

Client Alert

Latham & Watkins
Environment, Land & Resources Department

The “Local Controversy” Exception to the Class Action Fairness Act — *Preston, Kaufman and Coffey*

Congress passed the Class Action Fairness Act (CAFA) in 2005 with the intention of reducing class action abuse.¹ CAFA greatly expands federal courts’ jurisdiction over class actions, but has several exceptions that are designed to keep purely local disputes in state courts. One of these exceptions, the “local controversy” exception, bars federal courts from exercising jurisdiction if: (1) more than two-thirds of the proposed class members are citizens of the forum state; (2) the “principal injuries” resulting from the alleged conduct were incurred in the forum state; (3) no class action asserting similar factual allegations has been filed against any of the defendants in the preceding three years; and (4) at least one defendant is a forum-state citizen from whom “significant relief is sought” and whose alleged conduct is a “significant basis” of the claims.²

The circuit courts have begun examining and interpreting key elements of the “local controversy” exception — significant recent decisions include the Fifth Circuit’s decision in *Preston v. Tenet Healthsystem Memorial Medical Center, Inc.*,³ the Third Circuit’s ruling in *Kaufman v. Allstate New Jersey Insurance Company*⁴ and the Tenth Circuit’s holding in *Coffey v.*

*Freeport McMoRan Copper & Gold.*⁵ Together, these opinions provide important guidance regarding the requirements and limitations of the “local controversy” exception.

Burden of Proof

Any party seeking to assert federal jurisdiction under CAFA bears the burden of showing that its jurisdictional requirements are met.⁶ The circuit courts that have addressed CAFA’s exceptions have found that once federal jurisdiction has been established, any party seeking to remand a case to state court bears the burden of showing that an exception to CAFA applies.⁷ Parties seeking to prove that the elements of a CAFA exception are present typically must do so by a preponderance of the evidence.⁸ Appellate courts review remand orders pursuant to the local controversy exception *de novo*.⁹

Two-Thirds Citizenship Requirement — *Preston*

To make a finding that the “local controversy” exception applies, courts must find, among other things, that more than two-thirds of the proposed class members are citizens of the

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forum state. This requirement has been a particularly thorny issue for many plaintiffs. An initial challenge is that accurate estimates of class size — and composition in terms of state citizenship — can be difficult to calculate. Furthermore, a central issue has been that simply showing evidence of residence does not typically suffice to prove citizenship because citizenship is defined by domicile, meaning residence *with intent to remain*. Thus, even where a class may appear to be limited exclusively or at least substantially to residents of the home state, that may not demonstrate by a preponderance of the evidence that the state citizenship requirement is met. Often courts must engage in an extensive evidentiary analysis to determine whether a party seeking to remand its case to state court has met its burden.

An example of this is *Preston v. Tenet Healthsystem Memorial Medical Center, Inc.*, where the Fifth Circuit Court of Appeals addressed this issue and concluded that based on the specific facts of that case, the parties seeking a remand had not met their burden. *Preston* illustrates the challenges that the two-thirds requirement poses and the fact-specific analysis that courts often engage in with respect to this rule.

In *Preston*, a plaintiff brought a putative class action in state court against two New Orleans hospitals.¹⁰ She sued on behalf of herself and others who purportedly suffered injuries in connection with the hospitals' alleged failure to maintain safe conditions and provide adequate transportation during and after Hurricane Katrina.¹¹ After one defendant removed the case to federal court pursuant to CAFA, the plaintiff and the other defendant moved to remand the case under the local controversy exception, and the district court ruled in their favor.¹²

Reviewing the district court's remand order *de novo* on appeal, the Fifth Circuit analyzed whether the parties

seeking remand had produced sufficient evidence to meet the two-thirds requirement of the local controversy exception.¹³ To show that more than two-thirds of the class members were Louisiana citizens on the date the action was filed — which was almost a year after the hurricane — one of the parties seeking remand introduced an affidavit describing pre-Katrina medical records that contained the patients' addresses.¹⁴ According to this affidavit, more than 80 percent of the patients resided in Louisiana.¹⁵ The circuit court found that these records, without more information on, for example, vehicle registrations or prior lengthy residence or employment in Louisiana, did not provide the requisite intent needed to prove that these patients were Louisiana domiciliaries, and therefore citizens.¹⁶ Particularly in light of the exodus of New Orleans residents to neighboring states after the hurricane, the court refused to presume that pre-Katrina addresses suggested that the hospital patients were domiciled in Louisiana more than a year later.¹⁷

Because the parties seeking remand did not produce sufficient evidence to show that the patients were ever domiciled in Louisiana — and marshaled no evidence to suggest that those patients who had left the state after Katrina had any intention of returning — the court refused to adopt a rebuttable presumption that the potential class members maintained their Louisiana domicile after Katrina.¹⁸ Furthermore, the court found that general statistics on voter turnout and on the proportion of total Katrina victims living outside of Louisiana who wanted to return home lacked sufficient specificity to prove the class members' citizenship.¹⁹ The court concluded that the evidence in the record — meaning the medical records — did not allow it to make a “credible estimate” that at least two-thirds of the potential class members were Louisiana citizens at the time the lawsuit was filed.²⁰ Accordingly, the court found that

the parties seeking remand had not met their burden and reversed the district court's decision.²¹

“Significant Basis” and “Principle Injuries” Requirements — *Kaufman*

The local controversy exception contains several other elements that parties seeking remand must prove. One of the leading circuit court decisions interpreting these elements is *Kaufman v. Allstate New Jersey Insurance Company*,²² in which the Third Circuit Court of Appeals interpreted the “significant basis” and “principal injuries” provisions.

In *Kaufman*, plaintiffs sued six auto insurance companies in New Jersey state court.²³ One of the defendants removed the action to federal court pursuant to CAFA, and the plaintiffs petitioned to remand it to state court under the local controversy exception.²⁴ Before the district court heard the petition, the plaintiffs dismissed three of the defendants.²⁵ The district court remanded the case, and the three companies that remained in the case appealed.²⁶

For the local controversy exception to apply, an action must include a local defendant “whose alleged conduct forms a significant basis for the claims asserted by the proposed plaintiff class.”²⁷ In determining whether a defendant in the case met this description, the district court considered all six original defendants rather than the three that remained in the action.²⁸ The court ruled that this was an error, and that the local controversy exception requires courts to take into account only those parties presently in the action.²⁹

On appeal, only one of the three defendants, Allstate NJ, was a New Jersey citizen, and it was thus the only defendant that could possibly meet the “significant basis” requirement.³⁰ The

defendants argued that the language of this provision required that every class member have a claim against Allstate NJ.³¹ Because the individual members of the plaintiff class each had a claim against only one of the companies, the defendants maintained that the plaintiffs could not meet this requirement.³² The circuit court disagreed, concluding that the local defendant's conduct must form a significant basis of the overall action, seen in relation to the conduct of the other defendants, but need not form a basis of every individual claim.³³ The court ruled further that “the local defendant's alleged conduct must be an *important* ground for the asserted claims in view of the alleged conduct of all the Defendants,” and that merely showing the conduct was “more than trivial” did not suffice.³⁴ Finally, criticizing the district court's reliance on market share data in its significant basis analysis, the court noted that “the fact that the local defendant is a major player in a particular market is also not determinative.”³⁵ The court remanded the case for reconsideration of the significant basis provision under these standards.³⁶

The court in *Kaufman* also interpreted the provision limiting the applicability of the local controversy exception to cases in which the “principal injuries resulting from the alleged conduct or any related conduct were incurred” in the home state.³⁷ One defendant argued that this requirement could not be met unless principal injuries “from the alleged conduct” *and* principal injuries from “any related conduct” were incurred in the home state.³⁸ This defendant maintained that its insurance sales outside that state constituted “related conduct” under this provision, that such conduct caused “principal injuries” outside the home state, and that the requirement was therefore not met.³⁹ The court found this interpretation “at odds with the plain language of the provision” and rejected it.⁴⁰

“Defendant From Whom Significant Relief is Sought” Requirement — *Coffey*

Parties seeking to remand their case under the local controversy exception also must prove that at least one defendant is a forum-state citizen from whom “significant relief is sought.” Earlier this month, the Tenth Circuit Court of Appeals addressed this requirement, in *Coffey v. Freeport McMoRan Copper & Gold*.⁴¹ In a case of first impression, the court held that a “defendant from whom significant relief is sought” does not mean a “defendant from whom significant relief *may* be obtained.”⁴² The court explained that under CAFA, a company’s wherewithal or ability to pay a potential judgment is not a factor in determining whether it is a local defendant.⁴³

In *Coffey*, plaintiffs filed a putative class action in Oklahoma state court, asserting state law claims based on the defendants’ alleged contamination of their property through the operation of a smelter. The defendants included Blackwell Zinc Company, Inc. (BZC), who owned and operated the smelter for more than 50 years, as well as other legal entities that have since owned BZC. After the defendants removed the case to federal court under CAFA,⁴⁴ the plaintiffs moved to remand the case under the local controversy exception, and the district court ruled in their favor.⁴⁵

Reviewing the district court’s remand order on appeal, the Tenth Circuit analyzed whether this case satisfied the requirements of the local controversy exception and it also interpreted the meaning of the provision “defendant from whom significant relief is sought.” Under the local controversy exception, plaintiffs are required to show that there is at least one “local defendant”: (1) from whom significant relief is sought by members of the plaintiff class; (2) whose alleged conduct forms a significant basis for the claims asserted by the proposed plaintiff class;

and (3) who is a citizen of the state in which the action was originally filed.⁴⁶

The defendants in this case did not dispute that the conduct of BZC formed a significant basis for the claims brought by the putative plaintiff class. However, the defendants argued that the plaintiffs failed to show that BZC was a “defendant from whom significant relief is sought” by the putative class members.⁴⁷ In particular, the defendants asserted that this statutory language requires consideration of a defendant’s ability to pay a judgment and, in this case, BZC had no assets to satisfy any potential judgment and therefore, could not be considered a “defendant from whom significant relief is sought.”⁴⁸ The Tenth Circuit rejected this argument and agreed with the district court’s analysis. The court explained that, consistent with CAFA’s statutory language, this exception “refers to a defendant from whom significant relief is ‘sought,’ rather than a defendant from whom the relief ‘may be obtained’ or ‘can be collected.’”⁴⁹ The court determined that the “significant relief element was satisfied [in this case], where the petition claimed that every potential plaintiff was entitled to recover from BZC and that the putative class sought to collect damages from all defendants jointly and severally.”⁵⁰ Moreover, the court stated that this case was a “classic example of what Congress intended to cover” when it created the local controversy exception — “a controversy that uniquely affect[ed] a particular locality to the exclusion of all others.”⁵¹

Conclusion

CAFA gives parties in class action and mass action lawsuits broader access to federal courts; however, certain exceptions, including the local controversy exception, limit this access and provide a means for parties to keep certain actions in state court. Because CAFA is a relatively new law, courts are still interpreting its

provisions — including key aspects of these exceptions — for the first time. An understanding of the relevant, most recent case law on CAFA can help defendants craft an advantageous strategy toward class action and mass action lawsuits. Businesses that are or may be involved in this type of litigation should remain apprised of developments in this rapidly evolving area of law.

Endnotes

- ¹ CAFA gives federal courts jurisdiction over class actions in which “minimal diversity” is present (*i.e.*, where at least one class member has different state citizenship than at least one defendant); the amount in dispute is greater than \$5 million; the class includes at least 100 people; and the defendants do not include states, state officials, or certain other governmental entities. 28 U.S.C. § 1332(d)(2), (5). CAFA also grants federal jurisdiction over “mass actions,” which involve 100 or more individual plaintiffs whose claims share common questions of law or fact, but are not class actions. 28 U.S.C. § 1332(d)(11). The mass action provisions require that at least one plaintiff’s claim exceeds \$75,000, and that the plaintiffs’ aggregated claims are in excess of \$5 million. *See* 28 U.S.C. § 1332(d)(11); *Abrego Abrego v. Dow Chem. Co.*, 443 F.3d 676, 689 (9th Cir. 2006).
- ² 28 U.S.C. § 1332(d)(4)(A).
- ³ *Preston v. Tenent Healthsystem Mem’l Med. Ctr., Inc.*, 485 F.3d 793 (5th Cir. 2007).
- ⁴ *Kaufman v. Allstate N.J. Ins. Co.*, 561 F.3d 144 (3d Cir. 2009).
- ⁵ *Coffey v. Freeport McMoRan Copper & Gold*, No. 09-6106, slip op. (10th Cir. Sept. 4, 2009).
- ⁶ *See, e.g., Blockbuster, Inc. v. Galeno*, 472 F.3d 53, 58 (2d Cir. 2006); *Abrego Abrego*, 443 F.3d at 686; *Evans v. Walter Indus., Inc.*, 449 F.3d 1159, 1164 (11th Cir. 2006); *Brill v. Countrywide Home Loans, Inc.*, 427 F.3d 446, 448 (7th Cir. 2005).
- ⁷ *Grimsdale v. Kash N’ Kary Food Stores, Inc.*, 564 F.3d 75, 78 (1st Cir. 2009); *Kaufman*, 561 F.3d at 153; *Serrano v. 180 Connect, Inc.*, 478 F.3d 1018, 1024 (9th Cir. 2007); *Hart v. FedEx Ground Package Sys. Inc.*, 457 F.3d 675, 680-81 (7th Cir. 2006); *Frazier v. Pioneer Ams. LLC*, 455 F.3d 542, 546 (5th Cir. 2006); *Evans*, 449 F.3d at 1165. District courts also have placed this burden on the party moving to remand. *See, e.g., Magee v. Advance Am. Servicing of Ark., Inc.*, No. 6:08-cv-6105, 2009 WL 890991, at *3 (W.D. Ark. Apr. 1, 2009); *McClendon v. Challenge Fin. Investors Corp.*, No. 1:08CV1189, 2009 WL 589245, at *10 (N.D. Ohio Mar. 9, 2009); *Moua v. Jani-King of Minn., Inc.*, 613 F. Supp. 2d 1103, 1107 (D. Minn. 2009).
- ⁸ *See, e.g., McClendon*, 2009 WL 589245, at *10; *Anthony v. Small Tube Mfg. Corp.*, 535 F. Supp. 2d 506, 514-15 (E.D. Pa. 2007).
- ⁹ *See, e.g., Preston*, 485 F.3d at 796; *Kaufman*, 561 F.3d at 151; *Evans*, 449 F.3d at 1161-62. In the context of the CAFA exceptions, appellate courts review factual findings for clear error. *Preston*, 485 F.3d at 796.
- ¹⁰ *Preston*, 485 F.3d at 795.
- ¹¹ *Id.* at 796.
- ¹² *Id.*
- ¹³ *Id.*
- ¹⁴ *Id.* at 798.
- ¹⁵ *Id.*
- ¹⁶ *Id.* at 798, 800.
- ¹⁷ *Id.* at 799-801.
- ¹⁸ *Id.* at 801-02.
- ¹⁹ *Id.* at 802.
- ²⁰ *Id.* at 803.
- ²¹ *Id.* at 803-04.
- ²² *Kaufman*, 561 F.3d 144.
- ²³ *Id.* at 150.
- ²⁴ *Id.*
- ²⁵ *Id.* at 153.
- ²⁶ *Id.* at 150.
- ²⁷ 28 U.S.C. § 1332(d)(4)(A)(i)(II)(bb).
- ²⁸ *Kaufman*, 561 F.3d at 153.
- ²⁹ *Id.*
- ³⁰ *Id.* at 154.
- ³¹ *Id.*
- ³² *Id.* at 154-55.
- ³³ *Id.* at 155.
- ³⁴ *Id.* at 157 (emphasis in original).
- ³⁵ *Id.*
- ³⁶ *Id.*
- ³⁷ *Id.* at 158 (quotation omitted).
- ³⁸ *Id.*
- ³⁹ *Id.*
- ⁴⁰ *Id.*
- ⁴¹ *Coffey v. Freeport McMoRan Copper & Gold*, No. 09-6106, slip op. (10th Cir. Sept. 4, 2009) (as of the date of this *Client Alert*, no notice of appeal or petition for rehearing has been filed).

⁴² *Id.*, slip op. at 10 (emphasis added) (quoting the district court's decision).

⁴³ *Id.*

⁴⁴ The defendants also asserted federal jurisdiction based on CERCLA.

⁴⁵ *Coffey*, No. 09-6106, slip. op. at 3.

⁴⁶ 28 U.S.C. § 1332(d)(4)(A)(i).

⁴⁷ *Coffey*, No. 09-6106, slip. op. at 7. The defendants also argued that plaintiffs failed to show that BZC is a citizen of Oklahoma, which the court rejected.

⁴⁸ *Id.* at 9.

⁴⁹ *Id.* (quotation omitted).

⁵⁰ *Id.* (quotation omitted).

⁵¹ *Id.* at 6 (quotation omitted).

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