

Class Action Alert

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Supreme Court Closes a Loophole for Class Action Plaintiffs Who Want to Avoid Federal Court

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On March 19, 2013, the Supreme Court held that a class action plaintiff cannot avoid federal jurisdiction under the Class Action Fairness Act (“CAFA”) by stipulating prior to class certification that he and the class will not seek damages exceeding \$5 million in aggregate value. See *Standard Fire Insurance Company v. Knowles*. The central premise of the Court’s ruling is that a proposed class representative cannot legally bind the absent members of a putative class before the class is certified. *Knowles* deals a blow to plaintiff class action lawyers who have tactically employed such stipulations to keep their class actions in friendlier state court fora.

Should a Pre-Certification Stipulation Prevent Federal Jurisdiction Under CAFA?

In April 2011, plaintiff Greg Knowles filed a putative class action complaint in Arkansas state court, asserting state-law claims on behalf of Arkansas residents. Knowles alleged that the Standard Fire Insurance Company had unlawfully failed to include a general contractor fee when the company made certain homeowner’s insurance loss payments. Knowles sought to certify a class of hundreds, or possibly thousands, of similarly-harmed Arkansas policyholders. As alleged in the complaint, Knowles and the class sought to recover aggregate damages of less than \$5 million. The complaint attached an affidavit from Knowles, further stipulating that he would not, at any time in the course of litigation, seek damages for the putative class exceeding \$5 million in the aggregate.

In May 2011, Standard Fire removed the case to the United States District Court for the Western District of Arkansas, relying on CAFA’s jurisdictional provisions. Under CAFA, a federal district court has original jurisdiction over a class action if, among other things, the “matter in controversy exceeds the sum or value of \$5 million.” CAFA also directs that in determining the amount in controversy, “the claims of the individual class members shall be aggregated” from the “persons (named or unnamed) who fall within the definition of the proposed or certified class.” Knowles moved to remand the case to the state court, arguing that CAFA did not apply because his stipulation guaranteed that the amount in controversy would fall below the \$5 million statutory threshold. In opposition, Standard Fire emphasized that the amount in controversy would indisputably exceed CAFA’s threshold, but for the named plaintiff’s purported stipulation. The Western District of Arkansas agreed that, on the face of the pleading, the amount in controversy was slightly more than \$5 million—but held that under existing Eighth Circuit precedent, Knowles’ stipulation foreclosed Standard Fire from demonstrating a higher amount in controversy to meet CAFA’s jurisdictional threshold, and remanded the case to the state court. Standard Fire sought to appeal the remand order, but the Eighth Circuit declined to hear the case.

A split among federal circuit courts existed on the question whether a named plaintiff’s stipulation to limit class damages is effective to avoid CAFA jurisdiction. Some federal appellate courts have held that a putative class representative’s attempts to limit damages in his complaint—or, as with Knowles, in a stipulation—are not dispositive in determining the amount in controversy, while others have held that such efforts defeat CAFA jurisdiction. The Supreme Court agreed to review the *Knowles* case to resolve that split.

The Supreme Court’s Simple Answer Is “No”

The Supreme Court ruled that a named plaintiff may not avoid CAFA removal jurisdiction simply by stipulating that she will not seek damages in excess of CAFA’s \$5,000,000 jurisdictional threshold. Delivering the unanimous opinion of the Court, Justice Stephen Breyer reasoned that Knowles’ proffered stipulation could not bind absent class members that he purported to represent, before the putative class was certified. Timing is critical: for jurisdictional purposes, a federal court’s inquiry is limited to examining the case as of the time it was filed in state court. At the time Knowles filed his action in state court, he lacked the authority to concede the amount in controversy issue on behalf of absent

class members. Consequently, Knowles' pre-certification stipulation did not bind anyone but himself, and thus could not reduce or limit the aggregate value of the putative class members' claims. The District Court, therefore, erred in concluding that Knowles' pre-certification stipulation trumped where the CAFA jurisdictional threshold had otherwise been satisfied. As the Supreme Court stated succinctly in reversing: "Our reason is a simple one: Stipulations must be binding."

Because stipulations must be binding, and because a named plaintiff cannot bind absent class members prior to certification, the sub-\$5 million amount in controversy to which Knowles stipulated was, in effect, contingent. As the Court pointed out, there are a variety of reasons why Knowles' contingent stipulation might not survive the class certification process. For instance, because a class representative bears a fiduciary duty not to "throw away" what could be a major component of the class's recovery, a court might find that Knowles' artificial cap on damages made him an inadequate representative for the class. Or, another class member might intervene and file an amended complaint—with no stipulation—and the court might permit the case to proceed with the new representative.

It follows that, for purposes of determining the amount in controversy, CAFA does not forbid a federal court to consider the very real possibility that a non-binding, class-limiting stipulation may not survive the class certification process. In the Supreme Court's view, treating a nonbinding stipulation as if it were binding would "exalt form over substance" and run directly counter to CAFA's primary objective of ensuring federal court consideration of interstate cases of national importance. Federal courts must ignore nonbinding stipulations about the amount in controversy.

Practical Impact of *Knowles*

The Court's ruling deals a blow to a growing practice among plaintiff class action lawyers, who had been unilaterally stipulating, often successfully, to limit the class's recovery in order to keep the litigation in state courts, where class certification is sometimes easier to achieve. Federal judges are now directed to ignore pre-certification stipulations concerning damages and, as CAFA requires, simply aggregate claims to determine the amount in controversy. The Court was clear that a putative class representative lacks the authority, pre-certification, to bind absent class members.

Finally, it is worth noting that the Court declined to consider whether pre-certification stipulations limiting attorney's fees can be binding. Unlike proposed class members, attorneys usually are present at the time a case is filed in state court and, at least arguably, can agree to be bound by stipulations limiting their requested fees. Indeed, the logic employed by the Court in *Knowles* regarding stipulations as to damages might compel the opposite result when it comes to stipulations concerning attorney's fees.

If you have any questions regarding this alert, please contact one of our authors or any member of [**Venable's Class Action Defense Group**](#).