

HEADNOTES

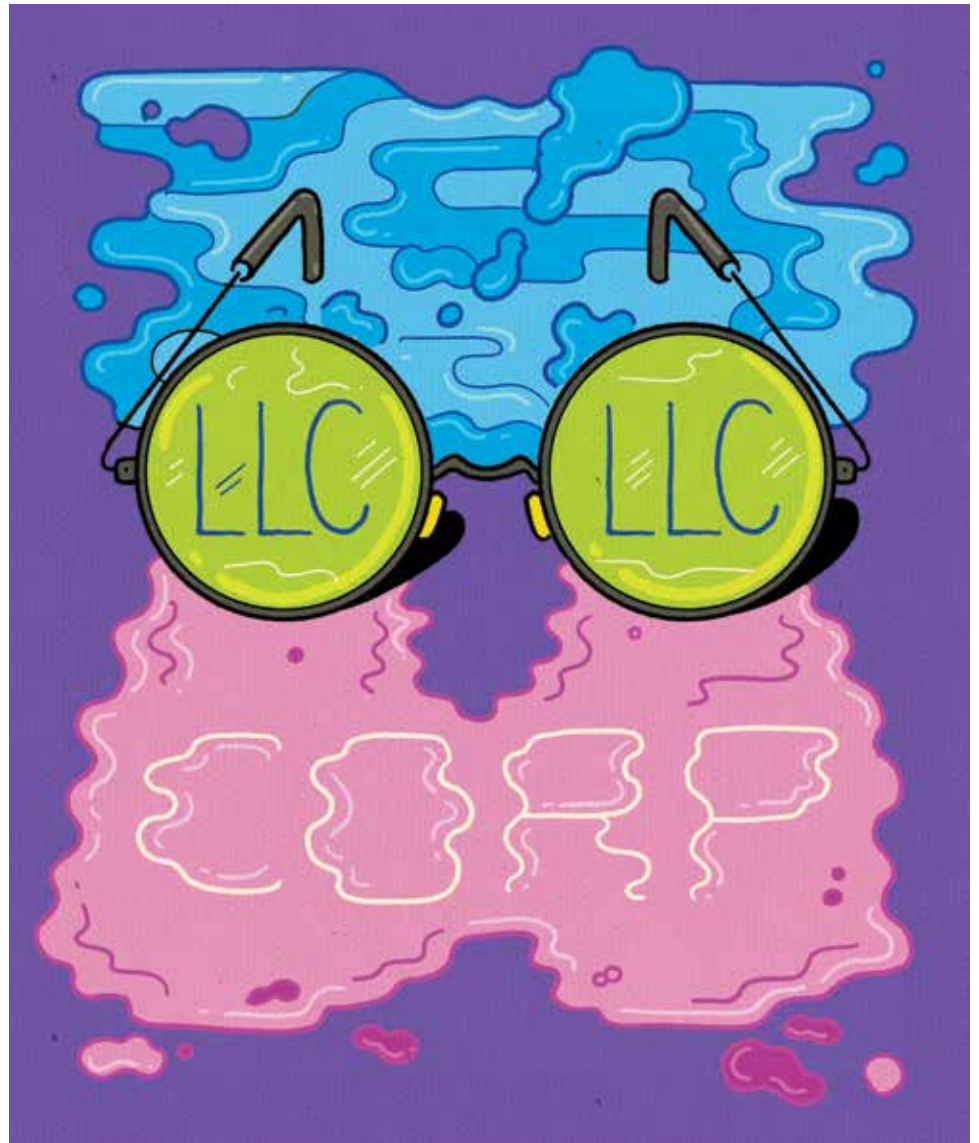
CORPORATE LAW

“Nowhere Man”: Treat LLCs Like Corporations to Ensure Diversity Jurisdiction Remains Viable

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In speaking for the U.S. Supreme Court, Justice Frankfurter explained that “[d]iversity jurisdiction is founded on assurance to nonresident litigants of courts free from susceptibility to potential



local bias.” *Guar. Tr. Co. v. York*, 326 U.S. 99, 111 (1945). As limited liability corporations (LLCs) have surpassed corporations as the predominant business entity in the United States, federal courts have declined to treat them the same for diversity purposes, depriving litigants of access to federal courts and burdening them with onerous requirements before they can file a complaint or seek removal. To ensure that diversity jurisdiction remains a viable way to access federal courts, LLCs and corporations should be treated the same for diversity purposes.

Under 28 U.S.C. § 1322(c), a corporation is “deemed” to be a citizen of the state in which it is incorporated and the state

in which it has its principal place of business. Unlike a corporation’s citizenship, however, the citizenship of an LLC is determined by the citizenship of each of its members. *See, e.g., Wise v. Wachovia Sec., LLC*, 450 F.3d 265, 267 (7th Cir. 2006); *Harvey v. Grey Wolf Drilling Co.*, 542 F.3d 1077, 1080 (5th Cir. 2008).

Accordingly, pleading requirements differ for suits that involve corporations and those that involve LLCs. While complaints invoking diversity jurisdiction where the defendant is a corporation must allege only the company’s state of incorporation and principal place of business, plaintiffs who wish to sue LLCs must allege the citizenship of the natural persons

who are members of the LLC.

Determining the ultimate membership of an LLC, and the citizenship of those members, is often burdensome if not impossible. Most states do not require that LLCs report their members, nor is an LLC's membership otherwise made public. This information is frequently only obtainable from the LLC itself, which has little incentive to voluntarily provide it. For that reason, even if there is complete diversity among an LLC's membership and prospective plaintiffs, they may be foreclosed from even commencing an action in federal court. *See, e.g., Sienna Ventures, LLC v. Halley Equip. Leasing, LLC*, No. 18-cv-201 (E.D.N.Y. Apr. 2, 2018) (dismissing complaint for failing to properly invoke jurisdiction). The same is true for defendants who are sued by LLCs that seek to remove the case to federal court.

Further complicating matters is that an LLC's members may themselves be LLCs, and therefore a citizen of all of their natural members. In turn, those LLCs' members may also be LLCs. Given the complexity of modern business entities, this can create a problem of infinite regress. If any member at any part of an LLC's chain of ownership is not diverse from the plaintiff or plaintiffs, there is not complete diversity and, therefore, diversity jurisdiction is unavailable.

Such treatment favors form over substance. Today many large and complex business entities are organized as LLCs rather than corporations. For example, in 2017, Google converted from a corporation to an LLC. (*See* Natasha Lomas, *Google parent Alphabet forms holding company XXVI, to complete 2015 corporate reorganization*, TECHCRUNCH+, Sept. 4, 2017.) There are also significantly more LLCs than corporations today. According to the Internal Revenue Service's Integrated Business Data from its Statistics of Income program, there were 50 percent more LLCs than corporations that filed federal tax returns in 2015, the most recent year for which data are available.

Although corporations and LLCs are taxed differently, they are functional equivalents for purposes of diversity. Both corporations and LLCs can have numerous owners, and it is equally encumbering to determine their citizenship, regardless of whether the owners are called "shareholders" or "members."

Treating LLCs as citizens of their membership serves no purpose except to keep litigants out of federal court. The founders were concerned that out-of-state litigants would not receive a fair shake in state court. *See Guaranty Trust Co.*, 326 U.S. at 111. But if the parties are unable to determine whether there are any same-state parties among an LLC's members, it

is unclear how such a purpose could be served. The citizenship standard afforded to corporations that considers the entity's state of incorporation (or, for LLCs, state of organization) and principal place of business better achieves this goal. *See Wood v. Davis*, 18 How. 467, 469 (1856) ("It has been repeatedly decided by this court, that formal parties, or nominal parties, or parties without interest, united with the real parties to the litigation, cannot oust the federal courts of jurisdiction. . . .").

Moreover, the current standard can waste resources as cases may be litigated for years only to be dismissed upon the discovery of a non-diverse LLC member. *See, e.g., Belleville Catering Co. v. Champaign Marketplace, LLC*, 350 F.3d 691, 692 (7th Cir. 2003); *Thermoset v. Bldg. Materials of Am.*, No. 15-13942 (11th Cir. Mar. 2, 2017). And if a case is thrown out of federal court for lack of complete diversity, the statute of limitations may not be tolled, which could deprive plaintiffs of any relief by the time the claims reach state court. *See Ovidia v. Bloom*, 756 So. 2d 137, 139 (Fla. Dist. Ct. App. 2000).

Treating LLCs in the same manner as corporations avoids all of these problems and ensures that diversity jurisdiction remains a viable path to accessing federal courts in the 21st century. ■