SHORING UP THE "DOCTRINAL WALL" OF *CHAPMAN V. BARNEY*: IN SUPPORT OF THE AGGREGATE APPROACH TO LIMITED LIABILITY COMPANY CITIZENSHIP FOR PURPOSES OF FEDERAL DIVERSITY JURISDICTION

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I. INTRODUCTION

Imagine yourself as counsel for plaintiff Renter, Inc., an Oregon corporation, which is involved in a sizable commercial rent dispute with defendant Landlord LLC, a Delaware limited liability company with its principal place of business in the state of Washington. All extra-judicial attempts to resolve the dispute have failed, so you prepare to litigate. Since the plaintiff and defendant appear to be diverse in state citizenship, and the amount in controversy exceeds $75,000, you decide to file your complaint in an Oregon federal district court, invoking federal diversity jurisdiction under 28 U.S.C. section 1332. The defendant answers the complaint, conceding federal subject matter jurisdiction, and brings a counterclaim against your client.

After much time and expense, you eventually try your case to a jury, which, unfortunately, finds for the defendant on its counterclaim. Your client, of course, is dissatisfied with this outcome, and you appeal the judgment to the Ninth Circuit Court of Appeals. On appeal, much to your shock and embarrassment, the appellate court refuses to reach the merits of your case, vacates the judgment below, and delivers a scathing opinion that rebukes both you and opposing counsel for needlessly wasting the courts' (and the clients') time and resources. The reason for this unseemly result? Since a limited liability company's citizenship is determined by the citizenships of each of its members, and not by its principal place of business or state of organization, and because a number of Landlord LLC's *members* were *Oregon* citizens, the defendant LLC was not diverse in state citi-

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zenship from the plaintiff *Oregon* corporation. The lower court, therefore, never had subject matter jurisdiction to hear the case.[1]

As the above scenario suggests, in actions predicated upon federal diversity jurisdiction, proper analysis and classification of a business organization's citizenship is crucial to the determination of whether relief may be available in a federal forum. But what is the citizenship of a particular business organization for purposes of diversity jurisdiction? Under current federal statute and historical jurisprudence, the answer is plain: A corporation is regarded as a citizen of both its state of incorporation and the state of its principal place of business,[2] while the citizenships of unincorporated business associations are determined by the state citizenships of each of their individual members.[3]

This distinction between corporations and all other unincorporated business associations finds its roots in the 1889 case of *Chapman v Barney*,[4] and serves as a "doctrinal wall"[5] that silently guards the entrance to our federal court system. This doctrine of incorporation status as determinative of a business organization's citizenship for purposes of federal diversity jurisdiction has endured for nearly one-and-a-quarter centuries, and still stands today. To preserve its structural integrity, this author believes that continued judicial reinforcement is in order.

The *Chapman* wall recently came under siege in the 1990 landmark case of *Carden v. Arkoma Associates*.[6] *Carden* involved a contract dispute between Arkoma Associates, a limited partnership formed under the laws of Arizona, and two individuals who were citizens of Louisiana. The limited partnership brought suit in a Louisiana

1. This hypothetical scenario is based on the recent case of *Belleville Catering Co. v. Champaign Market Place, L.L.C.*, 350 F.3d 691 (7th Cir. 2003). For additional commentary on the case, see Stephanie Francis Ward, *A Ruling Like a Ruler on the Hands—Appellate Judge Takes Attorneys to Task for Jurisdiction Error*, ABA JOURNAL E-REPORT, Dec. 12, 2003, *at* http://www.abanet.org/journal/ereport/dec12lawyer.html (last visited Feb. 18, 2004).

2. 28 U.S.C. § 1332(c)(1) (1996).

3. Chapman v. Barney, 129 U.S. 677, 682 (1889).

4. 129 U.S. 677.

5. *See* United Steelworkers of Am. v. R.H. Bouligny, Inc., 382 U.S. 145, 151 (1965) ("Petitioner urges that . . . we have heretofore breached the doctrinal wall of *Chapman* v. *Barney* and, that step having been taken, there is now no necessity for enlisting the assistance of Congress. But *Russell* does not furnish the precedent which petitioner seeks.") (citation omitted). *See also* Debra R. Cohen, *Citizenship of Limited Liability Companies for Diversity Jurisdiction*, 6 J. SMALL & EMERGING BUS. L. 435, 438 n.12 (2002) (citing other court opinions reaffirming the "doctrinal wall" of *Chapman*).

6. 494 U.S. 185 (1990).

federal district court, invoking diversity jurisdiction.[7] Defendant Carden moved to dismiss for lack of subject matter jurisdiction, and argued that complete diversity was absent because one of Arkoma's limited partners was a citizen of Louisiana.[8] The district court denied the motion,[9] found in favor of plaintiff Arkoma, and Carden appealed. The Fifth Circuit affirmed, and decided that, for purposes of diversity jurisdiction, Arkoma's citizenship was based only on the citizenships of its general partners, and not of its limited partners.[10] Carden appealed to the United States Supreme Court, and in a 5-4 decision, the Court reversed.[11] Writing for the majority, Justice Scalia refused to breach the "doctrinal wall" and reaffirmed the principle that, for purposes of diversity jurisdiction, the citizenship of an unincorporated association is to be determined by the citizenships of *all* its members.[12]

Since the decision in *Carden*, a surge in the popularity of various hybrid business organizations,[13] especially limited liability companies (LLCs), has brought further attacks on this venerable doctrine by courts and commentators alike.[14] As disputes involving LLCs have

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7. *Id.* at 186.

8. *Id.*

9. *Id.*

10. Arkoma Assocs. v. Carden, 874 F.2d 226, 228-29 (5th Cir. 1988), *rev'd*, 494 U.S. 185 (1990).

11. Carden v. Arkoma Assocs., 494 U.S. 185, 198 (1990).

12. *Id.* at 196.

13. The term "hybrid business organizations," as used in this Comment, refers to modern unincorporated associations, including the Limited Partnership (LP), Limited Liability Partnership (LLP), and Limited Liability Company (LLC).

14. Criticisms of the "aggregate" or "persons composing" characterization of unincorporated associations for diversity purposes are not new to the courts. *See, e.g.*, Int'l Union, United Auto., Aircraft & Agric. Implement Workers of Am. v. Piasecki Aircraft Corp., 241 F. Supp. 385, 389 (D. Del. 1965) ("There are persuasive arguments that unincorporated associations should be treated as citizens of the state where the principal place of business is located. But I am convinced that any such innovation in diversity standards can only result from legislative action."); R.H. Bouligny, Inc. v. United Steelworkers of Am., 336 F.2d 160, 165 n.4 (4th Cir. 1964), *aff'd*, 382 U.S. 145 (1965) ("We readily concede that vis-a-vis a corporation, it would be quite feasible to treat a modern labor union as a citizen for diversity purposes. But the question of policy is certainly not one for decision of an intermediate appellate court."). The American Law Institute also has drafted proposed legislation aimed at amending the current treatment of unincorporated associations for diversity purposes. *See generally* American Law Institute, Study of the Division of Jurisdiction Between State and Federal Courts, §§ 1301(b)(2), 1302(b) (1969). Commentators and legal scholars also have criticized the corporation-versus-unincorporated association distinction for diversity purposes. *See generally* 4 JAMES WM. MOORE ET AL., MOORE'S FEDERAL PRACTICE § 17.25 (3d ed. 1997); Cohen, *supra* note 5; Leigh A. Bacon, *"Freedom of" or "Freedom From"? The Enforceability of Contracts and the Integrity of the LLC*, 50 DUKE L.J. 1087, 1104-10 (2001); Warren H. Johnson,

increasingly reached the courts, judges have wrestled with the classification of these new beasts for diversity purposes, often questioning whether a LLC is more akin to a corporation, and thus entitled to entity citizenship, or more like a partnership, which requires an examination of member citizenship in the aggregate. Tellingly, all courts faced with the issue of LLC citizenship for federal diversity jurisdiction purposes have relied on the decision in *Carden* to support an aggregate approach to LLC citizenship.[15]

This Comment advocates steadfast adherence to the "doctrinal wall" of *Chapman v. Barney*. Part II briefly reviews the historical treatment of corporations and unincorporated associations for purposes of diversity jurisdiction. Part III identifies and analyzes the aggregate and entity functional factors of limited liability companies. Part IV seeks to rebut recent arguments that call for a wholesale entity approach to LLC citizenship in the diversity jurisdictional analysis. The Comment concludes that arguments in favor of extending corporate citizenship to LLCs are unpersuasive, and courts and Congress should continue to analyze LLC citizenship in the aggregate.

Limited Liability Companies (LLC): Is the LLC Liability Shield Holding Up Under Judicial Scrutiny?, 35 NEW ENG. L. REV. 177 (2000); Robert J. Tribeck, *Cracking the Doctrinal Wall of* Chapman v. Barney*: A New Diversity Test for Limited Partnerships and Limited Liability Companies*, 5 WIDENER J. PUB. L. 89 (1995).

15. *See infra* note **Error! Bookmark not defined.** (listing cases involving citizenship of LLCs for diversity jurisdiction purposes).