

**ABRAHAM**  
v.  
**LAKE FOREST, INC. and N.E.I. CORPORATION**  
(La. App. 1979)

After taking a judgment against NEI Corporation, Alabama (hereinafter referred to as "Alabama") plaintiff brought this suit against Lake Forest, Inc., the owner of all of the stock in Alabama and NEI Corporation, the owner of all of the stock in Lake Forest, attempting to pierce Alabama's corporate veil and to make the other corporations liable for Alabama's debt. Plaintiff has appealed from a dismissal of the suit and raises the issue that the facts and circumstances support the imposition of liability on Lake Forest and NEI as a matter of law.

On March 14, 1973, plaintiff purchased for \$21,524 an option to purchase some 119 acres on Cody Road near Mobile, Alabama, for \$389,382.50. Shortly thereafter plaintiff began to negotiate with a representative of Lake Forest to sell the option. These negotiations culminated with a sale and assignment of the option by Abraham to Lake Forest's newly formed subsidiary Alabama for \$375,500. On the same date Abraham and Alabama jointly exercised the option to purchase the property and Alabama subsequently took title to the property for \$389,382.50.

The price Alabama paid for the option consisted of \$172,117.50 in cash paid to Abraham and his partner, and Alabama's note for \$203,382.50. Between March 14, 1974, and January 10, 1975, payments amounting to \$50,845.64 on the principal were made, leaving a balance of \$152,536.86, the amount of the judgment taken by Abraham against Alabama and the amount sued on in this case, plus accrued interest.

In connection with Alabama's purchase of the property it borrowed \$550,000 from the First National Bank of Mobile, secured by a mortgage on the property. Its plans to develop the property into 385 residential sites and 14 acres of commercial property did not materialize and Alabama sold the property on November 4, 1975, for \$490,000. After deduction of the mortgage balance and the closing costs Alabama received \$33,185.36. It is Alabama's disposition of this sum which creates one of the principal issues raised by plaintiff and which will be discussed in detail hereafter.

NEI Corporation, one of the defendants in this case, is a large public corporation engaged in the real estate development and management business throughout the United States. It operates through numerous wholly owned subsidiaries, some of whose stock such as Lake Forest it directly owns while the stock of others, such as Alabama, is owned by other subsidiaries, such as Lake Forest in this case. Alabama was incorporated for the immediate purpose of acquiring the property on which Abraham had the option and for the long range

purpose of developing that property residentially and commercially. It was incorporated with the minimum of \$1,000 paid in capital and never generated any revenues of its own. All of the funds in excess of those realized by Alabama when it sold the property in November, 1975, were advanced by Lake Forest. This amounted to about \$290,000 including the \$172,117.50 originally paid by Alabama to Abraham and his partner, the \$50,845.64 paid on the principal of the note held by Abraham, and interest payments amounting to \$22,783.61. Although Alabama had its own bank account these transactions were handled by Lake Forest, but complete accounting records were kept to reflect that they were loans being made by Lake Forest to Alabama. Any operating expenses incurred by Alabama were likewise paid by Lake Forest with appropriate accounting entries made to show these as loans to Alabama. When Alabama sold the property the net proceeds of \$33,185.36 were represented by a check payable to the order of Alabama, and although the check was endorsed by Alabama it was deposited in the Ohio bank account of NEI Corporation. Accounting entries were made in the books of Alabama showing its receipt of the funds, its payment of the funds to Lake Forest, and reduction of Alabama's debt to Lake Forest. Lake Forest's books reflected its receipt of the funds on account of Alabama's indebtedness and its payment on account of its indebtedness to NEI Corporation.

In the management of the corporate affairs of NEI, Lake Forest and Alabama, separate boards of directors and slates of officers were elected and separate minutes of meetings of the boards were maintained, although the same individuals for the most part sat on the boards and held office in each of the corporations.

Plaintiff argues primarily that he is entitled to the judgment against Lake Forest and NEI because Alabama is the alter ego and a mere business conduit of the other corporations. \*\*\*

Plaintiff's primary argument rests on legal principles recently considered by this court in *Dillman v. Nobles*, 351 So.2d 210 (La. App. 4th Cir.1977) where the following analysis was given: As a general rule a corporation is a distinct legal entity whose shareholders are not individually liable for its debts. However, this rule admits of the "alter ego" exception which, in turn, is supported either by a fraud or deceit practiced on a creditor by the shareholder acting through the corporation or *even in the absence of* fraud when the business of the corporation has been conducted under such circumstances where corporate formalities have been disregarded to the extent that the corporation ceases to be distinguishable from the shareholders. Some of the factors to be considered are the commingling of corporate and shareholder funds, the failure to observe statutory formalities in connection with the transaction of corporate affairs, under-capitalization, failure to provide separate bank accounts and bookkeeping records, failure to hold regular shareholder and directors' meetings and ownership of all shares by a single shareholder. In this case the court concluded that the alter ego doctrine applied,

and the shareholder was individually liable. The same result was reached by the courts in *Smith-Hearron v. Frazier, Inc.*, 352 So.2d 263 (La.App. 2nd Cir.1977) and *Ogaard v. Wiley*, 325 So.2d 642 (La.App. 3rd Cir.1975).

However, although the court recognized these same principles in *Kingsman Enterprises v. Bakerfield Elec. Co.*, 339 So.2d 1280 (La.App. 1st Cir.1976) it reached the opposite result emphasizing that the separation of the corporate entity from its shareholders is the firmly established general rule and should be disregarded only in exceptional circumstances. The court went on to say:

“Appellant elicits partial facts from other cases as authority for finding that the corporations were the alter egos of Womack. However, this approach is inadequate because it fails to consider the totality of circumstances as is necessary in such cases.”

The court repeatedly emphasized that the “totality of facts” in the case did not support the alter ego theory even though the plaintiff did establish a number of important factors tending to support the theory.

We have concluded that plaintiff in the instant case is in much the same position.

On plaintiff’s side of the case, he established that all of Alabama’s stock was owned by one shareholder, Lake Forest. In a sense it can be said that Alabama was under-capitalized in that it purchased property for \$790,000 while having only \$1,000 of capital stock. There was a commingling of funds in the sense that Alabama had practically no funds of its own, virtually all of the funds it used were put up by Lake Forest and/or NEI, and even the proceeds from the sale of the property were deposited in NEI’s account and were never put into Alabama’s bank account. Finally, almost all of the business of the corporation was accomplished by unanimous consent of the shareholders, which obviated the necessity of meetings of Alabama’s shareholders and board of directors.

On the other hand everything Alabama did was in compliance with corporation law. Individuals are specifically authorized to assume only limited liability by setting up a minimally capitalized corporation. Furthermore, the law specifically authorizes the establishment of a corporation by a sole stockholder and the use of unanimous consent agreements among shareholders and directors in lieu of meetings. Since all of the funds paid to Abraham and his partner originated from NEI no practical purpose would have been served for NEI to write a check to Lake Forest, for Lake Forest to write a check to Alabama, and for Alabama to write a check to plaintiff with intervening deposits into separate corporate accounts. It was sufficient under these circumstances for the matter to be covered with bookkeeping entries. Separate minute books were kept, resolutions were adopted, elections were

held, positions and offices were filled and all of the facets of a separate formal corporation were observed by Alabama.

In any event, even though plaintiff can isolate a number of factors which favor his position they lose their significance when considered as a part of the totality of facts in this case. Plaintiff was a sophisticated real estate entrepreneur who was quite familiar with the practice of undertaking separate real estate developments through separate minimally capitalized corporations. In fact, he admitted that he himself utilized this practice in his own business. Although his initial negotiations were with Lake Forest's representative he knew several months before the option was exercised by Alabama that it would purchase the option from him. On October 1, 1973, plaintiff wrote a file memorandum to the effect that the note would be given by "Ala. Subsidiary N.E.I." In the option jointly exercised on October 10 by plaintiff and Alabama, plaintiff advised the sellers that he had assigned all of his rights under the option to NEI Corporation, Alabama. Finally, he voluntarily accepted the note on November 28, 1973, from Alabama alone.

In none of the cases cited by plaintiff where the corporate veil was pierced on the alter ego theory was there even a voluntary creditor, let alone one who was as knowledgeable and free to enter into a transaction as was the plaintiff in this case. For instance in the *Dillman* case, plaintiff was a tort victim and the court refused to shield the individual tortfeasor behind a practically invisible and purely artificial corporation. In the *Smith-Hearron* case, the court constituted the activities of the shareholder as "machinations" and spoke of "fraud and chicanery" in connection with his dealings with the plaintiff. In the *Ogaard* case, the court dealt with a tort claim and again refused to shield shareholder of a corporation which hardly had any functions.

In the instant case the plaintiff made a business judgment which, at the time he accepted the note, seemed to be quite prudent. He had gotten appraisals on this property which indicated that it had a great potential and he was apparently convinced that Alabama could capitalize on the project. Needless to say, Alabama was equally optimistic because it and its parent corporations invested considerable sums in the purchase of the property. When plaintiff took the note he was obviously speculating on the success of the project itself and was not relying on the credit of the parent corporation. He was apparently satisfied to take the risk considering the fact that he stood to make a relatively quick profit on the option which he had purchased just six months previously. While we understand from the jurisprudence that it is not necessary to establish fraud in order to support the alter ego theory we are satisfied that the doctrine contains equitable features which require that the type of claim and the relative positions of the parties be considered before applying the doctrine. In the instant case, these considerations do not support the application of the theory.

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