

# CLIENT ALERT

March 8, 2016

## Supreme Court Severely Restricts Federal-Court Access for Non-Corporate Entities, Including Certain REITs and RICs

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### SPEED READ

The Supreme Court on Monday severely restricted federal-court access for business trusts, including many REITs, in *Americold Realty Trust v. Conagra Foods*. Under *Americold*, business trusts are now citizens for diversity-jurisdiction purposes of every state of which at least one of their shareholders is a citizen. For business trusts with wide shareholder bases, this ruling significantly curtails the ability to invoke diversity jurisdiction to get into federal court except in certain class actions. Business trusts involved in federal-court litigation should immediately assess whether the *Americold* decision affects the jurisdiction of the court to continue to hear their cases. Business trusts should also consider whether the benefits of increased federal-court access justify converting from a trust to a corporation.

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Business trusts, statutory trusts and non-corporate real-estate investment trusts now face a significant jurisdictional barrier that will reduce their access to the federal courts, following a March 7 ruling by the U.S. Supreme Court. The decision, *Americold Realty Trust v. Conagra Foods, Inc.*, held that entities organized as Maryland non-corporate "real estate investment trusts" are citizens, for diversity-jurisdiction purposes, of every state of which at least one of their shareholders is a citizen. The *Americold* decision rejected the position taken by many U.S. Courts of Appeals, which had held that business trusts were citizens only of the states of which their *trustees* were citizens, and that the citizenship of the shareholders was irrelevant. Although the ruling arose in the context of a real estate investment trust, the Court's reasoning also appears to apply to registered investment companies organized as Delaware statutory trusts, Massachusetts business trusts, and similar state law trusts. (Congress has adopted a specific statutory exception for entities formed as corporations limiting corporate citizenship to the state of incorporation and the state in which the firm's principal place of business is located.)

As a practical matter, lawsuits are heard in federal court on one of two bases. Either the suit involves federal law (for example, the federal securities laws) or the parties to the suit are "diverse," meaning they are citizens of different states. Diversity jurisdiction allows the federal courts to hear lawsuits that arise under state law, so long as no plaintiff and defendant have overlapping state citizenship.

Because the law requires "complete diversity," except for certain class actions, if even one of the trust's shareholders has the same state citizenship as any one of the adverse parties, a state-law suit by or against the trust cannot proceed in federal court on diversity grounds. It is common for business organizations to employ diversity jurisdiction to have legal disputes resolved in the federal court system. For business trusts with wide shareholder bases (including non-corporate publicly traded real estate investment trusts), the *Americold* ruling significantly curtails the ability to invoke diversity jurisdiction to get into federal court—either as a plaintiff or as a defendant removing a case from state court.

This has always been true for partnerships, limited partnerships and labor unions. After *Americold*, it is now true for business trusts, statutory trusts, and non-corporate real estate investment trusts. And while the Supreme Court has never addressed this question in the context of LLCs, the Supreme Court's broad and unanimous holding in *Americold* makes it likely that LLCs too will be subject to this rule, as a number of U.S. Courts of Appeals already have held.

Entities organized as trusts under state law that are involved in active federal court litigation should immediately examine whether the *Americold* decision affects the jurisdiction of the court to continue to hear their cases. Because the Supreme Court's decision affects the subject-matter jurisdiction of federal courts, a jurisdictional challenge on this basis cannot be waived and may be raised by either party at any time during the litigation. Indeed, the issue arose in the *Americold* case when the appellate court held it lacked jurisdiction, even though all parties wanted the court to find jurisdiction and hear the case.

The Supreme Court's decision also affects the choice of a corporate versus a non-corporate form. Entities organized as trusts under state law—particularly federally tax-qualified REITs organized as non-corporate real estate investment trusts under Maryland law—should consider whether the benefits of increased federal-court access outweigh other considerations and justify a shift to the corporate form.

*Goodwin Procter* was co-counsel to the National Association of Real Estate Investment Trusts as amicus curiae in the Supreme Court case. Watch for an invitation to an upcoming Goodwin Procter webinar addressing important litigation and business-structure issues arising from the *Americold* decision.

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