When Is The Citizenship Of An LLC Member Relevant For Diversity Purposes: The Spectator On The Sideline Test Applied

By: Jerome W. Cook

On April 4, 2017, a federal district court within our Sixth Circuit had occasion to consider whether the citizenship of a limited liability company defeated diversity jurisdiction. *Kelly v. American Foods Group et al*., 2017 WL 1281153. In holding that the citizenship of the limited liability company was relevant to the diversity jurisdiction issue, the district court in *Kelly* had occasion to revisit the concept of "nominal party," the "Spectator on the Sideline Test," the holding in *Mortenson Family Dental Center, Inc. v. Heartland Dental Care, Inc.*, 526 Fed. Appx. 506 (6th Cir. 2013), and their application to yet another fact pattern involving the relevance of a limited liability company's citizenship.

The presence of an unincorporated association, like a limited liability company, as a party to a federal Complaint or a Notice of Removal, signals the need for an extra measure of due diligence by the litigator. By now it should be generally known that the citizenship of a limited liability company will include, by attribution, the citizenship of each and every member. *Delay v. Rosenthal Collins Group, LLC*, 585 F.3d 1003 (6th Cir. 2009). But a limited liability company may have members that are limited liability companies as well. The inquiry and final resolution of the jurisdictional question may therefore require a descent into a tangled root system of the limited liability company's organizational tree. If one member or sub-member (or sub-sub-member….etc.) of the limited liability company is revealed to have the same citizenship as one of the opposing parties, then diversity jurisdiction does not exist. This is the general rule.

Any litigator who has embarked upon this sojourn and found, deeply buried along a remote root hair, a sub-sub-sub…member with an unexpected citizenship has likely experienced joy (if opposing jurisdiction) or horror (if seeking jurisdiction). And no matter on what side of this emotional state one happens to be, there must arise in both a certain sense of form over substance. This can be particularly poignant when, from all appearances, the sub-sub-sub…member had no connection whatsoever with the dispute presented. *Question: If such a member, if joined to the suit in its own capacity, would qualify as a "nominal party" at best, then is it proper to attribute its citizenship to a real party in interest for diversity jurisdiction purposes?*

For context, when adjudicating the issue of diversity jurisdiction, a federal district court must disregard nominal parties and decide only on the citizenship of the real parties in interest. *Certain Interested Underwriters at Lloyd's v. Layne*, 26 F.3d 39, 42 (6th Cir. 1994). So what is a nominal party? Here are some clues. A party may be a nominal party if it is not a "player" in the real dispute. A party may be a nominal party if it is not asserting a claim, even if it could. A party may be a nominal party if it does not have an interest in the result of the lawsuit. Expressed differently, a party may be a nominal party if it will not receive any relief from the outcome of the suit. In essence, a nominal party is only "…a spectator on the sideline. That it will give a trophy to the winner does not make it a player in the game." *Mortenson Family Dental Center, Inc. v. Heartland Dental Care, Inc.*, 526 Fed. Appx. 506, 509 (6th Cir. 2013). A nominal party appears to be the opposite of a "real party in interest." It may be the anti-real party in interest.

The "Spectator on the Sideline" test is not a brand new concept but was coined in 2013 in *Mortenson.* The Sixth Circuit in *Mortenson* was presented with a limited liability company that had been joined as one of two party plaintiffs to the lawsuit. The alleged nominal party had two members. One was the other party plaintiff, which was a corporation with a citizenship in Kentucky. The other was the Defendant corporation which had a citizenship in Delaware and Illinois. The Defendant sought removal to Federal District Court in Illinois but this was denied on the basis that the limited liability co-plaintiff exhibited aggregate citizenship in Kentucky, Delaware and Illinois, and the Defendant's citizenship was Delaware and Illinois.

On appeal, the citizenship of the limited liability company (Kentucky, Delaware and Illinois) named as a co-plaintiff was held to be irrelevant to diversity jurisdiction because the limited liability company was found to be a "nominal party." *Id.* at 509. Most recently, in *Kelley, supra*, *Mortenson* was cited in support of the proposition that a defendant limited liability company was also a "nominal party." It was argued by that same defendant that the citizenship of one its members should not be attributed to it where that member was comprised of sixteen (16) trusts and only one of them had the same citizenship as the plaintiff. However, in *Kelly*, the "nominal party" status was rejected, attribution of its member's citizenship was upheld, and diversity jurisdiction was defeated. With this in mind, how did *Kelley* and *Mortenson* differ?

In *Mortenson* the plaintiff and defendant disputed their percentage ownership in a limited liability company named Moreheart that was joined as the co-plaintiff. Moreheart was not a party to the operating agreement and, though the operating agreement granted certain rights to Moreheart, it had not asserted any of them and did not stand to obtain any relief. No claims were asserted against Moreheart. As such, the Sixth Circuit in *Mortenson* held that Moreheart was a nominal party whose citizenship was irrelevant for diversity purposes.

In *Kelly*, a plaintiff with a Kentucky citizenship sued two limited liability companies and an individual. The individual had a Pennsylvania citizenship. ASL, one of the two limited liability companies, had a Wisconsin citizenship. AFG, the second of the two, had two members, one of which, RDI Shareholder, was itself a limited liability company whose members consisted of sixteen (16) trusts, one which had a trustee with a Kentucky citizenship. The plaintiff in *Kelly* was injured when struck by a truck driven by an employee of ASL. AFG was alleged to have an ownership interest in ASL, to exercise managerial control over ASL, to be a primary member of ASL, and to be jointly and severally liable with ASL. *Kelley, supra*. As such, AFG was found to be a real party in interest, not a nominal party. Because AFG's citizenship was therefore relevant to diversity jurisdiction, the fact that both AFG and the plaintiff had a Kentucky citizenship defeated diversity jurisdiction.

But *Kelly* held that the Kentucky citizenship of the trustee should be attributed to AFG without *Kelly* giving any consideration as to whether or not RDI Shareholder itself would be a "nominal party." Rather, *Kelly* cited *Americold Realty Trust v. Conagra Foods, Inc.*, 136 S. Ct. 1012, 1016 (2016) for the proposition that the citizenship of all trustees is relevant in determining diversity. That may be true as to the citizenship of RDI Shareholder but it does not necessarily follow that RDI Shareholder would be anything but a "nominal party" if joined to the lawsuit in its own name. On the other hand, the Sixth Circuit in *Mortenson* was presented with members of the alleged nominal party which were each considered real parties in interest in their own right and were joined. Given this subtlety, it is not entirely clear as to whether the Sixth Circuit in *Mortenson* would have attributed RDI Shareholder's citizenship to AFG. This was the essential context addressed in *Mortenson* where the citizenship of a party plaintiff itself was considered irrelevant to diversity jurisdiction because it was a "nominal party." There are other moving parts in *Kelly* that ultimately may have led to the same result, but on this point caution may be required.

So what then is the proper application of the rule that, when adjudicating the issue of diversity jurisdiction, a federal district court must disregard nominal parties and consider only the citizenship of the real parties in interest? *See*, *Certain Interested Underwriters at Lloyd's v. Layne*, 26 F.3d 39, 42 (6th Cir. 1994). If the citizenship of a limited liability company, joined as a party, may be disregarded for diversity jurisdiction when that party is deemed to be a "nominal party," then why would the federal courts ever attribute the citizenship of its members (sub-members… sub-sub-members…etc.) if those members (sub-members…sub-sub-members…etc.) would never qualify as real parties in interest in their own right? In other words, if those members (sub-members…sub-sub-members…etc.) were simply "spectators on the sideline." Expressed differently yet again, why is the "nominalness" of a party so important that it will render the citizenship of that party irrelevant for jurisdictional purposes when the "nominalness" of a remote member or sub-member of that party is apparently not considered at all when evaluating whether it is appropriate to attribute its citizenship to that very party for jurisdictional purposes? This issue, which is not addressed in either *Mortenson* or *Kelly*, is a compelling one on its face. However, to unravel it and illuminate it for the error that it is, proves to be a rather complicated analysis.

Fortunately, the source of the answer appears to have been addressed by the United States Supreme Court in *Carden v. Arkoma Assocs.*, 494 U.S. 185 (1990). In *Carden*, the dissent would have applied a "real party to the controversy test" that would have disregarded the citizenship of a limited partner. This was rejected in *Carden* and expressed in the following terms: "In sum, we reject the contention that to determine, for diversity purposes, the citizenship of an artificial entity, the court may consult the citizenship of less than all of the entities members." Id. at 195. I recommend *Carden* and its progeny to you if further justification is required.

The lesson: When evaluating the citizenship of a limited liability company party for diversity jurisdiction purposes, attribute the citizenship of all of its members, and if those include limited liability companies, then sub-members and sub-sub…members etc. to the party. Once this is accomplished, if the attributed citizenship of any member is problematic for diversity jurisdiction, then consider whether the *party* is a "nominal party." If a "nominal party," then that party's citizenship should not be considered relevant for diversity jurisdiction purposes. If the party is not a "nominal party" then the aggregate attributed citizenship of all members (sub-members, sub-sub members…. etc.) are relevant for diversity jurisdiction purposes. It will not prove helpful to consider the "nominalness" of those members, sub members….sub-sub-members, as if they were joined as parties in their own right, in order to interfere with the attribution of their citizenship to the party actually joined to the lawsuit. As compelling as that analysis may appear, currently it would fail. Have fun.

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