DIVERSITY JURISDICTION: Where Do Dead Corporations Live?: Determining the Citizenship of Inactive Corporations for Diversity Jurisdiction Purposes

Dawn Levy

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WHERE DO DEAD CORPORATIONS LIVE?: DETERMINING THE CITIZENSHIP OF INACTIVE CORPORATIONS FOR DIVERSITY JURISDICTION PURPOSES

INTRODUCTION

Recently, there has been much debate regarding the continued viability of diversity jurisdiction in the modern era. However, since it appears that diversity jurisdiction will not be abolished anytime in the near future, all disputes concerning the applicability of diversity rules must be resolved in accordance with present constitutional and congressional requirements.

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1 Diversity jurisdiction is grounded in Article III, § 2 of the United States Constitution which provides that "judicial Power shall extend . . . to Controversies between Citizens of different States." Moreover, Congress has authorized district courts to hear cases involving citizens of different states if the amount in controversy requirement contained in 28 U.S.C. § 1332(a) is satisfied. Thus, the district courts have original jurisdiction over all civil actions where the matter in controversy exceeds the sum or value of $50,000 and is between citizens of different states.

2 See, e.g., William A. Braverman, Janus Was Not a God of Justice: Realignment of Parties in Diversity Jurisdiction, 68 N.Y.U. L. REV. 1072, 1084 n.56 (1993) ("there is simply no analogy between today's situation and that existing in 1789" when there was a real need for diversity jurisdiction) (citing HENRY J. FRIENDLY, FEDERAL JURISDICTION: A GENERAL VIEW 141 (1973)). One suggestion for revising the current diversity requirements is to limit the applicability of diversity jurisdiction to complex multi-state litigation, interpleader actions and suits involving aliens. See JUDICIAL CONFERENCE OF THE U.S., REPORT OF THE FEDERAL COURTS STUDY COMMITTEE 38-42 (1990). More modest changes include: (1) prohibiting plaintiffs from invoking diversity jurisdiction in their home states; (2) deeming corporations to be citizens of every state in which they are licensed to do business; (3) excluding attorney's fees, punitive damages and damages for pain and suffering from the amount in controversy; and (4) raising the jurisdictional amount to $75,000. See id.

3 See Braverman, supra note 2, at 1092 (stating that although Congress has been willing to regulate diversity jurisdiction at the margins, it has resisted attempts to eliminate it altogether).
As the law stands today, both natural born persons and corporations (artificial persons) are citizens of at least one state for diversity jurisdiction purposes.\(^4\) Natural persons are citizens of the state where they are domiciled, and corporations are citizens of the states where they are incorporated. Furthermore, 28 U.S.C. § 1332(c) provides that a corporation shall also be deemed a citizen of any state where it has its principal place of business. Therefore, for many corporations a dual citizenship is created because a corporation will be a citizen of both the state of its incorporation and the state of its principal place of business. Although there are different tests used to determine the principal place of business site,\(^5\) it is generally agreed that a corporation can only have one principal place of business.\(^6\)

Several recent diversity cases involving defunct or inactive\(^7\) corporations have sparked debate over (1) whether a corporation must have a principal place of business for diversity purposes, and, if so, (2) how that place is to be determined. The main issue in these cases is how to determine the citizenship of a corporation which is inactive at the time a diversity suit is commenced. Should the state of incorporation be the

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\(^4\) 28 U.S.C § 1332(a), (c) (1994).

\(^5\) See, e.g., Scot Typewriter Co. v. Underwood Corp., 170 F. Supp. 862 (S.D.N.Y. 1959) (creating a "nerve center" test which considers the site of executive and administrative functions in determining the corporation's principal place of business); cf. Kelly v. United States Steel Corp., 284 F.2d 850 (3d Cir. 1960) (creating a "bulk of activities" test which emphasizes the corporation's center of production or service activities).

\(^6\) See, e.g., U.S. Fidelity and Guar. Co. v. DiMassa, 561 F. Supp. 348 (E.D. Pa. 1983), aff'd, 734 F.2d 3 (3d Cir. 1984); Campbell v. Associated Press, 223 F. Supp. 151 (E.D. Pa. 1963) ("The use of the terms 'State' and 'its' in the amended Act—both terms used in the singular—indicates that one principal place of business was intended. If more than one place were contemplated, would not places have been used?"); see also CHARLES A. WRIGHT ET AL., 13B FEDERAL PRACTICE AND PROCEDURE § 3624, at 611 (2d ed. 1984) ("Section 1332(c) clearly requires that every corporation must have one—but only one—principal place of business").

\(^7\) The terms inactive and defunct are used interchangeably in this Note, as well as in the overwhelming majority of the relevant case law. Generally, the terms refer to a corporation which had been conducting business activities in a state, but subsequently ceased all active business conduct in that state. A small minority of cases does distinguish the two terms by using the word defunct to refer to the type of corporation described above, while reserving the term inactive for a corporation which has been granted a charter in a state but has not yet commenced business. See, e.g., Gavin v. Read Corp., 356 F. Supp. 483, 486 (E.D. Pa. 1973). For a detailed explanation of the term "inactive," see infra pp. 673-76.
sole determinant since an inactive corporation cannot have a place of business? Or should a defunct corporation’s last principal place of business, as well as the state of incorporation, determine its citizenship?

In addition to several district courts, three United States courts of appeals have considered this issue and reached different conclusions. The Second Circuit determined that an inactive corporation’s last principal place of business is always determinative of its citizenship, while the Third Circuit held that an inactive corporation cannot possibly have any principal place of business when it does not conduct any business activities. Somewhere in the middle of the continuum is the Fifth Circuit, which has held that an inactive corporation’s principal place of business is relevant, but not dispositive, in determining its citizenship. The majority of district courts addressing the issue is in accord with the Second Circuit approach.

This Note argues that in order to effectuate the true purpose of the federal diversity statute and to prevent abuse of the federal judicial system, an inactive corporation’s last principal place of business must be a determinative factor in ascertaining its citizenship for diversity purposes. Part I of this Note briefly discusses the history of diversity jurisdiction, focusing on the congressional intent and reasons for adopting the diversity rule. Part II analyzes the inactive corporation and the problems that arise when such an entity is involved in

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9 Wm. Passalacqua Builders, Inc. v. Resnick Developers South, Inc., 933 F.2d 131 (2d Cir.), aff’d, 933 F.2d 131 (2d Cir. 1991).


11 Harris v. Black Clawson Co., 961 F.2d 547 (5th Cir. 1992).

potential diversity litigation. This Part also examines the different approaches of the only three United States courts of appeals that have addressed this problem. Finally, Part III compares the various circuit courts’ approaches and concludes that the Second Circuit approach best comports with the rationale for diversity jurisdiction and prevents misuse of the federal system.

I. THE HISTORY AND PURPOSE OF DIVERSITY JURISDICTION

A. The Early Years—The Constitutional and Pre-1958 Attitude Towards Diversity

The framers of the United States Constitution granted the federal judiciary diversity jurisdiction in order to create a neutral forum to protect foreign (out-of-state) litigants from the inherent prejudices of the local state courts. The framers, guided by their desire to preserve the peace of the union, designed this mechanism to reduce disharmony between citizens of the different states. As James Madison explained, “It may happen that a strong prejudice may arise in some states, against the citizens of others [so that]...[a] citizen of another state might not...get justice in a state court.” Diversity jurisdiction, it was argued, would reduce the friction between citizens of the different states by providing a neutral forum to litigate their disputes, thereby achieving national harmony and unity among the states. Consequently, judicial interpreta-

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13 See Burgess v. Seligman, 107 U.S. 20, 34 (1883) (“the very object of giving to the national courts jurisdiction...in controversies between citizens of different states was to institute independent tribunals, which...would be unaffected by local prejudices and sectional views...”); see also J.A. Olson Co. v. Winona, 818 F.2d 401 (5th Cir. 1987); Asher v. Pacific Power & Light Co., 249 F. Supp. 671 (N.D. Cal. 1965); S. REP. No. 1830, 85th Cong., 2d Sess. (1958), reprinted in 1958 U.S.C.C.A.N 3102 [hereinafter S. REP. No. 1830]; WRIGHT ET AL., supra note 6, § 3601.

14 See Braverman, supra note 2, at 1079.


tions of diversity rules should be consistent with this strong policy of protecting the foreign litigant from local prejudices.

Diversity jurisdiction was also created to encourage interstate commerce and investment. The framers hoped that diversity jurisdiction would provide the nation's merchants with security concerning the contracts they made in foreign states. In fact, both scholars and legislators have argued that no other single element in our governmental system has done as much to promote the development of enterprises as the existence of federal courts sitting in diversity cases.

B. Post-1958—Abuse and the Modern Trend Toward Limiting Diversity Jurisdiction

In 1958, Congress amended 28 U.S.C. § 1332, so that a corporation is deemed a citizen of "any state by which it has been incorporated and of the state where it has its principal place of business." The legislative history behind the 1958 amendment provides much insight into the reasons for its adoption and the expected results of its implementation. Two main objectives dominated the amendment's adoption. First, the amendment was designed to ease the workload of the federal courts. If a corporation is a citizen of both its state of incorporation and principal place of business, the likelihood that complete diversity exists between the parties is diminished. As a result, the number of diversity cases heard by the federal courts is reduced.

Second, the amendment attempted to remedy the abuse created by entirely local corporations invoking diversity juris-

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17 Braverman, supra note 2, at 1078, 1081-82.
20 28 U.S.C. § 1332(c) (1958). The amendment also increased the amount in controversy to $10,000 to help reduce the workload of the federal courts sitting in diversity jurisdiction. Moreover, in 1988 Congress further restricted the number of diversity cases by increasing the jurisdictional amount to the current amount of $50,000.
21 See generally S. REP. NO. 1830, supra note 13; see also WRIGHT ET AL., supra note 6, § 3624.
diction. In essence, the pre-1958 statute gave "rise to the evil whereby a local institution, engaged in a local business and in many cases locally owned," was able to litigate in the federal courts simply because it had obtained a charter from another state. Similarly, local plaintiffs were abusing the diversity rule by dragging entirely local corporations into federal court. Therefore, by amending 28 U.S.C. § 1332 to include a corporation's principal place of business to determine its citizenship, Congress purported to preclude what were in fact local entities from suing, or being sued by, local citizens in federal court simply because they were chartered in a different state.

In fact, the Senate committee that proposed the 1958 amendment found that 62% of all diversity cases involved corporations as parties. More significant, however, is the 1951 Report of the Committee on Jurisdiction and Venue statistic demonstrating that 57.3% of all diversity cases contained a non-resident corporation doing business in the local state. This second statistic firmly corroborates the assertion that prior to the 1958 amendment the authority to invoke diversity jurisdiction was being abused, particularly in cases involving local corporations chartered in foreign states.

Moreover, the Senate report underlying the new amendment emphasized that diversity jurisdiction was meant to "provide a separate forum for out-of-state citizens against prejudices of local courts and local juries." Furthermore, diversity jurisdiction "was never intended to extend to local corporations which, because of a legal fiction, [could be] considered

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22 See generally S. REP. NO. 1830, supra note 13; see also WRIGHT ET AL., supra note 6, § 3624.
23 S. REP. NO. 1830, supra note 13, at 3101-02; see Black and White Taxicab and Transfer Co. v. Brown and Yellow Taxicab and Transfer Co., 276 U.S. 518 (1928).
24 See generally S. REP. NO. 1830, supra note 13; see also WRIGHT ET AL., supra note 6, § 3624.
26 S. REP. NO. 1830, supra note 13, at 3100.
27 S. REP. NO. 1830, supra note 13, at 3111.
28 S. REP. NO. 1830, supra note 13, at 3102.
citizens of another state." The "fiction" the report referred to was the "stamping" of a corporation as a citizen of its state of incorporation only, regardless of where a majority of the corporation's activity occurred. The pre-1958 diversity statute permitted this type of legal fiction. Therefore, the main concern of the amendment was to remedy this evil by limiting the circumstances under which a corporation could sue or be sued in federal court.

Although the Senate committee was attempting to limit diversity jurisdiction, it was not urging that diversity jurisdiction be abolished altogether. In fact, the Senate report emphasized a bulk of expert opinions which indicated that local prejudice continues to exist despite the existence of the highly integrated society in which we live. Moreover, the Senate committee proclaimed that diversity jurisdiction is "essential to the proper administration of justice under the system of dual sovereignty established by [the] Constitution." In essence, it is a way of maintaining the proper balance between the authority of the individual states and that of the federal government. Thus, Congress' position when it amended 28 U.S.C. § 1332(c) in 1958 was that diversity jurisdiction remain an integral part of the judicial system while litigants' abuse of its protections be eliminated.

Contrary to the manifest reasons for the amendment's adoption, how the amendment would be implemented is somewhat less obvious from its legislative history. One original committee proposal suggested that a corporation be deemed a citizen of its state of incorporation and of any state from which it derived more than half its gross income. A second proposal suggested that a corporation be deemed a citizen of its state

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29 S. REP. No. 1830, supra note 13, at 3101.
30 S. REP. No. 1830, supra note 13, at 3101-02.
31 S. REP. No. 1830, supra note 13, at 3116-17; see Charles L. Brieant, Diversity Jurisdiction: Why Does the Bar Talk One Way But Vote the Other Way With Its Feet?, 60 N.Y.S.B.J. 20, 21 (1989) ("anyone who believes that there is no local chauvinism in the state courts is hiding his head somewhere").
32 S. REP. No. 1830, supra note 13, at 3116.
33 S. REP. No. 1830, supra note 13, at 3116.
of incorporation and of every state in which it is doing business. The committee rejected these two proposals, however, and instead recommended the "principal place of business" standard because it was a simpler and more familiar criteria for courts to apply. The committee report indicates that because the "principal place of business" test of citizenship had ample precedent in court decisions and in federal statutes, such as the Bankruptcy Act, courts already had "sufficient criteria to guide [them] in future litigation under [the new] bill." For example, in a bankruptcy proceeding, a bankrupt corporation's state of incorporation and its last principal place of business are determinative for diversity jurisdiction purposes. Thus, when Congress passed the 1958 amendment, it intended for federal courts to interpret "principal place of business" in diversity cases as it is interpreted in the Bankruptcy Code.

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37 For discussion of these provisions and their relation to citizenship of inactive corporations, see infra pp. 686-87.
38 S. REP. No. 1830, supra note 13, at 3102.
40 Wm. Passalacqua Builders, Inc. v. Resnick Developers South, Inc., 933 F.2d 131, 141 (2d Cir. 1991); see MANUAL FEDERAL PRACTICE, supra note 26, § 1.25; infra pp. 686-87 on Fada case for an explanation of bankruptcy provisions.
II. THE UNIQUE PROBLEMS OF INACTIVE CORPORATIONS INVOLVED IN DIVERSITY JURISDICTION LITIGATION

It is agreed that Congress intended for corporations to have only one principal place of business,41 despite the possibility that corporations might conduct substantial business activities in numerous states.42 However, it is unclear whether Congress considered the opposite scenario—that an inactive corporation might not have a principal place of business at all.43 Therefore, when a corporation is inactive at the time a diversity suit is filed against it, there is an issue as to whether the corporation has a principal place of business to determine its citizenship for diversity purposes.

A. Inactive Corporations and the Traditional Tests of Principal Place of Business

A corporation may be deemed inactive in a state when, at the time the suit is filed, "only a flicker of corporate activity remains."44 This flicker of activity generally refers to the winding up of old business45 and precludes affirmative activities such as the production of goods and services46 and the conducting of any active business.47

41 U.S. Fidelity and Guar. Co. v. DiMassa, 561 F. Supp. 348, 351 n.8 (E.D. Pa. 1983), aff'd, 734 F.2d 3 (3d Cir. 1984); Campbell v. Associated Press, 223 F. Supp. 151, 154-55 (E.D. Pa. 1963) ("The use of the terms 'State' and 'its' in the amended Act—both terms used in the singular—indicates that one principal place of business was intended. If more than one place were contemplated, would not places have been used?"); see WRIGHT ET AL., supra note 6, § 3624 ("Section 1332(c) clearly requires that every corporation must have one—but only one—principal place of business.").

42 Sanders Co. Plumbing and Heating v. B.B. Andersen Constr. Co., 660 F. Supp. 752, 755 (D. Kan. 1987) ("It appears that Congress recognized but did not accept the possibility that a corporation would have many offices in many states at which it transacts a substantial amount of business . . . .").

43 Id. at 754 ("Congress does not appear to have considered the antithesis—that an inactive corporation may have no principal place of business at all.").


46 Comtec, 711 F. Supp. at 523 n.3.

Several factors, rather than one dispositive element, usually combine to trigger a corporation's inactive status. For example, a corporation is clearly dormant if it has not generated revenue, has not entered into contracts and has not employed paid personnel for a period of years. Similarly, when a corporation has ceased conducting any active business, has no substantial assets or liabilities, and has no address, telephone number or employees, it is inactive. Moreover, other indicia of a corporation's inactive status are the failure to maintain an office in a state, failure to possess any office equipment or furniture, and failure to make any sales or purchases in the state. Inactivity is also presumed when a corporation has no business office, no employees, no service personnel and no other ongoing activities. Finally, in addition to becoming inactive by a voluntary withdrawal from business activity in a state, a corporation may also be rendered inactive by government or administrative action.

Therefore, for purposes of diversity jurisdiction analysis, the relevant factors considered in determining whether a corporation is inactive in a particular state are whether the corporation: (1) has ceased conducting all active and ongoing business activities, including entering into contracts or making any sales or purchases; (2) has any substantial assets or liabilities in the state; (3) has any employees or pays any wages or salaries; (4) occupies any office space; (5) owns, rents or possesses any office equipment or furniture; and (6) has an address or telephone number where it can be reached in the state.

It is not necessary, however, for the corporation and the state to have absolutely no connection in order for the corporation to be considered inactive. For example, the failure to cancel a corporation's certificate of incorporation or to formally

155 (E.D.N.C. 1993).
49 Storr Office Supply, 832 F. Supp. at 156.
51 Harris v. Black Clawson Co., 961 F.2d 547, 550 (5th Cir. 1992).
52 See, e.g., Midlantic Nat'l Bank v. Hansen, 48 F.3d 693, 694 (3d Cir.) (holding that corporation was rendered inactive when the Office of Thrift Supervision and the Resolution Trust Company seized its holdings forcing it to cease actively engaging in business), cert. dismissed, 116 S. Ct. 32 (1995).
53 Interpetrol Bermuda Ltd. v. Rosenwasser, No. 86 Civ. 5631, 1987 WL 7734,
dissolve the corporation\textsuperscript{64} will not by itself preclude a corporation's inactive status. Similarly, listing a state as a corporation's principal place of business in annual reports and other documents filed with the government does not defeat a corporation's inactive status.\textsuperscript{65} Moreover, the mere storage of corporate records,\textsuperscript{66} the conduct of a lawsuit,\textsuperscript{67} the maintenance of an agent authorized to receive complaints,\textsuperscript{68} or the ownership of some accounts receivable,\textsuperscript{69} standing alone, are all insufficient to void a corporation's inactive status.

When a corporation is active, however, various courts employ different tests to determine the site of a corporation's principal place of business. There are three basic tests. Some jurisdictions, including New York, apply the "nerve center" test which defines the principal place of business as the site of executive and administrative functions.\textsuperscript{69} Other jurisdictions utilize a "place of activities" test which looks to the corporation's center of production or service activities in determining its principal place of business.\textsuperscript{70} Lastly, some jurisdictions use a "total activity test" which first considers the general rules of the two previous tests in light of the particular circumstances of a corporation's organization, and then balances the facts of each case to determine the location of the corporation's principal place of business.\textsuperscript{71}

\textsuperscript{64} \textit{Gavin}, 356 F. Supp. at 486 (holding that despite corporation's failure to dissolve, it was still deemed inactive for principal place of business analysis).
\textsuperscript{65} \textit{See}, e.g., \textit{Harris}, 961 F.2d at 550; \textit{see also} \textit{Sanders} Co. Plumbing and Heating v. B.B. Andersen Constr. Co., 660 F. Supp. 752, 764 n.² (D. Kan. 1987).
\textsuperscript{66} \textit{See}, e.g., Wm. Passalacqua Builders, Inc. v. Resnick Developers South, Inc., 608 F. Supp. 1261, 1263 (S.D.N.Y. 1985); \textit{see also} \textit{Sanders}, 660 F. Supp. at 753 (finding corporation had ceased operations in state despite presence of certain closed files placed at a rented storage facility).
\textsuperscript{67} \textit{See}, e.g., \textit{Passalacqua}, 608 F. Supp. at 1263.
\textsuperscript{68} \textit{See}, e.g., \textit{Gavin}, 356 F. Supp. at 486.
\textsuperscript{70} \textit{See}, e.g., \textit{Scot Typewriter Co. v. Underwood Corp.}, 170 F. Supp. 862, 865 (S.D.N.Y. 1959).
\textsuperscript{71} \textit{See}, e.g., \textit{Kelly} v. United States Steel Corp., 284 F.2d 850, 854 (3d Cir. 1960).
\textsuperscript{72} \textit{See}, e.g., \textit{Harris} v. Black Clawson Co., 961 F.2d 547, 549 (5th Cir. 1992); \textit{see also} \textit{WRIGHT ET AL.}, supra note 6, § 3625, at 625 (arguing that \textit{Scot} and \textit{Kelly} can simply be viewed as applications of the rule that the bulk of corporate activity governs the choice of principal place of business) (cited in \textit{Harris}, 961 F.2d at 549.
These traditional tests for determining a corporation's principal place of business do not offer much assistance when confronted with an inactive corporation. This is so because there are no factors to use to establish an inactive corporation's principal place of business. There are no business activities, no employees and no office. If a principal place of business can be established for a corporation using the traditional tests, this means that the corporation has enough connections with the state to be deemed active in that state.

Thus, determining the principal place of business of an inactive corporation differs from doing so for an active corporation. While the traditional tests can be used to determine the principal place of business of the corporation while it was active, once the corporation is inactive a further analysis is necessary. A court must decide whether the previous determination of the principal place of business will stand, or whether the previous determination is void because the factors upon which it was based (e.g., place of activities or nerve center) no longer exist. The appellate courts are split on this second part of the analysis.

B. The Circuit Split on the Relevance of Last Principal Place of Business

Only three United States courts of appeals have addressed the issue of the citizenship of an inactive corporation. Each court, relying on congressional intent and plain meaning interpretations of the federal diversity statute, has reached a different result.

1. The Second Circuit Approach: Last Principal Place of Business Always Considered

The Second Circuit addressed the issue of an inactive corporation's citizenship for the purposes of diversity jurisdiction in *Wm. Passalacqua Builders, Inc. v. Resnick Developers South, Inc.* Wm. Passalacqua Builders ("Passalacqua"), a

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64 933 F.2d 131 (2d Cir. 1991).
building contractor, contracted with Resnick Developers South ("Developers") to build a hotel in Florida.\textsuperscript{65} Passalacqua was incorporated in Ohio and qualified to do business in Florida, while Developers was incorporated in Florida.\textsuperscript{65} Passalacqua sought arbitration to resolve disputes over the price of extra work needed to complete the contract. The arbitrator entered a final judgment against Developers.\textsuperscript{67} After Developers had satisfied approximately half of the judgment, Passalacqua brought suit against Developers in the United States District Court for the Southern District of New York.\textsuperscript{63} At the time suit was filed, Passalacqua was an inactive corporation whose last business activity was in Florida.\textsuperscript{69}

Developers challenged the district court's subject matter jurisdiction by arguing that Passalacqua's principal place of business when the suit commenced was Florida, its last principal place of business.\textsuperscript{70} Therefore, since both Passalacqua and Developers were citizens of Florida, complete diversity was lacking. Passalacqua, on the other hand, argued that it did not have a principal place of business because it was inactive at the time suit was filed.\textsuperscript{71} Thus, Passalacqua argued it was a citizen only of Ohio, its place of incorporation, and since Developers was a citizen of Florida only, complete diversity existed.\textsuperscript{72}

The district court held that although Passalacqua was an inactive corporation at the time the suit was brought, it was still a citizen of Florida, its last principal place of business.\textsuperscript{73} The court based its holding upon the decision in \textit{Puerto Rico Maritime Shipping Authority v. Star Lines},\textsuperscript{74} which held that the principal place of business for a corporation that is inactive at the time suit is filed is the state of the corporation's last business activity. Thus, since Developers was incorporated in,

\textsuperscript{65} \textit{Id.} at 133.
\textsuperscript{67} \textit{Passalacqua}, 933 F.2d at 133-34.
\textsuperscript{68} \textit{Id.} at 134.
\textsuperscript{69} \textit{Passalacqua}, 608 F. Supp. at 1263.
\textsuperscript{70} \textit{Id.}
\textsuperscript{71} \textit{Id.}
\textsuperscript{72} \textit{Id.}
\textsuperscript{73} \textit{Id.} at 1263-64.
\textsuperscript{74} No. 78 Civ. 602 (S.D.N.Y. 1979).
and therefore was a citizen of, Florida, Passalacqua was a non-diverse plaintiff.\textsuperscript{75} Furthermore, because Passalacqua was an indispensable party to one count of the complaint, its absence from the action required the dismissal of the entire count.\textsuperscript{76}

On appeal, the Second Circuit affirmed the district court's interpretation that when a corporation has ceased business activity, diversity jurisdiction is determined by the corporation's state of incorporation and by the place it last transacted business.\textsuperscript{77} The appellate court, relying on notions of congressional intent, argued:

To allow inactive corporations to avoid inquiry into where they were last active would give them a benefit Congress never intended for them, since under such a rule a defunct corporation, no matter how local in character, could remove the case to federal court based on its state of incorporation.\textsuperscript{78}

A rule that the corporation's last principal place of operation is dispositive of its citizenship precludes inherently local corporations from invoking diversity jurisdiction simply on the basis of their state of incorporation.

Moreover, the appellate court compared the diversity statute\textsuperscript{79} to the federal bankruptcy laws in effect at the time.\textsuperscript{80} This comparison, the court noted, is particularly instructive because Congress amended 28 U.S.C. § 1332(c) in 1958 to follow the provisions of the bankruptcy laws.\textsuperscript{81} The Bankruptcy Code grants lower courts jurisdiction over a bankrupt corporation either in its place of domicile or in its principal place of operation.

\textsuperscript{75} Passalacqua, 608 F. Supp. at 1261.

\textsuperscript{76} Id. at 1263-64. The first two counts of the complaint were for equitable relief seeking to pierce the corporate veil, since Developers was among several corporate entities controlled entirely by members of the Resnick family. The third count was for fraud, and the fourth count alleged an oral guarantee by one of the defendants to pay the sum owed. The fraud count was the one dismissed because Passalacqua was indispensable. However, since Passalacqua was not indispensable to the resolution of the remaining claims against defendants, \textit{FED. R. CIV. P. 19(b)} did not require the entire complaint to be dismissed. \textit{Wm. Passalacqua Builders, Inc. v. Resnick Developers South, Inc.}, 933 F.2d 131, 141 (2d Cir. 1991).

\textsuperscript{77} Passalacqua, 933 F.2d at 141.

\textsuperscript{78} Id.

\textsuperscript{79} 28 U.S.C § 1332(c) (1988).

\textsuperscript{80} Passalacqua, 933 F.2d at 141.

business. The appellate court then referred to *Fada of New York, Inc. v. Organization Service Co.*, which authorized a New York district court's jurisdiction over a bankrupt corporation even though New York had not been its place of business for at least six months prior to the filing of the bankruptcy petition. Thus, since the new diversity laws were modeled after the bankruptcy provisions, the court concluded that issues concerning citizenship for diversity purposes should be decided according to the same standards as those established for bankruptcy matters.

In sum, the Second Circuit's approach is that when a corporation has ceased business activities in a state at the time suit is brought, its citizenship for diversity jurisdiction, similar to bankruptcy jurisdiction, is determined by both the state of incorporation and the last principal place of business.

2. The Third Circuit Approach: Last Principal Place of Business Never Considered

The Third Circuit considered the issue of inactive corporations and diversity in *Midlantic National Bank v. Hansen*. Midlantic National Bank ("Midlantic"), a national banking association with its principal place of business in New Jersey, made several loans to Elmer and Eileen Hansen, the joint owners of all stock of Hansen Bancorp, Inc. ("HBI"), a corporation organized under the laws of Delaware. HBI used some of these funds to finance the purchase of two savings and loan associations, one in Florida and one in New Jersey. In January of 1992, the Office of Thrift Supervision and the Resolution Trust Corporation seized control of the Hansens' New Jersey

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24 125 F.2d 120 (2d Cir. 1942).
25 Id. at 121.
27 Id.
28 48 F.3d 693 (3d Cir.), *cert. dismissed*, 116 S. Ct. 32 (1995) (*certiorari* was dismissed upon request of the parties pursuant to Rule 46.1 of the United States Supreme Court Rules).
29 Id. at 694.
30 Id.
The seizure rendered HBI inactive because HBI was a holding company and when all of its holdings were seized, it was forced to cease actively engaging in business.

Six months later Midlantic brought a collection suit against HBI for defaulting on several of the loans in the New Jersey district court based on diversity jurisdiction. Midlantic argued that it was diverse from HBI because HBI was not active in New Jersey, Midlantic’s principal place of business, at the time the suit was brought. Therefore, HBI was a citizen of Delaware only, its state of incorporation. HBI challenged the federal jurisdiction, contending that its principal place of business at the time the suit was brought was indeed New Jersey, even though it had been inactive for six months prior to the commencement of the suit.

As evidence of HBI’s New Jersey citizenship, the Hansens claimed that at the beginning of 1991 HBI moved its headquarters from Pennsylvania to New Jersey. In addition, in an affidavit submitted to the district court, HBI’s chairperson of the board and chief executive officer alleged that: (1) in 1991 HBI transferred all its books and records, including all accounting and financial records, to New Jersey; (2) in early 1991 all employees of HBI were terminated or transferred to positions with the New Jersey subsidiary; (3) from the beginning of 1991 HBI’s chief executive officer’s office was located in New Jersey; and (4) from early 1991 substantially all of the accounting, financial, corporate and legal activities were conducted from HBI’s headquarters in New Jersey.

The Hansens argued that the five months between HBI’s cessation of business activities and the filing of the complaint “did not . . . dissipate HBI’s local character for diversity purposes.” Therefore, the Hansens argued that since HBI’s last principal place of business was New Jersey, and that since

90 Id. at 695.
91 Id. at 695 n.2.
92 Hansen, 48 F.3d at 695.
93 Id. at 694.
94 Id.
95 Id. at 696.
96 Id. at 696 n.3.
97 Hansen, 48 F.3d at 696 n.3.
98 Id. at 696.
Midlantic's principal place of business was also New Jersey, complete diversity did not exist. The district court was not persuaded by the Hansens' reasoning and denied their motion to dismiss the suit for lack of subject matter jurisdiction.

On appeal, the Third Circuit held that, for purposes of diversity jurisdiction, an inactive corporation is a citizen of its state of incorporation only. The appellate court relied heavily on the rule that diversity jurisdiction is determined by examining the citizenship of the parties at the time the complaint is filed. The court began its discussion by stressing the fact that HBI was an inactive corporation at the time the complaint was filed. Furthermore, the court emphasized that "corporate activities" determine a corporation's principal place of business. This implies that a corporation without corporate activities, by definition, has no principal place of business. The court went on to conclude:

Inasmuch as we consider the actual business activities of the corporation to be determinative of the corporation's principal place of business, we conclude that as a general matter, an "inactive" corporation (that is, a corporation conducting no business activities) has no principal place of business, and is instead a citizen of its state of incorporation only.

Thus, the court held that since HBI was inactive at the time Midlantic filed suit, HBI could not have any principal place of business and was, therefore, only a citizen of its state of incorporation, Delaware.

The Third Circuit did acknowledge, however, that its holding conflicted with those reached by the Second and Fifth Circuits. Particularly, the Third Circuit responded to the Sec-

\[\text{id:1996}\]

\[\text{CITIZENSHIP OF INACTIVE CORPORATIONS}\]

\[\text{679}\]
ond Circuit’s concern that a local corporation may subvert Congress’ intent in enacting the principal place of business provision.109 The Third Circuit noted that by amending 28 U.S.C. § 1332, Congress purported to preclude what was in fact a local entity from suing, or being sued by, a local citizen in federal court simply because it was chartered in another state.110 Nevertheless, the Third Circuit determined that the benefits of certainty and clarity that are obtained from its “bright line” rule outweigh the potential harm identified by the Second Circuit.111 The Third Circuit also acknowledged the Second Circuit’s reliance upon Congress’ structuring of the 1958 amendment to 28 U.S.C. § 1332(c) to follow the provisions of the bankruptcy laws.112 The Third Circuit reasoned, however, that while Congress did originally instruct courts to look to bankruptcy precedent for guidance in interpreting the amended diversity statute, there had been emerging a set of separate principles and criteria for making the jurisdictional determination over the previous three decades.113

In addition, the Third Circuit admitted that its opinion conflicted with the majority of the district courts.114 Like the Second Circuit, most lower federal courts have held that an inactive corporation is a citizen of both its state of incorporation and of its last principal place of business.115 These district courts support their position with a plain meaning argument. They rely on Congress’ inclusion of the conjunction “and” when it amended the diversity statute to include a corporation’s principal place of business as a determinant of citizenship.116 Section 1332(c) expressly states that a corpora-

109 Id. at 698.
110 Id. at 698 n.7 (quoting JAMES W. MOORE ET AL., MOORE’S FEDERAL PRACTICE ¶ 0.77[3.-4] (2d ed. 1996)).
111 Id. at 698.
112 Hansen, 48 F.3d at 697 n.5.
113 Id. (citing JAMES W. MOORE ET AL., MOORE’S FEDERAL PRACTICE ¶ 0.77[3.-1] (2d ed. 1996)).
114 Id. at 697.
116 28 U.S.C § 1332(c)(1) (1994) (“a corporation shall be deemed a citizen of any state by which it has been incorporated and of the State where it has its principal place of business”) (emphasis added).
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...tion is a citizen of its state of incorporation and its principal place of business. By using the word “and,” Congress could not have meant that a corporation’s citizenship would be its principal place of business or its state of incorporation.117

The Third Circuit rejected this plain meaning argument, claiming that it did not believe Congress’ use of the conjunction “and” signifies its intention for courts to strain to locate a principal place of business when no such place exists.118 In fact, the Third Circuit reasoned that had Congress intended for the principal place of business to determine a corporation’s citizenship, Congress could have easily crafted the statute to read that a corporation is a citizen of the state in which it “has or has had” its principal place of business.119 Thus, the Third Circuit rejected the notion that the statute implicitly requires all corporations to have a principal place of business.120

3. The Fifth Circuit Approach: Last Principal Place of Business Considered on Case By Case Basis

The Fifth Circuit addressed the issue of the inactive corporation’s citizenship for diversity in Harris v. Black Clawson Co.121 Harris was injured in an industrial accident while working at the Manville Forest Products Corporation’s Louisiana plant.122 He was severely burned when steam was accidentally injected into a concrete machine he had been working on as part of a maintenance team.123 The other two members of the team were killed in the accident.124 Harris, together with the representatives of the other men, brought suit in Louisiana state court. The defendants removed the case to the United States District Court for the Western District of

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117 Allendale, 818 F. Supp. at 1304-05; see Comtec, 711 F. Supp. at 524 (stating that “[b]y using the conjunction ‘and,’ Congress intended for all of the requirements of the statute to be fulfilled”).
118 Hansen, 48 F.3d at 698.
119 Id.
120 Id.
121 961 F.2d 547 (5th Cir. 1992).
122 Id. at 548-49.
123 Id.
124 Id.
Louisiana. The plaintiffs were then given leave to add another two defendants, one of which was Ford, Bacon and Davis Construction Company ("FB & DCC").

At the time the suit was filed, FB & DCC had been inactive in Louisiana for over five years. It had no business office, no employees and no other ongoing business activities in Louisiana. After adding FB & DCC, plaintiffs moved to remand the case to the state court. Plaintiffs argued that FB & DCC was a citizen of Louisiana because Louisiana was its last principal place of business. Therefore, because all the plaintiffs were also Louisiana citizens, complete diversity was destroyed. The plaintiffs maintained that despite its inactive status, FB & DCC was still a citizen of Louisiana because while inactive it represented in its annual reports and other documents filed with the Louisiana Secretary of State that its principal place of business was Louisiana.

The *Harris* district court rejected this argument stating that such reports and filings were not dispositive for diversity jurisdiction purposes. The district court then provided examples of other contexts where representations to government agencies, such as the Secretary of State or the Securities and Exchange Commission, are not binding for purposes of diversity jurisdiction. The district court dismissed the plaintiffs' subject matter jurisdiction challenge and granted summary judgment for the defendants on the ground that plaintiffs' claims were barred by the Louisiana Statute of Repose.

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125 *Id.*
126 *Harris*, 961 F.2d at 549.
127 *Id.* at 550 n.6.
128 *Id.* at 550.
129 *Id.* at 549.
130 *Id.*
131 *Harris*, 961 F.2d at 550.
132 *Id.*
134 *Harris*, 961 F.2d at 551 (LA. REV. STAT. ANN. § 9:2772 (1991) precludes any suit based on the allegedly defective "design . . . or construction of an improvement to immovable property" from being brought more than ten years after the completion of work performed).
Rather than adopt a bright line test similar to either the Second or Third Circuit, the Fifth Circuit adopted a more flexible approach regarding an inactive corporation's citizenship. On appeal from the *Harris* district court, the Fifth Circuit held that although an inactive corporation's last place of business is not dispositive, it is relevant to a determination of its citizenship for diversity purposes. Moreover, the Fifth Circuit held that the amount of time that has elapsed between the corporation's cessation of business activities and the commencement of the suit should determine the relevance of its last place of business in a diversity jurisdiction analysis. Thus, as a matter of law, where a corporation has been inactive for a substantial period of time, then that state is not the principal place of business. However, if the corporation has been inactive for a short period of time, then its last principal place of business will be relevant in determining its citizenship for diversity purposes. The Fifth Circuit noted that questions of substantiality must be decided on a case-by-case basis.

The Fifth Circuit concluded that because FB & DCC had been inactive in Louisiana for over five years prior to the filing of the suit, a substantial amount of time, Louisiana was not its principal place of business. Therefore, complete diversity existed between the parties. The appellate court found it unnecessary to determine whether a corporation is required by 28 U.S.C. § 1332 to have a principal place of business because all of the plaintiffs were citizens of Louisiana and as long as defendant was not a citizen of Louisiana, complete diversity existed.

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125 *Id.*
126 *Id.; see* Midlantic Nat'l Bank v. Hansen, 48 F.3d 693, 697 (3d Cir.) (discussing the approach of the Fifth Circuit in *Harris*, 961 F.2d at 551.
127 *Harris*, 961 F.2d at 551.
128 *Id.* at 551 n.10.
129 *Id.* at 551.
130 *Id.*
131 *Cf.* Midlantic Nat'l Bank v. Hansen, 48 F.3d 693, 698 (3d Cir.) ("We reject the notion that implicit in the statute's terms is the requirement that all corporations be deemed to have a principal place of business."), *cert. dismissed*, 116 S. Ct. 32 (1995).
132 *Harris*, 961 F.2d at 551 n.12.
III. A COMPARISON OF THE THREE APPROACHES

Determining which of the three approaches to the diversity issue is the best requires a thorough analysis of the federal diversity statute.\footnote{28 U.S.C. § 1332 (1994).} The strict construction, plain meaning and legislative history prongs of such an analysis all point to the superiority of the Second Circuit approach.\footnote{At least one commentator agrees that it would be feasible and desirable for the courts to hold that no principal place of business exists for a corporation in certain situations. \textit{See} Friedenthal, \textit{supra} note 81, at 213, 224 (pointing out that even the members of the judicial conference that proposed the amendment admitted that in some situations it might not be possible to identify a principal place of business). This position appears to be in accord with the Third and Fifth Circuit approaches. However, this author is referring to situations where corporate enterprises are so widely dispersed geographically that there are too many places which could serve as a principal place of business. \textit{See}, e.g., \textit{Kelly v. United States Steel Corp.}, 284 F.2d 850, 853 (1960) (stating that the concept of principal place of business may get artificial in some cases, like the one at bar, where the corporation had fourteen divisions of the parent corporation and eleven principal subordinate companies, in addition to the fact that company’s manufacturing activities were spread practically all over the U.S. and extended to foreign countries). In contrast, when dealing with a defunct corporation in a diversity case, the issue is not how to determine the principal place of business among a multitude of choices, but rather whether such a place actually exists. Therefore, since the inquiries are different, it is not imperative that the same rule apply in both situations.} \footnote{\textit{Kantor v. Wellesley Galleries Ltd.}, 704 F.2d 1088, 1092 (9th Cir. 1983); \textit{see} \textit{China Basin Properties, Ltd. v. One Pass, Inc.}, 812 F. Supp. 1038 (N.D. Cal. 1993).}

A. Strict Construction Analysis

Traditionally, the federal diversity statute is strictly construed.\footnote{\textit{Kantor}, 704 F.2d at 1092; \textit{see} \textit{One Pass}, 812 F. Supp. 1038.} Therefore, any doubts should be resolved against finding jurisdiction.\footnote{At least one commentator agrees that it would be feasible and desirable for the courts to hold that no principal place of business exists for a corporation in certain situations. \textit{See} Friedenthal, \textit{supra} note 81, at 213, 224 (pointing out that even the members of the judicial conference that proposed the amendment admitted that in some situations it might not be possible to identify a principal place of business). This position appears to be in accord with the Third and Fifth Circuit approaches. However, this author is referring to situations where corporate enterprises are so widely dispersed geographically that there are too many places which could serve as a principal place of business. \textit{See}, e.g., \textit{Kelly v. United States Steel Corp.}, 284 F.2d 850, 853 (1960) (stating that the concept of principal place of business may get artificial in some cases, like the one at bar, where the corporation had fourteen divisions of the parent corporation and eleven principal subordinate companies, in addition to the fact that company’s manufacturing activities were spread practically all over the U.S. and extended to foreign countries). In contrast, when dealing with a defunct corporation in a diversity case, the issue is not how to determine the principal place of business among a multitude of choices, but rather whether such a place actually exists. Therefore, since the inquiries are different, it is not imperative that the same rule apply in both situations.} The Second Circuit’s approach is most in accord with this principle because it reduces the frequency of finding diversity jurisdiction. By looking at the inactive corporation’s state of incorporation and its last principal place of business, corporations are more likely to be citizens of two different states. This increases the probability that complete diversity will not exist between the parties to a suit.

In contrast, the Third Circuit approach expands the probability that diversity jurisdiction will be found. By looking only at an inactive corporation’s state of incorporation, the Third
Circuit precludes a corporation's citizenship in the state of its principal place of business if it is different from the state of incorporation. Thus, the likelihood that the parties will be diverse is increased because the corporation is only a citizen of one state.

The Fifth Circuit approach restricts jurisdiction more than that of the Third Circuit because it allows an inactive corporation's last principal place of business to be considered when the corporation has been inactive for an insignificant period of time. Nevertheless, it still does not foreclose as many possibilities as the Second Circuit.

B. Plain Meaning Analysis

The Second Circuit approach is also supported by a plain meaning interpretation of the statute. First, 28 U.S.C § 1332(c) expressly states that a corporation is a citizen of both its state of incorporation and its principal place of business. The clear majority of district courts, which utilizes a plain meaning rationale, agrees that the use of the conjunction "and" implies that Congress intended for both of the requirements of the statute to be fulfilled before diversity jurisdiction will attach.\(^\text{147}\) As such, any conclusion that an inactive corporation has no principal place of business ignores a key element which is a prerequisite to diversity jurisdiction.\(^\text{143}\) Second, when Congress used the conjunction "and," it could not have meant that a corporation's citizenship would be based on its state of


\(^{143}\) Comtec, 711 F. Supp. at 525.
incorporation or its principal place of business.\textsuperscript{149} If Congress intended such a result, it would have expressly used the word "or" and not the word "and" in the statute.\textsuperscript{150}

Thus, the statute contains the implicit assumption that all corporations have a principal place of business.\textsuperscript{151} Moreover, since there is nothing in Section 1332 to suggest that a corporation's principal place of business should be ignored once that corporation becomes inactive, a plain reading of the statute requires a court to utilize the corporation's last principal place of business in determining its citizenship.\textsuperscript{152} The Second Circuit approach is the only view consistent with these conclusions because the Second Circuit demands that an inactive corporation's last principal place of business always be determinative of its citizenship. This, of course, implies that all corporations must have a principal place of business for diversity purposes.

The Third Circuit rejects the plain meaning interpretation by arguing that Congress' use of the conjunction "and" does not signify that it intended for the courts to strain to locate a principal place of business when no such place exists.\textsuperscript{153} The Third Circuit stresses that Congress provided that a corporation should be deemed a citizen of the state in which it has its principal place of business. Thus, if Congress truly wanted an inactive corporation's last principal place of business to be determinative of its citizenship, the Third Circuit argues, it could have easily done so by providing that a corporation be deemed a citizen of the state where it "has or has had" its principal place of business.\textsuperscript{154}

Nevertheless, the Second Circuit view still prevails because Congress clearly worded the statute to require consideration of the state of incorporation and the principal place of business. By using the word "and," as opposed to "or," there was no need for Congress to include the words "has had" to the

\textsuperscript{149} Allendale, 818 F. Supp. at 1305.

\textsuperscript{150} Id.


\textsuperscript{152} Allendale, 818 F. Supp. at 1305.


\textsuperscript{154} Id.
statute. Furthermore, the Second Circuit approach does not require a court to strain to find a principal place of business, as the Third Circuit contends, because the inactive corporation's last principal place of business can easily be ascertained by use of traditional tests used for active corporations.\textsuperscript{155} The Second Circuit approach does not attempt to find a principal place of business based on the current activities of the corporation, but rather on factors present when the corporation was active.

In addition, although the Fifth Circuit did not address the use of the word "and," its position is inconsistent with the plain meaning interpretation. This is so because the Fifth Circuit interpretation allows for the last principal place of business to be ignored when the corporation has been inactive for a substantial period of time, thus allowing for one of the required elements to be overlooked.

C. Legislative History Analysis

The Second Circuit approach is also most in accord with the legislative history supporting the 1958 amendment which added a consideration of the principal place of business to 28 U.S.C. § 1332. Congress' intent in adding the principal place of business requirement was to preclude federal courts sitting in diversity from hearing actions between corporations that are local in nature.\textsuperscript{156}

In essence, Congress did not want federal jurisdiction invoked in localities where corporations had local ties.\textsuperscript{157} This is because diversity jurisdiction was created to allow foreign litigants to avoid local prejudice in state courts by providing them with a neutral federal forum.\textsuperscript{158} However, because there is no threat of prejudice or favoritism when a corporation has its principal place of business in the same state in which its adversary is a citizen, the protection of a federal forum is unnecessary.\textsuperscript{159} Consequently, an inactive corporation, by virtue

\textsuperscript{155} See supra pp. 673-74.
\textsuperscript{157} China Basin Properties, Ltd. v. One Pass, Inc., 812 F. Supp. 1038, 1040 (N.D. Cal. 1993); see supra pp. 666-71 for discussion of legislative history.
\textsuperscript{159} Interpetrol Bermuda, Ltd. v. Rosenwasser, No. 86 Civ. 5631, 1987 WL 7734,
of having engaged in its business operations in a state which was its last principal place of business, has established a connection with the state and, therefore, is not subject to the risks of being an "alien" in the state.\textsuperscript{160}

Moreover, the same reasoning applies even if a corporation has been inactive in a state for a long period of time. While the corporation was active it received the benefits of conducting business in the state. Therefore, the corporation should not be able to escape scrutiny for acts which took place while it was active in the state. Furthermore, such a corporation is unlikely to face greater prejudice merely because it has been inactive in the state for a long period of time. A small local corporation which conducted business mainly within the state will still be considered "local" once it becomes inactive. Such a corporation is not a foreign or alien company and, therefore, does not require the protection of diversity jurisdiction. Similarly, the bias against a large interstate corporation is unlikely to increase merely because the corporation has been inactive in the forum state for a long period of time. This is because the prejudice against corporations is often unrelated to their "foreignness" but, rather, is caused by their economic "bigness."\textsuperscript{161}

The Second Circuit approach is most consistent with the legislative history because it requires courts always to look at the inactive corporation's last principal place of business to determine its citizenship for diversity purposes. In this way, local corporations are precluded from suing or being sued in federal court based solely on their states of incorporation. This is precisely the type of situation Congress was trying to prevent when it amended Section 1332.\textsuperscript{162}

The Third Circuit has acknowledged that its approach may subvert Congress' intent in amending Section 1332,\textsuperscript{163} but it

\textsuperscript{160} China Basin Properties, Ltd. v. Allendale Mut. Ins. Co., 818 F. Supp. 1301, 1304 (N.D. Cal. 1992); see One Pass, 812 F. Supp. at 1040 ("[A] corporation, which, when active, had its principal place of business in California, is unlikely to suffer local prejudice in California state courts. Thus, the policy behind the creation of diversity jurisdiction does not apply in this case.").

\textsuperscript{161} See WRIGHT ET AL., supra note 6, § 3624.

\textsuperscript{162} See S. REP. NO. 1830, supra note 13, at 3101-02; 104 CONG. REC. 12,683-85 (1958).

stated that the certainty and clarity which are obtained from its "bright line" test outweigh the harm identified by the Second Circuit in *Passalacqua*.\(^{164}\) The Third Circuit's reasoning, however, fails to consider that the Second Circuit approach also creates a "bright line" test because it always considers the inactive corporation's state of incorporation and its last principal place of business. Thus, since the Second Circuit's approach is both consistent with the legislative history and provides certainty and clarity, it is the more useful approach.

The Fifth Circuit chose to adopt a more flexible approach based on its belief that the Second Circuit approach has the potential to find an inactive corporation's principal place of business to be a state where it would never have found it to be when it was active.\(^{165}\) The Fifth Circuit rationale is premised on its interpretation of the Second Circuit's holding in *Passalacqua* that the place where a corporation was "last active" is determinative of its citizenship.\(^{165}\) Thus, according to the Fifth Circuit's reasoning, the Second Circuit approach deems an inactive corporation a citizen of a state where it merely transacted its last business activity, regardless of whether, prior to the corporation becoming inactive, it engaged in enough corporate activity in that state to make that state the corporation's principal place of business.

This conclusion is inconsistent with a more faithful reading of the Second Circuit's holding in *Passalacqua*. First, the "last active" language to which the Fifth Circuit refers immediately follows the Second Circuit's enunciation in *Passalacqua* of the rule that a court should consider both the state of incorporation and the principal place of business in deciding whether diversity jurisdiction is present.\(^{167}\) This illustrates that when the Second Circuit referred to the place where the corporation was last active or last transacted business, it was referring to the corporation's last principal place of business and not merely the place where it last transacted any business activity.

\(^{164}\) Id.

\(^{165}\) Harris v. Black Clawson Co., 961 F.2d 547, 551 (5th Cir. 1992).

\(^{166}\) Id. (discussing Wm. Passalacqua Builders, Inc. v. Resnick Developers South, Inc., 933 F.2d 131, 141 (2d Cir. 1991)).

\(^{167}\) *Passalacqua*, 933 F.2d at 141.
Second, the Fifth Circuit ignores the Passalacqua language describing the rationale for the court’s holding. Passalacqua stated that if courts were to allow inactive corporations to avoid inquiry into where they were last active, then a defunct corporation, no matter how local in character, could remove a case to federal court based on its state of incorporation.\textsuperscript{168} The Second Circuit concern centers on local corporations being able to sue or be sued in federal court. Thus, it is unlikely that a corporation whose activities were insufficient to make a state the corporation’s principal place of business while it was active, would be deemed a “local” corporation by the Second Circuit. Consequently, since the Second Circuit is concerned about local corporations, it could not have meant that any place where a corporation last transacted business would be its principal place of business.

Third, the Fifth Circuit ignores the fact that the Second Circuit held that Passalacqua was a citizen of Florida because there was evidence supporting the conclusion that Florida was Passalacqua’s last principal place of business when it was active.\textsuperscript{169} This supports the assertion, contrary to the Fifth Circuit’s belief, that the Second Circuit will deem an inactive corporation a citizen of the state which was its last principal place of business, and not a citizen of any place where it last transacted any business.

The Second Circuit approach is also consistent with the second goal of the 1958 amendment which was to ease the workload of the federal courts sitting in diversity.\textsuperscript{170} By applying a rule that an inactive corporation is always a citizen of its state of incorporation and its last principal place of business, the Second Circuit is increasing the odds that two parties will not be completely diverse from one another. This reduces the possibility of diversity jurisdiction being found, and thereby reduces the workload of the federal courts. In contrast, the Third Circuit test allows for greater diversity jurisdiction because it only looks at the state of incorporation. This increases the chances that a corporation will be diverse from other par-

\textsuperscript{168} Id.
\textsuperscript{169} Id.
\textsuperscript{170} See generally S. REP. NO. 1830, supra note 13; see also WRIGHT ET AL., supra note 6, § 3624.
ties in the litigation. Similarly, the Fifth Circuit test only allows for the last principal place of business to be used if the corporation has been inactive for an insubstantial period of time, and even in such cases the last principal place of business is not dispositive of citizenship, but is only a relevant factor to be considered.

CONCLUSION

Diversity jurisdiction continues to be a volatile topic in the legal community. Most of the debate centers around the continued viability of such jurisdiction in the modern era. More specifically, diversity jurisdiction ties up the resources of the federal system when federal courts must hear cases involving essentially local entities. Diversity cases involving inactive corporations litigating in states where they were formerly active is a typical example of this situation.

In order to preserve the integrity of diversity jurisdiction, courts should attempt to limit the scope of its applicability to situations where its protections are essential for the proper administration of justice. Thus, as the Second Circuit has reasoned, an inactive corporation's last principal place of business should always be determinative of its citizenship for diversity purposes. Such a corporation should not avoid scrutiny, nor should it be precluded from seeking judicial relief, in the court of the state where it conducted significant activities while it was active. Moreover, the Second Circuit's approach of using both the inactive corporation's state of incorporation and its last principal place of business to determine citizenship for

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171 See, e.g., Braverman, supra note 2, at 1084 n.56 ("there is simply no analogy between today's situation and that existing in 1789" when there was a real need for diversity jurisdiction) (citing HENRY J. FRIENDLY, FEDERAL JURISDICTION: A GENERAL VIEW 141 (1973)). One suggestion for revising the current diversity requirements is to limit the applicability of diversity jurisdiction to complex multi-state litigation, interpleader actions and suits involving aliens. See JUDICIAL CONFERENCE OF THE U.S., supra note 2, at 38-42. More modest changes include: (i) prohibiting plaintiffs from invoking diversity jurisdiction in their home states; (ii) deeming corporations to be citizens of every state in which they are licensed to do business; (iii) excluding attorney's fees, punitive damages and damages for pain and suffering from the amount in controversy; and (iv) raising the jurisdictional amount to $75,000. See JUDICIAL CONFERENCE OF THE U.S., supra note 2, at 38-42.

172 See, e.g., S. REP. NO. 1830, supra note 13, at 3101-02, 3111-12.
diversity purposes best comports with the plain meaning of 28 U.S.C. § 1332, with the legislative history of the constitutional grant of diversity jurisdiction and with the goals and purposes of the 1958 amendment to Section 1332.

Dawn Levy