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Federal Diversity Jurisdiction and the “Gaping Hole Problem”

This week we take a look at one of the two primary jurisdictional means by which a case may be brought in federal court – *id est* federal diversity jurisdiction. In addition, we examine what has been referred to as the “Gaping Hole Problem” in diversity jurisdiction that arises from the potential exercise of supplemental jurisdiction.

I. Overview of Federal Jurisdiction

Though we have discussed the concept of federal subject matter jurisdiction in a previous post – *Can I Make a Federal Case Out of It?* – as it is necessary to understand federal jurisdiction for the discussion of this post, we shall once more revisit the topic. As a general rule, there are two primary means by which a federal court may have jurisdiction over a case. The first is what is called federal question jurisdiction. The basis for federal question jurisdiction arises from 28 U.S.C. § 1331, which provides: “The district courts shall have original jurisdiction of all civil actions arising under the Constitution, laws, or treaties of the United States.” Put simply, if the case is based upon an issue of federal law, then a federal court will have jurisdiction to decide the case. For example, if someone brings a *qui tam* case pursuant to the Federal False Claims Act, then that case could be heard in a federal court. On the other hand, if someone brings a case seeking damages for violations of

the Indiana Deceptive Consumer Sales Act, then federal question jurisdiction does not apply to allow the case to be heard in federal court.

The other method for providing federal jurisdiction is known as diversity jurisdiction. Diversity jurisdiction, under certain circumstances, permits a federal court to decide cases that are not predicated upon issues of federal law, but rather, are based entirely upon state law issues. For this reason, diversity jurisdiction is a powerful tool that can be utilized either by plaintiffs in filing the case initially in federal court or by defendants who can seek to remove the case from state court to federal court. There are many perceived advantages of being in federal court. Some such advantages are the utilization of electronic filing systems and access to some of the best judges in the entire country.

Another major advantage of federal jurisdiction is that it allows a case to be heard by judges that are lifetime appointments by the federal government and thus who are not subject to election or retention by people of the local state. It is for this reason that Article III, section 2 of the U.S. Constitution provided the basic framework for diversity jurisdiction. The Constitution states: "The judicial power shall extend . . . to controversies . . . between citizens of different states[.]" The fundamental idea in adding this portion to the constitution was to prevent a citizen of one state from getting railroaded by a judiciary in another state that finds itself more sympathetic to the party in whose state the case has been brought. This is particularly true due to the various aspects of the law that often compel a plaintiff to sue a defendant in the defendant's home state, even if the plaintiff is not from that state.

Even though diversity jurisdiction arises from Article III of the Constitution, it is more formally outlined by 28 U.S.C. § 1332. Unlike § 1331 that outlines federal question jurisdiction, § 1332 is rather lengthy and includes very specific tests and analyses for various aspects of diversity jurisdiction. For our purposes it is sufficient to say that § 1332 has two basic requirements for jurisdiction.

The first is that the amount in controversy be in excess of \$75,000. Now we could easily do an entire post on how the amount in controversy is determined, but for now let us just leave it as saying that the case involves the potential of a plaintiff being awarded more than \$75,000. Here is a small, but rather important detail, when pleading a case in federal court under diversity jurisdiction that many lawyers often fail to understand. The amount in controversy requirement specifically states that the amount must be in **excess** of \$75,000. That means that if the amount in controversy is exactly \$75,000 then the case does not qualify for diversity jurisdiction. The amount in controversy must be at least \$75,000.01. Another thing to keep in mind, the amount in controversy set forth in § 1332 has

not always been \$75,000. From time to time, Congress chooses to alter this amount. Thus, it is important to check the most current version of the statute before trying to determine whether the case meets the amount in controversy.

The second requirement is that the parties be diverse. Now this does not mean the same thing as when you hear someone speaking of diversity on a college campus. This means that the parties to the case are not from the same state. However, it is slightly more complicated than that. Section 1332 actually requires what is known as “complete diversity.” The distinction between ordinary diversity and complete diversity only arises when there are more than two parties to a case. In order to illustrate the distinction, the only fitting way is by example.

Example 1: not-complete diversity

The plaintiff is from Indianapolis, Indiana, and he sues two people for causing him injury. The first defendant is from Detroit, Michigan and the second is from South Bend, Indiana. In this instance we could represent the case like this:

Indiana
vs
Michigan and Indiana

Because the plaintiff is from a different state than one of the defendants, there is diversity. But, there is not complete diversity because one of the defendants is from the same state as the plaintiff. Note that it is entirely irrelevant that the plaintiff is not from the same city or county as the Indiana defendant.

Example 2: complete diversity

There are three plaintiffs – John, Michael, and Adam. Adam is from Indiana. John and Michael are from North Dakota. They sue two companies for products liability. Both of those companies are registered in and headquartered in Delaware. Thus we can represent it as:

Indiana, North Dakota, & North Dakota
vs
Delaware and Delaware

In this example there is complete diversity. This is because no single plaintiff is from the same state as a defendant. It does not matter that two of the plaintiffs are from the same state and both defendants are from Delaware.

The easiest way to look at complete diversity is to find the divider between the parties names that is the “vs” if the same state appears on both sides of the “vs” then there is not complete diversity.

Now that we have the basics of amount in controversy and complete diversity we can begin our discussion of the “Gaping Hole Problem.”

II. The Gaping Hole Problem

The Gaping Hole Problem arises when supplemental jurisdiction is exercised in a case that is in federal court because of diversity jurisdiction. Supplemental jurisdiction, governed by 28 U.S.C. § 1367, allows the court to hear additional claims to the ones over which the court has jurisdiction so long as those additional claims arise out of a “common nucleus of operative fact.” To cut through the lawyer speak, what this means is that because a federal court can hear and decide at least one claim in a case, it can also hear other claims so long as they come from the same basic issues as the claim they could otherwise hear. This fits into the concept of judicial economy because it does not waste time by requiring two different courts to have to hear the same basic evidence.

The Gaping Hole Problem is the potential for supplemental jurisdiction to be used to defeat diversity jurisdiction requirements. This would mean that a party seeking to bring a case in federal court who would not be able to meet the requirements for diversity jurisdiction either because adding the additional party/claim would mean having a plaintiff from the same state as a defendant – thus defeating complete diversity – or adding a plaintiff who does not on his or her own meet the amount in controversy only after the case has been brought in federal court. What this would allow is for a clever lawyer to work the system by a mere timing mechanism to get around the diversity jurisdiction requirements and bring a case in federal court that would not have been otherwise permitted.

To illustrate this point, let us look at a great example, the case *Rosario Ortega v. Star-Kist Foods, Inc.* In that case, a nine year-old girl in Puerto Rico named Beatriz injured her finger on a Star-Kist tuna can and suffered severe complications. Beatriz’s mother sought to sue for injuries to both her daughter and herself. Beatriz’s mother desperately wanted the case to be decided in federal court, because, at least at the time, civil jury trials were not available in Puerto Rico local courts. Beatriz on her own was able to meet all of the requirements necessary to file her case in federal court under diversity jurisdiction. Her mother, on the other hand, did not have a claim that, on its own, met the amount in controversy requirement. Thus, the issue in Beatriz’s case was whether the use of supplemental jurisdiction would allow her mother to bring her claim alongside Beatriz’s claim.

Now, remember what the purpose of supplemental jurisdiction is – *id est* to keep multiple courts from having to hear the same evidence and thus wasting court time. There is no question that both Beatriz and her mother had claims arising from the same nucleus of facts and that, for the most part, the exact same evidence would have to be heard to establish either claim. That said, there is also the danger of using this mechanism to defeat the diversity jurisdiction requirements. It was this danger that concerned the First Circuit Court of Appeals when it decided the case. The court ultimately held that the analysis for exercising supplemental jurisdiction in a diversity jurisdiction case required the court to determine if each plaintiff individually met the diversity jurisdiction requirements. Thus, because Beatriz's mother did not meet the amount in controversy requirement, her claim could not proceed in federal court alongside the claims of her daughter.

Whatever you do, do not stop reading this post there, because the First Circuit was not the final say on this case, and their decision is not how the law works today. Beatriz's mother sought review of the decision by the Supreme Court of the United States. The Court agreed to review the decision along with another similar case decided by the Eleventh Circuit. Due to this consolidation, Beatriz's mother's case was decided under a different name. The case became known as *Exxon Mobil Corp. v. Allapattah Services, Inc.* In that case, the nation's highest court held that so long as at least one party has met the requirements of diversity jurisdiction then the court may exercise supplemental jurisdiction over another party's claims **so long as** the only deficiency in the other party's claims is the amount in controversy. Where the other party fails to meet the requirements for complete diversity, then supplemental jurisdiction cannot be used to bring that party into the case. The Court stated, "A failure of complete diversity, unlike the failure of some claims to meet the requisite amount in controversy, contaminates every claim in the action."

This decision, effectively plugged the Gaping Hole in the statute that had caused confusion between the various federal circuits. It created a resolution that permitted justice and judicial economy to allow the addition of related claims that did not meet the amount in controversy and yet did not permit a complete back door to the most basic diversity jurisdiction requirement that the parties be completely diverse.

One interesting angle to this problem is what to do after a party has been added that defeats diversity. The D.C. Circuit, for one, has specifically addressed this issue in *In re Lorazepam & Clorazepate Antitrust Litigation*. In that case, the court found that the inclusion of certain parties defeated diversity. However, instead of dismissing the case entirely for failure to meet subject matter jurisdiction, the court found that the nondiverse parties could simply be removed.

The court noted that this would appear on its face to be in contention with the Supreme Court's decision in *Allapattah*. However, it resolved the conflict by looking to what it described as "the fiction that Rule 21 relates back to the date of the complaint." Through this mechanism, the court could treat the matter as though the nondiverse parties were never a part of the case in the first place. Moreover, "[t]he fiction also allows the district court to save its prior rulings, and the jury's findings, which otherwise were entered without jurisdiction."

One caution to the lesson of *In re Lorazepam* is that once the nondiverse parties have been "scrubbed" from the case, there is still one very important analysis that must be made. The court must look to the totality of the case and determine whether, pursuant to Rule 19, the removed parties are indispensable parties to the case. If they are, then they cannot be removed from the case and the case cannot proceed. Discussion of indispensable parties and Rule 19 is best saved for another day.

Join us again next time for further discussion of developments in the law.

Sources

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