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LIMITATION OF DIVERSITY JURISDICTION IN CASES AFFECTING FOREIGN CORPORATIONS

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LIMITATION OF DIVERSITY JURISDICTION IN CASES AFFECTING FOREIGN CORPORATIONS — On February 29, 1932, President Hoover sent to the Senate and House of Representatives a message recommending that the jurisdiction of federal courts based on diversity of citizenship be modified by "providing that where a corporation, organized under the laws of one State, carries on business in another State it shall be treated as a citizen of the State wherein it carries on business as respects suits brought within that State between it and the residents thereof arising out of the business carried on in such State." [1]

On December 9, 1931, Senator Norris had introduced a bill which merely added to the first paragraph of 28 U. S. C. A., sec. 41 (Judicial Code, sec. 24) the proviso that "where a corporation organized under the laws of one or more states or under the laws of one or more foreign countries, carries on business in a state other than one wherein it has been organized, it shall for the purposes of jurisdiction in a district court of the United States be treated as a citizen of such state wherein it carries on business as respects all suits brought within that state between itself and residents thereof and arising out of the business carried on in such state." [2] This last bill had, therefore, anticipated

[1] 75 Cong. Rec. 5047 (1932). A number of bills limiting and restricting either the power or the jurisdiction of the district courts were already pending in Congress, those attracting widest public attention being, of course, the bills introduced in the House and Senate by Representative LaGuardia (H. R. 5315, 75 Cong. Rec. 333 (1931)) and by Senator Norris (S. B. 935, 75 Cong. Rec. 3455 (1932)) respectively, declaring the public policy of the United States with respect to labor organizations and restricting the power of the courts to issue restraining orders and temporary or permanent injunctions in cases growing out of labor disputes; those limiting or taking away the power of district courts and circuit courts of appeals to restrain or enjoin the enforcement of orders of state administrative boards (H. R. 336, 75 Cong. Rec. 89 (1931); H. R. 90, 75 Cong. Rec. 83 (1931); H. R. 345, 75 Cong. Rec. 90 (1931); S. B. 3243, 75 Cong. Rec. 2691 (1932)), and those taking away jurisdiction of suits relating solely to intrastate business brought by or against public utilities and based solely on diversity of citizenship or the Constitution, laws or treaties of the United States (S. B. 3085, 75 Cong. Rec. 2191 (1932)). Of lesser popular appeal was the bill introduced by Senator Norris on December 9, 1931, amending the first paragraph of 28 U. S. C. A., sec. 41 (Judicial Code, sec. 24) by eliminating entirely jurisdiction based on diversity, except as between citizens of a state and internationally foreign states, citizens or subjects (S. B. 939, 75 Cong. Rec. 196 (1931)).

[2] S. B. 937, 75 Cong. Rec. 196 (1931). Closely related to the Norris proviso in that it aims to correct a situation which has always furnished an impressive argument for the opponents of jurisdiction based on diversity is the Dyer bill (H. R. 8904, 75 Cong. Rec. 3509 (1932)), introduced in the House on February 5, 1932.

the President's recommendation — in fact it went a little farther in including corporations of foreign countries.

It will be noted that neither the President's recommendation nor the Norris proviso affects jurisdiction,

(1) of suits between a foreign corporation *not* doing business in a state, and a resident of such state;
(2) of suits between a foreign corporation doing business in a state, and a citizen of another state;
(3) of suits between a foreign corporation doing business in a state, and a corporation organized under the laws of some state other than that of the first corporation;
(4) of suits between a foreign corporation doing business in a state, and residents of that state, arising out of business *not* carried on in that state, i.e., carried on in some other state or country.

Needless to say, we are dealing here only with questions of jurisdiction, and not of venue.[3]

To the complete elimination of jurisdiction based on diversity of citizenship — an object which Senator Norris sought to accomplish by S. B. 939 — the President expressed himself as being opposed. Without stating what the reasons which induced the constitutional grant of judicial power in controversies between citizens of different states were, he said those reasons still existed. It was only to these special cases involving corporations of other states — cases which court decisions had brought within the scope of the diversity jurisdiction conferred by statute — that his recommendation was directed; these cases, as he conceived it, did not fall within the real purpose and spirit of the constitutional grant.

This bill very deftly disposes of the decision in Swift v. Tyson, 16 Pet. (41 U. S.) 1 (1842), to the effect that questions of "general commercial law" are not controlled by the provision that "the laws of the several states" shall be regarded as rules of decision in the federal courts. The bill accomplishes this result by changing the word "laws" to "law," and the word "rules" to "rule," and by inserting "the" before "rule," in the Rules of Decision Act (28 U. S. C. A., sec. 725).

[3] The extent to which the recommendation and the Norris proviso will affect the General Removal Act should, however, be considered. The first sentence of the General Removal Act (28 U. S. C. A., sec. 71) relates to cases arising under the Constitution, laws or treaties of the United States; obviously, the right of foreign corporation defendants to remove such cases remains as before. The second sentence relates to the removal of "any other suit of a civil nature, at law or in equity, of which the District Courts of the United States are given jurisdiction by this title"; jurisdiction having been deleted in the cases described in the Norris proviso there can, of course, be no removal in such cases. The third sentence relates to the removal of separable controversies, and judicial interpretation has limited it to controversies within the original jurisdiction (Salem Trust Co. v. Manufacturers' Finance Co., 264 U. S. 182, 44 Sup. Ct. 266 (1923)); such controversies falling within the terms of

This, of course, suggests an inquiry into the reasons that influenced the framers of the Constitution in extending the judicial power of the United States to controversies between citizens of different states. The general impression is that the grant of judicial power in these controversies was induced by apprehensions of local prejudice; but scholarly research has indicated that it was due in larger measure to the fear of state legislation, either past or future, weakening the power of the local courts, or embarrassing the execution of their judgments by stay laws and tender acts.[4] Possibly both reasons influenced the fathers of the Constitution.

More important is the question whether those reasons still exist. Distinguished writers have called attention to the fact that no other English speaking union has a scheme of federal courts. Judge Clark speaks of the "unreality of taking a case away from the state court on the theory that the court and jury are prejudiced, because they are not citizens of the same state as a corporation which happens to have been incorporated in another state."[5] He quotes opinions of judges of the High Court of Australia to the effect that the grant of power in the Commonwealth of Australia Constitution Act to create courts and to define their jurisdiction in matters between residents of different states was "a piece of pedantic imitation of the Constitution of the United States, and absurd in the circumstances of Australia, with its state courts of high character and impartiality" and that the

the Norris proviso would, therefore, no longer be removable. Likewise, judicial interpretation has limited the fourth sentence which related to removal on the ground of prejudice or local influence, to suits within the original jurisdiction (Cochran v. Montgomery County, 199 U. S. 260, 26 Sup. Ct. 58 (1904)); the right of removal on the ground of prejudice or local influence is, therefore, withdrawn in the cases falling within the Norris proviso.

The result is that the Norris proviso, if passed, will relegate to historical interest the long controversy over the power of states to require of foreign corporations, as a condition to their admission to do business in a state, an agreement not to remove suits against them to the federal courts. Such a statute was held unconstitutional, and the agreement based upon it void, in Home Insurance Co. v. Morse, 20 Wall. 45. The case was decided by a divided court, and in Doyle v. Continental Insurance Co., 94 U. S. 535 (1876), the court recoiled before the full consequences of its decision and set aside an injunction restraining the enforcement of a state statute which required the Secretary of State to cancel a license to do business because of removal of a suit to a federal court. To the same effect was the holding in Prewitt v. Security Mutual Life Insurance Co., 202 U. S. 246 (1905). Finally, in Terral v. Burke Construction Co., 257 U. S. 529 (1921), the Supreme Court reaffirmed its position in the Home Insurance Co. case, and overruled the other cases.

[4] See FRANKFURTER AND LANDIS, THE BUSINESS OF THE SUPREME COURT, ch. I (1928); Friendly, "The Historic Basis of Diversity Jurisdiction," 41 HARV. L. REV. 483 (1928).

[5] United States v. Mayor and Council of the City of Hoboken, N. J. et al., 29 F.(2d) 932, 937 (1929).

fear of local influence prejudicial to nonresidents seeking redress in the local courts was "little grounded in point of fact in Australia." The British North America Act,[6] while conferring upon the Parliament of Canada the right to provide for "the Constitution, Maintenance, and Organization of a General Court of Appeal for Canada, and for the Establishment of any additional Courts for the better Administration of the laws of Canada,"[7] left to the provinces the administration of justice therein and the constitution, maintenance and organization of provincial courts.[8] It was not until 1875 that the Supreme Court of Canada was established. It now has appellate jurisdiction in civil and criminal causes over the highest court of final resort of the respective provinces.[9] The organic act provided, however, that the Governor General should appoint the judges of the superior, district, and county courts in each province.[10] Likewise the Union of South Africa Act provides for a Supreme Court of South Africa, but makes the supreme and district courts of the provinces provincial and local divisions of the Supreme Court.[11]

The instances of these unions of British possessions are, however, hardly apropos. None of them is a federal union, as we understand the term. No violent rupture of the ties which bound them to a common authority preceded the act of union. None of the component provinces, with the exception of the Transvaal and the Orange Free State, ever claimed to be a sovereign state. The inhabitants were, and remained, subjects of the Crown, and the organic legislation was enacted by the Sovereign "by and with the Advice and Consent of the Lords Spiritual and Temporal, and Commons, in Parliament assembled."

On the other hand, our political history had a different origin and was marked by other developments — the revolution, the Virginia and Kentucky resolutions, the Hartford Convention, nullification ordinances, the controversy over state rights and the Civil War. It is true that local prejudices are rapidly disappearing — history, however, remains, and the beginnings and development of our own history make "pedantic imitation" difficult, if not unprofitable.

The principal reason, as disclosed by historical investigation, for the insertion of the diversity clause in the Constitution — namely, the fear that as a result of hampering legislation state courts would be less vigorous and independent in the administration of justice —

[6] 30 & 31 Vict., c. 3 (1867).
[7] 30 & 31 Vict., c. 3, sec. 101 (1867).
[8] 30 & 31 Vict., c. 3, sec. 92, cl. 14 (1867).
[9] Can. Rev. Stat., 1927, c. 35, sec. 36.
[10] 30 & 31 Vict., c. 3, sec. 96 (1867).
[11] 9 Edw. VII, c. 9 (1909).

still exists. This explains the continued opposition of the American Bar Association to all legislation radically limiting the jurisdiction of the federal courts, or diminishing their power.[12] This fear comes from such legislation as that limiting the terms of state judges, making them subject to popular election, prohibiting comment on evidence,[13] allowing verdicts to be returned by less than the entire jury, the requirement of submission to the jury of issues of fact which are supported by only a scintilla of evidence,[14] requiring that certain issues, such as contributory negligence, be submitted to the jury,[15] making damage presumptive evidence of negligence,[16] forbidding appellate courts to declare a statute unconstitutional except on the judgment of more than a majority of the bench, and hampering by stay laws and tender acts the execution of judgments.[17]

Social and economic forces have not yet been effective in producing similar legislation in the provinces or states of the British unions. In our case, however, the war which separated the colonies from the British Crown was not merely a civil war — it was also a revolution, and its effects have continued. This, it is submitted, explains to some extent the frequent attacks upon the judiciary, both state and federal, which have marked our history — phenomena which rarely appear in the records of British possessions.

With an influential senator, as its sponsor, and with the President's recommendation behind it, the Norris proviso appears likely to pass. Thus, that *injuria temporum*, the holding in *Louisville, Cincinnati & Charleston R. Co. v. Letson*,[18] that a corporation, for the purposes of jurisdiction, is a citizen of the state of its creation, after reaching its climactic development in *Black & White Taxi Co. v. Brown & Yellow Taxi Co.*,[19] seems destined for demise in the near future.

[12] See letter of Paul Howland, chairman, Committee on Jurisprudence and Law Reform, American Bar Association, to Hon. Charles Curtis, 75 Cong. Rec., 5060 (1932).

[13] E.g., Georgia Code, forbidding judges expressing any opinion on matters of fact, held not binding on federal courts. Vicksburg & Meridian R. Co., 118 U. S. 545, 7 Sup. Ct. 1 (1885).

[14] E.g., in Ohio, Giddens v. Cleveland Ry. Co., 37 Ohio App. 8 (1931), but not followed in federal courts; see Baltimore & Ohio R. Co. v. Groeger, Admx., 266 U. S. 521, 45 Sup. Ct. 169 (1924); Western and Atlantic R. Co. v. Hughes, Admx., 278 U. S. 496, 49 Sup. Ct. 231 (1928).

[15] E.g., Const. Arizona, declared not binding on federal courts in Herron v. Southern Pacific Co., 283 U. S. 91, 51 Sup. Ct. 383 (1931).

[16] E.g., Ga. Civ. Code, sec. 2780, declared unconstitutional in Western & Atlantic R. Co. v. Henderson, 279 U. S. 639, 49 Sup. Ct. 445 (1928).

[17] E.g., Kentucky stay and tender laws, held not binding on federal courts, Wayman et al. v. Southard et al., 10 Wheat. (23 U. S.) 1 (1883).

[18] 2 How. (43 U. S.) 497 (1884).

[19] 276 U. S. 518, 48 Sup. Ct. 404 (1927).

Important as this result will be in the field of federal jurisdiction, it has an even greater significance in the realm of corporation law, for it marks another advance for the school of corporation realists as against their adversaries, the mystics, and a further diminution of the already waning influence of the *Dartmouth College* case.[20]

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[20] 4 Wheat. (15 U. S.) 518 (1818). The long career of the Letson case (it was decided in 1844) parallels that of another famous case, Osborn v. Bank of the United States, 9 Wheat. (22 U. S.) 738 (1884), in which Chief Justice Marshall held that a suit by a corporation created by an act of Congress is a case arising under a law of the United States. The Pacific Removal Cases, 115 U. S. 1 at 26, 5 Sup. Ct. 1113 (1884), extended the doctrine to all suits brought by or against such corporations — and Congress thereupon began the shearing process. By the Act of July 12, 1882 (22 Stat. 162, 163, sec. 4), national banks were denied the privilege of removal on the ground of federal incorporation. The Act of August 13, 1888 (25 Stat. 436, sec. 4) declared that for the purpose of all actions by or against them they should be deemed citizens of the states in which they were located. The Act of January 28, 1915 (38 Stat. 804, sec. 5) provided that no court of the United States should have jurisdiction of any action or suit by or against any railroad company on the ground that it was incorporated by Act of Congress, and finally the Judiciary Act of 1925 (43 Stat. 936, 28 U. S. C. A., sec. 42) took away entirely federal incorporation as a ground of jurisdiction except in those cases in which the government owns a majority of the capital stock.