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BNA Insights

How to Determine the Citizenship of LLCs (Hint: Keep Digging!)

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Limited liability companies (“LLCs”) resemble corporations in several respects. For example, corporate shareholders and LLC members are shielded from personal liability for organizational debts. Corporations and LLCs also each receive pass-through tax status. Despite these functional similarities, federal courts treat LLCs and corporations differently for purposes of diversity jurisdiction. Unlike corporations, whose citizenship is determined by the familiar state of incorporation and principal place of business inquiries, LLCs hold the citizenship of their members. This distinction complicates the diversity jurisdiction analysis, and litigants neglect it at their peril.

Carden and Its Progeny

Under 28 U.S.C. § 1332(c)(1), a corporation is deemed a citizen of both the state of its incorporation

and the state of its principal place of business. However, in its seminal decision, *Carden v. Arkoma Associates*, the Supreme Court refused to extend the statute to unincorporated associations.¹ Reasoning that § 1332(c)(1)'s use of the word “corporation” precluded its application to unincorporated associations, the Court held that a limited partnership did not possess citizenship independent of its members.²

Although *Carden* spoke directly to the citizenship of limited partnerships, the U.S. courts of appeals have applied its rationale to other forms of unincorporated associations, including LLCs. The U.S. Court of Appeals for the Seventh Circuit was the first circuit court to hold that for purposes of diversity jurisdiction, an LLC shares the citizenship of its members.³ Writing for

the court, Judge Posner observed that the limited liability company “is like a limited partnership” and concluded that the principle of *Carden* applied with equal force to LLCs.⁴

Since then, all federal courts of appeals to have considered the question agree that an LLC does not have independent citizenship status and instead holds the citizenship of its members for purposes of diversity jurisdiction.⁵

But what if an LLC's members are, themselves, unincorporated associations (e.g., additional LLCs or limited partnerships), whose own members also may consist of unincorporated associations? Under these circumstances, the U.S. Court of Appeals for the Second Circuit

⁴ *Id.*

⁵ E.g., *Pramco, LLC ex rel. CFSC Consortium, LLC v. San Juan Bay Marina, Inc.*, 435 F.3d 51, 54–55 (1st Cir. 2006); *Handelsman v. Bedford Vill. Assocs. Ltd. P'ship*, 213 F.3d 48, 51–52 (2d Cir. 2000); *Zambelli Fireworks Mfg. Co., Inc. v. Wood*, 592 F.3d 412, 420 (3d Cir. 2010); *Gen. Tech. Applications, Inc. v. Exro Ltda*, 388 F.3d 114, 121 (4th Cir. 2004); *Harvey v. Grey Wolf Drilling Co.*, 542 F.3d 1077, 1080 (5th Cir. 2008); *Delay v. Rosenthal Collins Grp., LLC*, 585 F.3d 1003, 1005 (6th Cir. 2009); *GMAC Commercial Credit, LLC v. Dillard Dep't. Stores, Inc.*, 357 F.3d 827, 829 (8th Cir. 2004); *Johnson v. Columbia Props. Anchorage, LP*, 437 F.3d 894, 899 (9th Cir. 2006); *Rolling Greens MHP, LP v. Comcast SCH Holdings, LLC*, 374 F.3d 1020, 1022 (11th Cir. 2004).

¹ 494 U.S. 185, 189 (1990).

² *Id.* at 196–97.

³ *Cosgrove v. Bartolotta*, 150 F.3d 729, 731 (7th Cir. 1998).

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has held that the citizenship of an LLC party is determined by a complete upstream analysis of its organizational structure.⁶

Despite these functional similarities, federal courts treat LLCs and corporations differently for purposes of diversity jurisdiction.

Recent decisions in the Second Circuit and the U.S. District Court for the Southern District of New York illustrate this analysis. For instance, *Bayerische* featured a diversity action against Aladdin Capital Management LLC (“Aladdin”). 692 F.3d at 49. Aladdin’s sole member was Aladdin Capital Holdings LLC (“ACH”), whose membership consisted of one limited partnership, four U.S. citizens and five corporations. The Second Circuit determined that Aladdin possessed the citizenship of ACH, which possessed the citizenship of each of its 10 members, stating: “[D]efendant Aladdin is a citizen of the various states of the United States of which its member, ACH, is a citizen (through ACH’s various members).”⁷

Similarly, in *Quantlab Financial, LLC v. Tower Research Capital, LLC*, plaintiff Quantlab Financial, LLC (“QLF”) commenced a diversity action against a competitor LLC.⁸ QLF’s sole member also was an LLC holding company, Quantlab Holdings, LLC (“QLH”). Applying the same upstream analysis, the Southern District of New York stated that QLF’s citizenship “depends on the citizenship of its sole member, [QLH], and, in turn, on the citizenship of [QLH’s] members.” In determining the citizenship of QLH’s members, and thus the citizenship of QLF, the court evaluated the citizenship of 10 layers of QLF’s organizational hierarchy, ultimately finding that the parties lacked complete diversity.⁹

As demonstrated by decisions like *Bayerische* and *Quantlab*, a diversity-destroying person or entity may be far removed from the LLC party (and

the litigation itself). However, the indirectness or tenuousness of the relationship between the non-diverse person or entity and the LLC party is immaterial to the LLC citizenship inquiry.

Practical Considerations

The citizenship test for LLCs gives rise to a number of practical considerations for lawsuits involving these corporate forms. First, access to the federal forum may be greatly diminished, as an LLC’s members may hail from many, and in some cases all, states. Similarly, lawsuits between an LLC and its member(s) are inherently non-diverse because an LLC holds the citizenship of each member, including the member(s) bringing suit.

Second, determining an LLC’s citizenship can be labor-intensive where its membership structure is complex. The upstream analysis of an LLC’s organizational hierarchy may require a considerable investment of time and resources. Few individuals may be capable of providing all requisite membership information, organizational records may be outdated and public records may be of limited assistance because state laws generally do not compel disclosure of LLC members’ identities.¹⁰ This is especially true when defendants are undertaking an upstream analysis to determine whether to remove a case to federal court, a process where counsel may have only days left to file a notice of removal.¹¹

Nevertheless, the costs of determining the parties’ citizenship before an action is commenced in, or removed to, federal court far outweigh the potential consequences of later discovering that diversity is incomplete. Federal subject-matter jurisdiction can be challenged at any time, including on appeal, or addressed by the court *sua sponte*.¹²

Moreover, defects in subject-matter jurisdiction, particularly those involving LLCs, cannot always be cured. Although non-diverse, dispensable parties may be dropped from an action at any time, it is well settled that the parties’ citizenship for

purposes of diversity jurisdiction is determined at the time of filing.¹³

Therefore, an LLC party cannot manufacture diversity by altering the composition of its membership after an action is commenced. Accordingly, the suspicion or presence of a jurisdictional defect, if left unaddressed, risks the vacatur of any judgment ultimately obtained.¹⁴

Moreover, the failure of an attorney to adequately investigate and accurately present the parties’ citizenship may result in admonition from the court, sanctions, fee reduction or malpractice liability.¹⁵ Indeed, if a case is improperly removed to federal court, “[a]n order remanding the case may require payment of just costs and any actual expenses, including attorney fees, incurred as a result of the removal.”¹⁶

In sum, a party should avail itself of diversity jurisdiction only after making a diligent effort to obtain a complete picture of the parties’ citizenship. The failure to do so unnecessarily risks court sanction and may jeopardize the enforceability of judgments later obtained.

Conclusion

Corporations and LLCs, though functionally similar, receive differential treatment for purposes of diversity jurisdiction. Unlike corporations, whose citizenship is determined by their state of incorporation and principal place of business, LLCs hold the citizenship of their members. Thus, LLCs often are subject to a more-searching citizenship analysis. Spe-

¹³ See *Grupo Dataflux v. Atlas Global Grp., LP*, 541 U.S. 567, 572–73 (2004) (“[I]t is well settled that [Fed. R. Civ. P. 21] invests district courts with authority to allow a dispensable nondiverse party to be dropped at any time, even after judgment has been rendered.” (internal citation and quotation marks omitted)); 13 CHARLES ALAN WRIGHT & ARTHUR R. MILLER, FEDERAL PRACTICE AND PROCEDURE § 3522 (3d ed. 1998) (“In diversity of citizenship cases . . . jurisdiction is assessed as of the time the case is commenced, and thus cannot be ousted by post-filing changes of citizenship.”).

¹⁴ See, e.g., *Handelsman v. Bedford Vill. Assocs. Ltd. P’ship*, 213 F.3d 48, 55 (2d Cir. 2000) (vacating judgment and remanding to state trial court where complete diversity was lacking).

¹⁵ E.g., *Thomas v. Guardsmark, LLC*, 487 F.3d 531, 535 (7th Cir. 2007); *Belleville Catering Co. v. Champaign Mkt. Place, LLC*, 350 F.3d 691, 694 (7th Cir. 2003).

¹⁶ 28 U.S.C. § 1447(c).

⁶ E.g., *Bayerische Landesbank, N.Y. Branch v. Aladdin Capital Management, LLC*, 692 F.3d 42, 49 (2d Cir. 2012).

⁷ *Id.* at 51.

⁸ 715 F. Supp. 2d 542 (S.D.N.Y. 2010).

⁹ *Id.* at 546, 549.

¹⁰ E.g., *Lewis v. Allied Bronze, LLC*, No. 07 Civ. 1621(BMC), 2007 BL 212672, at *2 (E.D.N.Y. May 2, 2007).

¹¹ See 28 U.S.C. § 1446.

¹² Fed. R. Civ. P. 12(h)(3); e.g., *Transatl. Marine Claims Agency, Inc. v. Ace Shipping Corp.*, 109 F.3d 105, 108 (2d Cir. 1997).

cifically, where an LLC party's membership is comprised of unincorporated associations, the citizenship analysis may entail an evaluation of

multiple layers of the LLC party's organizational hierarchy. Although a pre-lawsuit citizenship evaluation may be resource-intensive, its costs

pale in comparison to the avoidable, and potentially severe, consequences of overlooking jurisdictional defects.