Gordon Arata
MONTGOMERY BARNETT

Take Heed to Avoid Being Cast a Single Business Enterprise

AUGUST 27, 2018

The Louisiana Third Circuit's recent decision in *Duhon v. Petro "E," LLC,* 2018-57 (La.App. 3 Cir. 7/11/18), stands as a reminder to companies of the exposure to liability they may face under the single business enterprise (**SBE**) theory. Reversing a summary judgment dismissal, the court ruled that the plaintiff, an aggrieved landowner, presented facts sufficient enough to support her position that two energy companies were engaged in a single business enterprise, such that one should be held liable for the obligations of the other.

Simply stated, the SBE theory allows for one company to be held liable for the obligations of another company under certain conditions – generally when the two companies are being operated as one. This form of veil piercing goes both horizontally and vertically, in other words between sister companies and also between a subsidiary and its parent. However, the SBE theory allows for veil piercing solely among companies, not among individuals.

Louisiana courts analyzing an SBE allegation have applied an 18-factor test, originally set forth by the Louisiana First Circuit in *Green v. Champion Ins. Co.,* 577 So.2d 249 (La. Ct. App.), *writ denied*, 580 So.2d 668 (La.1991):

1. corporations with identity or substantial identity of ownership, that is, ownership of sufficient stock to give actual working control;
2. common directors or officers;
3. unified administrative control of corporations whose business functions are similar or supplementary;
4. directors and officers of one corporation act independently in the interest of that corporation;
5. corporation financing another corporation;
6. inadequate capitalization ("thin incorporation");
7. corporation causing the incorporation of another affiliated corporation;
8. corporation paying the salaries and other expenses or losses of another corporation;
9. receiving no business other than that given to it by its affiliated corporations;
10. corporation using the property of another corporation as its own;

11. noncompliance with corporate formalities;
12. common employees;
13. services rendered by the employees of one corporation on behalf of another corporation;
14. common offices;
15. centralized accounting;
16. undocumented transfers of funds between corporations;
17. unclear allocation of profits and losses between corporations; and
18. excessive fragmentation of a single enterprise into separate corporations.

This list of factors is not exhaustive, nor is any one factor dispositive in determining whether a single business enterprise exists. Instead, courts look at the totality of facts to see if the companies are being operated as separate entities. If a court finds that multiple entities constitute a single business enterprise, the court may disregard the concept of separateness and extend liability to each affiliated entity.

In reversing the district court's summary judgment dismissal, the Third Circuit in *Duhon* noted several factors suggestive of a single business enterprise:

1. the companies had common ownership and permitted the transfer of funds between themselves without any documentation, interest charges, or efforts made to collect unpaid loans;
2. the loans between the companies were not "arms-length" transactions;
3. the companies shared office space without one company paying rent to the other;
4. the companies shared the same phone and fax numbers;
5. the work performed by one company for the other was governed by a one-page agreement, which was different from all other contracts with other companies;
6. the companies participated together in acquiring the lease at issue; and
7. the contracted company never attempted to collect amounts due under the contract from the other company.

As noted previously, not all 18 factors need be met for a court to find a single business enterprise exists. Instead a court will perform a fact intensive analysis, guided by the factors set forth in *Green*, to determine whether two separate legal entities are in fact operating as one, or close enough, such that each separate company should be held liable for the actions of the other.

It is important for energy companies to take note of the single business enterprise theory, as it is fairly common in today's oil and gas industry to see related entities owned or operated by the same person(s) or entity. For example, the same person(s) or entity may own and control both Leasing, LLC and Operating, LLC. The owner may utilize Leasing, LLC to acquire oil and gas leases or other mineral rights and then use Operating, LLC to develop the minerals.

To mitigate liability for each company, it is imperative for each to have structures and systems in place that are independent from the other. Further, the related entities should separate their accounting and contract with one another as they would with any other, unrelated entity. Not doing so could expose, for example, Leasing, LLC to liability for damages caused by Operating, LLC.

Therefore, companies operating in this manner should always seek the advice of counsel regarding their exposure to liability under the single business enterprise theory.