Mohasco Industries from receiving Government contracts for failure of its subsidiaries' EEO compliance and then to permit another, perhaps more powerful corporation, to exercise arbitrary control or waive control at its own choosing over a wholly-owned subsidiary under identical circumstances and thus qualify for a Government contract, without EEO compliance by the subsidiary."

At our request the Department of Labor furnished to us copies of certain material contained in the Mohasco files. While the facts in that case may be as stated by you, the material furnished does not disclose whether the question of de facto control was raised or considered. Also, it should be noted that the President's Committee on Equal Employment Opportunity was established under an earlier Executive Order, 10925, and its program administered under regulations pertinent thereto, which--according to the Department of Labor--differ in many respects to the requirements of Executive Order 11246, as amended.

In view of the foregoing we are unable to determine that the Mohasco case is completely analogous to the Armstrong case or that the Department of Labor acted arbitrarily or capriciously in not reaching a conclusion consistent with the holding in the Mohasco case. In any event in view of section 201 of Executive Order 11246 the Secretary of Labor would be authorized to issue rules, regulations, guidelines and orders that may result in rulings contrary to those reached in prior cases.

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As to the court case (Williams v. New Orleans Steamship Assoc., 341 F. Supp. 613 (1972)), cited for the first time in the "Summation" forwarded with your letter of July 16, 1972, while the court in that case held that individual companies "may" be treated as a single employer for purposes of coverage of Title VII of the Civil Rights Act of 1964, where certain facts exist, the court did not hold that such companies "must" be treated as a single employer in all cases. Further the facts that were present in that case are set forth therein as follows:

> "[3] Plaintiffs have pointed out, and it has not been refuted by the defendants, that the New Orleans Steamship Association controls employment on the waterfront and establishes uniform employment policies and practices applicable to all member companies. It owns and operates a central hiring hall at which all longshoremen are hired on a day-to-day basis to work for the various member companies. The New Orleans Steamship Association derives its broad authority by delegation from the member companies. In view of this, the Court finds itself in agreement with the plaintiffs that for purposes of Title VII coverage the individual companies which make up the New Orleans Steamship Association would be treated as a single employer. * * *" (Emphasis added.)

As pointed out elsewhere herein GSA found that Thomasville remained separate and distinct in its functions and operations and that its personnel and labor relations programs remained the same as they were prior to acquisition by Armstrong. Thus, the factual situation as far as Thomasville's employment policies and practices were concerned is clearly distinguishable from that existing in the above-cited Williams case. We might also point out that the Williams case discloses that some of the criteria the Equal Employment Opportunity Commission (EEOC) has applied in determining whether an enterprise is integrated for purposes of calculating the number of its employees are "interchange of employees, centralized control of labor relations and standards which have been used by the NLRB" (National Labor Relations Board). As indicated above, it appears that the Department of Labor gave consideration to decisions of the NLRB and the courts in adopting its guidelines for determining whether a parent corporation and a subsidiary are to be considered a single entity for purposes of Executive Order 11246 and 41 CFR 60-1.40(a).

Error No. (4) Failure to Recognize Substantial Evidence.

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The material appearing under this heading in your letter relates to the question whether de facto exercise of control is practiced by Armstrong over Thomasville.

In urging that Armstrong does exercise de facto control over Thomasville you point out that six top Executive Officers of Armstrong control the "business and affairs" of Thomasville.

It is our understanding that at least after Armstrong acquired ownership of Thomasville—Thomasville had its own board of directors consisting of 10 members. Six of the ten were either directors or officers of Armstrong or both. However, one of the six was (and apparently still is) President of Thomasville and did not become an officer and director of Armstrong until after Armstrong had acquired ownership of Thomasville. Thus, four members of Thomasville's board of directors (after its acquisition by Armstrong) were neither directors nor officers of Armstrong. It should be noted here that Armstrong's board of directors consisted of 15 members including the six mentioned above.

To the extent that the six directors of Thomasville mentioned above (or any of the other directors) agreed with Armstrong policy they, of course, could have imposed such policy on Thomasville. Also, since Thomasville is a wholly owned subsidiary of Armstrong it is clear that Armstrong could completely dominate Thomasville if it chose to do so. However, as stated in letter of April 6, 1970, from the Solicitor, Department of Labor, to the Director of Equal Employment (your Exhibit "CC"), the cases of United States v. Lehigh Valley R.R., 220 U.S. 257 (1911) and Ford Motor Co. v. United States, 9 F. Supp. 590, cert. denied, 296 U.S. 636 (1935), both appear to indicate that common ownership or an interlocking directorate alone would not constitute sufficient grounds for disregarding corporate entities.

As corollary evidence you point out that:

"1) The parent corporation, Armstrong Cork Company, wholly owns Thomasville Furniture Industries, Inc.;

"2) Armstrong and Thomasville file quarterly and annual Statements of Consolidated Earnings and Consolidated Balance Sheets;

"3) The Senior Vice-President of Armstrong is President of Thomasville;

"4) The common Secretary of Armstrong and Thomasville released to the trade a Resolution of Nov. 25, 1968 by Armstrong's Board of Directors and announced Armstrong's readiness, willingness and ability to extend to any lender and supplier of Thomasville, upon request, a guaranty authorized by this resolution.

"The payments under a Government Contract to Armstrong will thus inure - see Resolution of Nov. 25, 1968 under 4 above - to the benefit of Thomasville.

* * * * *

"5) Armstrong and Thomasville commingle their operations, as evident from Armstrong's perennial nation-wide advertising in leading home and trade journals under the motto: 'ARMSTRONG - CREATORS OF THE INDOOR WORLD.'"

As to this last point, while it may be that such advertising has established the image of a single corporate entity in the eyes of the public, such advertising cannot make Armstrong a single corporate entity if it is not in fact such an entity.

All of these facts and more were recognized and treated by GSA in their opinion of January 28, 1971. GSA stated in its opinion that--

"* * * Its [Thomasville's] manufacturing operations have been continued in the basic pattern, in the same basic locations, and with the same end product as it had manufactured and sold prior to its acquisition. * * *"

Also, while recognizing that some advertising by Armstrong included Thomasville's products, GSA found that Thomasville has remained functionally independent of Armstrong, neither manufacturing, selling, nor distributing Armstrong's other products. Further, GSA noted in the opinion that Thomasville's personnel director remained the same and that it maintained its own independent personnel policies notwithstanding the Affirmative Program issued by Armstrong.

GSA then concluded that:

"Under these conditions and these facts, it seems clear that while Armstrong has potential control over the day

> to day operations of Thomasville, it does not actually or actively exercise such control. For these reasons then, it is clear that the authority exercised by Armstrong is limited to certain financial matters inherent in common ownerships, and amounts to potential control, not the de facto control of the actual day to day direction and control of Thomasville. It seems clear that each corporation acts in its day to day operations as an autonomous separate corporate entity. Each operates in widely separated geographic areas in functionally distinct manufacturing processes producing functionally distinct independent end products."

GSA's conclusion that Armstrong did not exercise de facto control over Thomasville was concurred in by the Department of Labor.

Considering the evidence of record, there would not be a sufficient legal basis for us to conclude that GSA's finding as to de facto control, as concurred in by the Department of Labor, is either arbitrary or capricious.

Error No. (5) Incompatibility with Federal Procurement Regulations.

The material set out under this heading of your May 30 letter relates to the fact that the Department of Labor in administering Executive Order 11246 has borrowed its guidelines for determining the corporate relationship of affiliates or subsidiaries from rulings of the National Labor Relations Board, which primarily exercises jurisdiction over labor disputes.

It is your view that since Executive Order 11246 imposes on a Federal contractor certain obligations embodied in his Federal contract it would be more appropriate to adopt the provisions of Federal Procurement Regulations, 41 CFR 1-1.701-2 which, for the purpose of making certain determinations under the Small Business Act defines "affiliates" as follows:

> "Business concerns are affiliates of each other when either directly or indirectly (a) one concern * * * controls or has the power to control the other, or (b) a third party or parties * * * controls or has the power to control both."

While we might agree that for the purpose of uniformity or otherwise the Secretary of Labor could have adopted the above definition of the term "affiliate" for the purposes of Executive Order 11246, or, as referred to in your Summation, the definition of the term "Control" as that term is defined

in the General Rules and Regulations of the Securities and Exchange Commission, 17 CFR 230.405(f), he was not required to do so under the controlling Executive Order. We might note here that the rulings of the National Labor Relations Board involve generally employer-employee relations as do rulings under the equal opportunity program in many cases.

Error No. (6) Unequal Treatment of Bidders.

Under this heading it is stated in your May 30, 1971, letter that:

> "If the interpretations by GSA and the Labor Department should prevail, it would pose a distinct hardship for corporations which are organized on a divisional basis, as there is no doubt that a division of a parent concern is eo ipso considered to be part and parcel of the parent corporation. Thus, corporations like General Electric Company, Container Corporation of America and Apache Flooring Company will be bidding at a distinct disadvantage when competing with a parent corporation which chooses to organize by dividing its corporate structure into wholly-owned subsidiaries. Under GSA's theory, the Government must then prove 'day-to-day' control. Under the Labor Solicitor's theory, expressed in his latest letter of February 26, 1971, the parent corporation is free to choose not to exercise control over the wholly-owned subsidiary, thus permitting the subsidiary to escape the costly and time-consuming obligation of developing affirmative action plans. Such unfair advantage should not be given one bidder over another under our competitive bidding systems."

While it may be true that where parent and subsidiary corporations are treated as separate entities they may have a bidding advantage over other bidders, the manner in which corporations are organized, if otherwise authorized, is of course, a matter solely for consideration by the corporations themselves. The fact they may be less competitive or more competitive because of their internal organization is a matter within their own control. Also, as previously noted, the Solicitor in his letter to you of February 26, 1971, stated, in effect, that the business may not be organized in a way purposely designed to escape its equal employment opportunity obligations.

Error No. (7). Negation of the "Good Faith Effort" Mandate.

Concerning this heading you state that:

"Affirmative Action Plans, properly demonstrated, pre-suppose a 'good faith effort'. Judicial determinations of 'good faith' have been rendered for many years. A parent corporation having pledged itself by the terms of its contract to put forth 'every good faith effort' to comply with Executive Order 11246 cannot honestly condone discriminatory employment practices of a wholly-owned subsidiary within its complete domain when it has the power to eliminate such practices.

"Therefore, it follows that any pledge by a Federal contractor, if made 'in good faith', should extend to any wholly-owned subsidiary within his complete domain."

While we agree that Armstrong, no doubt, could require an affirmative action program of Thomasville, we believe that, insofar as this particular contract is concerned Armstrong is pledged only to apply "every good faith effort" with respect to the parent corporation and to all subsidiaries which under the criteria discussed herein cannot be considered as separate entities.

In your letter of December 16, 1971, you refer to an article written by the Solicitor, Department of Labor, which is contained in the April 1971 issue of the New York University Law Review. You quote a paragraph from that article as follows:

"'B. ALL FACILITIES OF COVERED CONTRACTORS OR SUBCONTRACTORS ARE SUBJECT TO THE EXECUTIVE ORDER'

"'Section 204 of Executive Order 11,246 makes clear that all facilities of contractors or subcontractors are subject to the requirements of the equal opportunity clause, whether or not they are directly or indirectly engaged in the performance of government contract work. Upon application, a contractor or subcontractor may secure an exemption for facilities "which are in all respects separate and distinct from activities of the contractor related to the performance of the contract." However, since an exemption may be granted only upon a determination that it will not interfere with or impede the effectuation of the order, it is not surprising that almost none have been granted since the order was issued in 1965.'" "See Exhibit 'II' as attached."

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Relative to such matter you state that--

"It is significant to observe in this connection that, to the best of our knowledge, Armstrong has neither applied for nor has been granted an exemption for any of its facilities.

"What has been overlooked by the Labor Department, the legal successor to the President's Committee on Equal Employment Opportunity, the custodian of its files and executor of its former orders, consistent with Executive Order 11246 - see Sec. 403(a) and (b) of this Order - and what your office has failed to cite in its March 15, 1971, decision is the specific provision of Sec. 204 of Executive Order 11246:

"* * * 'in the absence of such an exemption all facilities shall be covered by the provisions of this Order.'"

We think it evident that the facilities referred to above are those facilities which under the guidelines discussed herein would be subject to the Executive Order. In other words if, in the instant case, Armstrong exercised de facto control over its subsidiary Thomasville, Thomasville would be subject to the provisions of the Executive Order and could only be exempted from its provisions by an exemption granted under section 204.

The remaining items discussed in your letter of December 16, 1971, and in your Summation, are, as indicated above, similar to those presented in your letter of May 30, 1971, and, we feel, have been adequately covered in our above discussion of that letter.

In summary, it is our view that the criteria followed in this case to determine whether a parent and its subsidiary should be treated as separate entities closely parallel those used by the National Labor Relations Board in deciding similar questions and we cannot say that their use here was unreasonable, arbitrary, or capricious. Also, we agree with the views of the Solicitor, Department of Labor, that the question whether Armstrong and Thomasville qualified under that criteria to be considered as separate entities was a close one. However, we remain of the view that based on the record we cannot say that the result obtained here was either arbitrary or capricious.

We believe it important in this case, to keep in mind that, as stated in connection with alleged error No. 2 and pertinent to other alleged

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errors where "choice" as to exercise of de facto control is mentioned, the subsidiary continued to be separate and distinct in its operation, and its personnel and labor relations program remained unchanged upon acquisition by Armstrong.

Accordingly, we see no proper basis to now reach a conclusion different from that reached in our earlier decision.

Very truly yours,

(SIGNED) ELMER B. STAATS

Comptroller General
of the United States