**UNITED STATES DISTRICT COURT**
**DISTRICT OF CONNECTICUT**

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| **TREASURER OF THE STATE OF CONNECTICUT** | : | |
| **v.** | : | **No. 3:02cv519 (JBA)** |
| **FORSTMANN LITTLE & CO., EQUITY PARTNERSHIP-VI, L.P., et al.** | : | |

**MEMORANDUM OF DECISION ON MOTION TO REMAND [Doc. # 13]**

## I. Introduction

The Treasurer of the State of Connecticut filed this action against Forstmann Little & Co. Equity Partnership-VI, L.P., Forstmann Little & Co. Subordinated Debt and Equity Management Buyout Partnership-VII, L.P., FLC XXXII Partnership, LP., FLC XXXIII Partnership, L.P., Fortsmann Little & Co., Theodore J. Forstmann, Sandra J. Horbach, Winston W. Hutchins, Steven B. Klinsky, Thomas H. Lister, Jamie C. Nicholls, and Gordon A. Holmes in Connecticut Superior Court, alleging that defendants placed millions of State pension funds in two improper investments, in disregard of defendants' own investment rules, and arranged for the value of those investments to be reduced in a pre-packaged bankruptcy, while protecting their own interests and those of other investors.

The Treasurer's claims are state law claims of breach of fiduciary duty, breach of contract, breach of the covenant of good faith and fair dealing, and breach of the Connecticut Uniform Securities Act. The complaint also asserts breach of fiduciary duty and contract claims on behalf of limited partnerships of which the Treasurer is a limited partner.

Defendants removed to federal court, invoking the Court's diversity jurisdiction. Plaintiff has moved to remand on the grounds that there is no diversity jurisdiction because she is not a citizen of Connecticut for purposes of the diversity statute, 28 U.S.C. § 1332, and the limited partners, Connecticut citizens, are properly joined as defendants. In addition, Plaintiff seeks an award of costs and expenses incurred as a result of defendants' removal. For the reasons set forth below, the motion to remand is GRANTED, and plaintiff's claim for costs and expenses is DENIED.

## II. Standard

A district court must remand a case "[i]f at any time before final judgment it appears that the district court lacks subject matter jurisdiction . . . ." 28 U.S.C. § 1447(c). The removing party bears the burden of proof in establishing its right to a federal forum. United Food & Commercial

Workers Union, Local 919, AFL-CIO v. CenterMark Properties Meriden Square, Inc., 30 F.3d 298, 301 (2d Cir. 1994); R.G. Barry Corp. v. Mushroom Makers, Inc., 612 F.2d 651, 655 (2d Cir. 1979). Where a defendant seeks to remove an action, it must support its asserted jurisdictional facts with "'competent proof' and 'justify its allegations by a preponderance of the evidence.'" United Food & Commercial Workers Union, 30 F.3d at 305 (quoting McNutt v. General Motors Acceptance Corp., 298 U.S. 178, 189 (1936)). "'In light of the congressional intent to restrict federal court jurisdiction, as well as the importance of preserving the independence of state governments, federal courts construe the removal statute narrowly, resolving any doubts against removability.'" Lupo v. Human Affairs Intern., Inc., 28 F.3d 269, 274 (2d Cir. 1994) (quoting Somlyo v. J. Lu-Rob Enters., Inc., 932 F.2d 1043, 1045-46 (2d Cir. 1991)).

## III. Discussion

The diversity statute, 28 U.S.C. § 1332, provides:

> The district courts shall have original jurisdiction of all civil actions where the matter in controversy exceeds the sum or value of $75,000, exclusive of interest and costs, and is between . . . citizens of different States . . . .

A state is not considered a citizen for purposes of diversity

jurisdiction. Moor v. County of Alameda, 411 U.S. 693, 717 (1973). By contrast, a political subdivision or entity of a state is a citizen of the state for diversity purposes "unless it is simply 'the arm or alter ego of the State.'" Moor, 411 U.S. at 717 (citing State Highway Comm'n of Wyoming v. Utah Constr. Co., 278 U.S. 194, 199 (1929)); accord Krisel v. Duran, 386 F.2d 179, 181 (2d Cir. 1967) (per curiam). Thus, diversity jurisdiction exists in this case only if the Treasurer, as trustee for the Connecticut Retirement Plans and Trust Funds, is an entity independent from and not an arm of the state of Connecticut.

The critical diversity determination, distinguishing between an independent entity and an 'arm or alter ego', asks whether or not "...the suit is, in effect, against the state...." State Highway Comm'n, 278 U.S. at 194; accord Krisel, 386 F.3d at 181 ("For the purpose of diversity jurisdiction, the determinative factor is whether the state is the real party in interest.").

A parallel and essentially equivalent inquiry extends a state's Eleventh Amendment sovereign immunity to entities considered alter egos or "arms of the state," but not to independent political subdivisions such as counties and municipal corporations. See Mt. Healthy City Sch. Dist. Bd.

of Educ. v. Doyle, 429 U.S. 274, 280 (1978).

Accordingly, for both diversity and immunity purposes, courts use the same criteria to evaluate whether an entity is an arm of the state or rather an independent political subdivision. See id. at 280-81 (citing and applying in an immunity analysis the criteria used in a diversity case, Moor, 411 U.S. at 717-721); Regents of the Univ. of California v. Doe, 519 U.S. 425, 430 n. 5 (1997)("We relied in Mt. Healthy on our earlier decision [Moor] that a California county is not an 'arm of the State' and therefore may be considered a 'citizen' of California for the purpose of determining the federal court's diversity jurisdiction over a state law claim."); Univ. of Rhode Island v. A.W. Chesterton Co., 2 F.3d 1200, 1203 (1st Cir. 1993)("Several ancillary principles derive from Moor. The criteria are substantially similar for evaluating whether an entity is a citizen of the State for diversity purposes, or a State for Eleventh Amendment sovereign immunity purposes...").[1]

[1] The two tests diverge in that, once an entity qualifies as an arm of the state, the diversity inquiry ends whereas the sovereign immunity analysis moves to the next question, namely, whether the state or its arm has waived its immunity. See State Highway Comm'n, 278 U.S. at 199-200 ("No consent by the state to submit itself to suit could affect the question of diverse citizenship."); Mt. Healthy, 429 U.S. at 280 ("We prefer to address instead the question of whether such an entity had any Eleventh Amendment immunity in the first place, since if we conclude that it had none it will be unnecessary to reach the question of waiver."); Krisel, 386 F.2d at 181; Rhode Island, 2 F.3d at 1202 n.4.

Whether a state agency is independent or an arm of the state is a question of federal law, see Regents, 519 U.S. at 429 n.5, that, for resolution, requires analysis of state law provisions defining the agency's character. See Regents, 519 U.S. at 429 n.5; Moor, 411 U.S. at 718-20; Mt. Healthy, 429 U.S. at 280-81. The seminal Supreme Court case addressing the question in the diversity context, Moor v. County of Alameda, did not enumerate an explicit list of criteria to be used in making the determination. However, the discussion in Moor counsels lower courts to consider whether, under state law, the entity in question:

> (1) is incorporated or has corporate powers; (2) may sue or be sued in its corporate capacity; (3) is liable for judgments against it and, to pay such judgments (or otherwise fund its operations), is authorized to raise funds (e.g. by levying taxes or issuing bonds) independent of or not appropriated from the State treasury; (4) may sell, hold, or otherwise deal in property; (5) may enter contracts in its own name; (6) may perform traditional and essential government functions (e.g. provision of water service, flood control, rubbish disposal etc.);[2] (7) exercises autonomy over internal operations (e.g. by, in the case of a county, generating revenue to provide a variety of public services); and (8) has been determined to have independent corporate character by the state's Supreme

[2] The Court notes also that, contrary to defendants' contention, "a state may, in its own name or through an alter ego, carry on activities which are traditionally regarded as proprietary functions but neither the state nor its alter ego thereby becomes a citizen for the purpose of diversity jurisdiction." Krisel, 386 F.2d at 181. Although the rationale for the Second Circuit's statement in Krisel is not clear, it appears to implicate the performance of proprietary functions as a relevant factor under the waiver prong of an immunity analysis, a prong not part of a diversity analysis.

Court (or presumably other court) decisions.

See Moor, 411 U.S. at 717-721; cf. Rhode Island, 2 F.3d at 1205-1217.

Analogously, a recent Second Circuit decision from the immunity context requires a district court to make an evaluation of six factors when determining whether an entity is an arm of the state:

> (1) how the entity is referred to in its documents of origin; (2) how the governing members of the entity are appointed; (3) how the entity is funded; (4) whether the entity's function is traditionally one of local or state government; (5) whether the state has veto power over the entity's actions; and (6) whether the entity's financial obligations are binding upon the state.

McGinty v. New York, 251 F.3d 84, 95-96 (2d Cir. 2001) (citing Mancuso v. New York Thruway Ass'n, 86 F.3d 289, 293 (2d Cir. 1996)).[3]

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[3] McGinty then instructs,

> "If these factors point in one direction, the inquiry is complete. If not, a court must ask whether a suit against the entity in federal court would threaten the integrity of the state and expose its treasury to risk...If the answer is still in doubt, a concern for the state fisc will control." McGinty, 251 F.3d at 96 (citation omitted).

McGinty's step two inquiry into the potential threat posed to the state's fisc by the case at issue will, of course, be irrelevant where, as here, the state-related entity is a plaintiff and seeks to recover a monetary judgment. This reality illustrates another difference that may obtain between the immunity context, in which the state-related entity asserting arm or alter ego status will always be a defendant (and therefore a judgment against it could drain the state treasury), and the diversity context, in which the state-related entity, as here, will sometimes be a plaintiff. However, notwithstanding whether the specific case prompting the analysis poses a threat to the state's treasury, both Moor and factor (6) in the first step of the McGinty inquiry teach that, in both the diversity and immunity context, an

Plaintiff argues that the State of Connecticut is the real party in interest because neither she nor the Connecticut Retirement Plans and Trust Funds ("CRPTF"), for which she is trustee, are independent of the state. The Treasurer further notes that she herself is a constitutionally elected state officer and not financially independent of the state. Assessing the factors directed by Moor and McGinty, the Court concludes that the plaintiff Treasurer does not act autonomously from but rather is an arm of the State of Connecticut.

In Fitzpatrick v. Bitzer, 519 F.2d 559 (2d Cir. 1975), aff'd in part, rev'd in part on other grounds, 427 U.S. 445 (1976), the Second Circuit held that the Connecticut State Employees Retirement System was the alter ego of the state and therefore entitled to the state's sovereign immunity under the Eleventh Amendment. As noted in that analysis, the Connecticut State Employees Retirement Fund (one of the component funds of the CRPTF) "has none of the indicia of independence from the state, such as separate incorporation or a power to sue in its own name. It is controlled by the state

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evaluation of whether a state related entity is independent from or rather an arm of the state must consider generally the state's liability for the entity's financial obligations. See Moor, 411 U.S. at 719-720; McGinty, 251 F.3d at 96 and 99-100; Rhode Island, 2 F.3d at 1202 n.4.

treasurer, see Conn. Gen Stat. § 5-156. Although the money in it may be used only for a designated purpose, it nonetheless remains 'public money.'" Fitzpatrick, 519 F.2d at 565.[4]

The office of Treasurer is established by the Connecticut State Constitution, see Conn. Const. art. IV §§ 1 and 22, and the Treasurer herself is an elected state official. See id. and Conn. Gen. Stat. 3-11 et seq. She administers and holds the CRPTF funds as part of her statutory duties, and she is required to "invest as much of the state's trust funds as are not required for current disbursements in accordance with the provisions of section 45a-203 or the provisions of this part." Conn. Gen. Stat. § 3-13d(a). The Treasurer administers the CRPTF with the advice of the Investment Advisory Council, a statutorily created body consisting of the Secretary of the Office of Policy and Management, the Treasurer, and five public members appointed by the Governor, the president pro tempore of the Senate, the Senate minority leader, the speaker of the House of Representatives and the minority leader of the

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[4] Conn. Gen. Stat. § 5-156(a) and (b) provide in pertinent part,

"(a) All member contributions and state appropriations shall be held in a separate retirement fund by the Treasurer, who may invest and reinvest as much of the fund as is not required for current disbursements in accordance with the provisions of part I of chapter 32.

(b) All participant contributions and state appropriations therefor shall be held in a separate account by the Treasurer ..."

House of Representatives. See Conn. Gen. Stat. § 3-13b. The Treasurer is required by statute to provide information regarding all investments to the Council, and if the Council disagrees with investment decisions made by the Treasurer, the Governor is given statutory authority to "direct the Treasurer to change any investments made by the Treasurer when in the judgment of said council such action is in the best interest of the state." Id. at § 3-13b(c)(2).

Thus, the Treasurer and the funds are subject to the direction and control of the State of Connecticut. See McGinty, 251 F.3d at 98-99 (where state legislature lacked veto power over decisions made by comptroller as trustee of state retirement funds but state statutes provided "strong oversight protections limiting his discretion," this factor supported finding the New York State and Local Employees' Retirement System an arm of the state); JMB Group Trust IV v. Pennsylvania Municipal Retirement Sys., 986 F. Supp. 534, 538 (N.D. Ill. 1997) (concluding that the Pennsylvania Municipal Retirement System was an arm of the state where the duties and responsibilities of the Retirement System were "totally defined and limited by the Commonwealth of Pennsylvania under the provisions of the Pennsylvania Code" and the board's "members are either Commonwealth officials acting ex officio

or appointees of the Governor").

With respect to both funding and Connecticut's liability for CRPTF's financial obligations, plaintiff proffers the affidavit of Catherine LaMarr, General Counsel to the Treasurer, stating that: "The Connecticut General Assembly is obligated to appropriate funds to the State Employees Retirement System each year on an actuarial reserve basis. Any losses incurred by the System will increase the obligations of the State in subsequent years." Aff. of Catherine LaMarr, at ¶ 4. LaMarr's statement comports with Conn. Gen. Stat. § 5-156a, which provides in pertinent part, "[t]he state employees retirement system shall be funded on an actuarial reserve basis."[5] Thus, as noted by the Second Circuit in Fitzpatrick, under Connecticut's statutory scheme, "a judgment against the fund would automatically increase the obligations of the general state treasury and amount to a judgment against the state." 519 F.2d at 565.

Defendants contend that Fitzpatrick was overruled sub

[5] Even if, as defendants argue, current appropriations are not paid into the funds, this does not show that if the funds were subjected to a loss, the state would not be statutorily required to maintain the funds' actuarial soundness. See Deposition of Howard Rifkin at 115 ("if the losses were substantial and reduced the overall value of the fund, the total fund, and benefits in part were being paid out of investment earnings in addition to the contributions made by participants and the plan sponsor, in this case, the state, then at some point an actuary would say that the state contribution would have to increase to offset the long term investment loss").

silentio by the Supreme Court in Regents of the University of California v. Doe, 519 U.S. 425 (1997). The Court disagrees. Regents v. Doe asked whether "the fact that the Federal Government has agreed to indemnify a state instrumentality against the costs of litigation, including adverse judgments, divests the state agency of Eleventh Amendment immunity," 519 U.S. at 426, and answered in the negative, holding “it is the entity’s potential legal liability, rather than its ability or inability to require a third party to reimburse it, or to discharge the liability in the first instance, that is relevant” to the Eleventh Amendment immunity analysis. Id. at 431. Continuing, the Supreme Court illustrated, "Surely, if the sovereign State of California should buy insurance to protect itself against potential tort liability to pedestrians stumbling on the steps of the State Capitol, it would not cease to be ‘one of the United States.’" Id. Defendants application of Regents to the present case thus seeks to force Connecticut into the position of a contractual insurer or indemnifier that merely bears the "ultimate financial liability," id. at 430-31, for any judgment against the allegedly independent entity of the CRPTF funds.

Defendants position is untenable in light of the Supreme Court’s statements in Regents itself, the distinguishing facts

of this case as set forth above, and Second Circuit precedent decided subsequent to Regents. Consistent with the principles in Moor, Regents affirmed the importance of a state's legal obligation for judgments against its arms or alter egos "as an indicator of the relationship between the State and its creation." Regents, 519 U.S. at 431. As set forth above, the office of Treasurer is established by the Connecticut State Constitution, CRPTF is a creation of the State of Connecticut with no corporate form, the funds in the CRPTF are public money in the custody of the Treasurer but under the direction and control of the State of Connecticut, and the state is generally required by statute to replenish losses, including judgments, sustained by the CRPTF.

Moreover, the Second Circuit recently applied the same analysis used in Fitzpatrick, although without citation, to conclude that the New York state retirement system was entitled to sovereign immunity because, inter alia, it received partial funding from the state and "the state will become responsible for replenishing monies used from the pension accumulation fund and the other reserve funds to pay a judgment . . . ." McGinty, 251 F.3d at 97, 99-100. Accordingly, here, as in McGinty, the funding relationship also weighs in favor of finding that the Treasurer is an arm

of the state.

As the removal statute is to be narrowly construed, and guided by the arm or alter ego factors distilled from Moor and enumerated in McGinty as informed by the Second Circuit's decision in Fitzpatrick, the Court concludes that defendants have failed to demonstrate that the Treasurer is a citizen of the State of Connecticut for purposes of the diversity statute.[6]

## IV. Costs and Expenses

When ordering the remand of a case, the district court "may require payment of just costs and any actual expenses, including attorney fees, incurred as a result of the removal." 28 U.S.C. § 1447(c). The statute "affords a great deal of discretion and flexibility to the district courts in fashioning awards...." Circle Indus. USA v. Parke Const. Group, 183 F.3d 105, 109 (2d Cir. 1999)(quotation omitted).

Although an award of costs and expenses need not be based on a finding of bad faith, see Morgan Guar. Trust Co. of New York v. Republic of Palau, 971 F.2d 917, 923-24 (2d 1992), a district court should exercise its discretion in furtherance

[6] Because the Court concludes that the Treasurer cannot be deemed a citizen of Connecticut for purposes of establishing diversity jurisdiction, the issue of alleged fraudulent joinder need not be addressed.

of the statutory goal "to deter improper removal," Circle Indus., 183 F.3d at 109, where the grounds for removal are "contrary to overwhelming authority," Wallace v. Wiedenbeck, 985 F.Supp. 288, 291 (N.D.N.Y. 1998), or without "any reasonable basis," Children's Vill. v. Greenburgh Eleven Teachers' Union Fed'n of Teachers, Local 1532, 867 F.Supp. 245, 248 (S.D.N.Y. 1994).

In the present case, the Court can not say that defendants' removal was contrary to overwhelming authority or lacked any reasonable basis. Although rejected by the Court, the defendants' argument for plaintiff's citizenship based on both a fact intensive analysis of essentially the same factors contemplated by Moor and an amalgamation of Justice Stevens' concurrence in Fitzpatrick v. Bitzer, 427 U.S. 445, 458-60 (1976) and the Supreme Court's opinion in Regents is not wholly without merit.

## V. Conclusion

For the foregoing reasons, plaintiff's motion to remand this case to Connecticut Superior Court [Doc. # 13] is GRANTED, and plaintiff's claim for costs and expenses is DENIED.

The Clerk is directed to remand this case to the State of

Connecticut, Superior Court for the Judicial District of Hartford.

IT IS SO ORDERED.

/s/
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Janet Bond Arterton, U.S.D.J.

**Dated at New Haven, Connecticut, this ____ day of October, 2002.**