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The Uncertain Status of the Legal Certainty Test: The Need for Consistency among Federal Courts When Determining the Amount-in-Controversy

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THE UNCERTAIN STATUS OF THE LEGAL CERTAINTY TEST: THE NEED FOR CONSISTENCY AMONG FEDERAL COURTS WHEN DETERMINING THE AMOUNT-IN-CONTROVERSY

INTRODUCTION

For the federal courts, jurisdiction is not automatic and cannot be presumed. Thus, the presumption in each instance is that a federal court lacks jurisdiction until it can be shown that a specific grant of jurisdiction applies. Federal courts may exercise only that judicial power provided by the Constitution in Article III and conferred by Congress. All other judicial power or jurisdiction is reserved to the states. And although plaintiffs may urge otherwise, it seems settled that federal courts may assume only that portion of the Article III judicial power which Congress, by statute, entrusts to them. Simply stated, Congress may impart as much or as little of the judicial power as it deems appropriate and the Judiciary may not thereafter on its own motion recur to the Article III storehouse for additional jurisdiction. When it comes to jurisdiction of the federal courts, truly, to paraphrase the scripture, the Congress giveth, and the Congress takethaway.[1]

As former District Court Judge John Sirica confirmed in his famous 1973 Watergate opinion, the limited jurisdiction of federal courts in the United States is a fundamental element of our judicial system.[2] Indeed, a plaintiff may only bring a lawsuit in federal court if the cause of action satisfies the jurisdictional limitations of the Constitution and any further Congressional restrictions.[3] First, a plaintiff may bring a claim in federal court if the cause of action arises "under this Constitution, the Laws of the United States, and Treaties made, or which shall be made, under their

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[1] Senate Select Comm. on Presidential Campaign Activities v. Nixon, 366 F. Supp. 51, 55 (D.D.C. 1973).

[2] *See id.* (discussing limited jurisdiction of federal courts and prerequisites to jurisdiction).

[3] *See generally* ERWIN CHEMERINSKY, FEDERAL JURISDICTION §§ 2.1-2.6, (4th ed. 2003) (discussing constitutional and statutory limits on federal jurisdiction).

Authority."[4] Second, if the plaintiff's cause of action does not arise under federal law but is against a citizen of a different state, he may bring his suit in federal court under diversity jurisdiction.[5] In diversity cases, Congress has further limited the jurisdiction of federal courts by enacting 28 U.S.C. § 1332, which grants federal courts original jurisdiction in diversity cases only if the dispute exceeds a monetary threshold amount.[6]

Although Congress established a jurisdictional threshold, it did not establish statutory guidelines for determining when the monetary requirement is satisfied, and therefore judicial interpretation has guided federal courts' determination of the amount in controversy.[7] In *St. Paul Mercury Indemnity Company v. Red Cab Company,*[8] the Supreme Court announced the "legal certainty" test, holding that "the sum claimed by the plaintiff controls if the claim is apparently made in good faith" and that "[i]t must appear to a legal certainty that the claim is really for less than the jurisdictional amount to justify dismissal."[9] Since the *Red Cab* decision, federal courts have split as to what courts may consider when determining if the amount in controversy exceeds the jurisdictional threshold.[10] Circuit courts that follow the minority approach have applied *Red Cab* strictly,

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[4] U.S. CONST. art. III, § 2, cl. 1 (granting original jurisdiction to federal courts in federal question actions).

[5] *See id.* (authorizing federal courts to hear cases "between Citizens of different States"). Courts have interpreted this jurisdictional grant to require complete diversity between the parties, so that all plaintiffs must be from different states than all defendants when a case is brought on diversity grounds. *See* Strawbridge v. Curtiss, 7 U.S. 267 (1806) (announcing "complete diversity" requirement for diversity jurisdiction).

[6] 28 U.S.C. § 1332(a) (2006) (establishing threshold amount in controversy for federal diversity jurisdiction). Congress originally set the jurisdictional threshold amount at $500. Federal Judiciary Act of 1789 § 11, 1 Stat. 73, 78-79. Congress has periodically increased the amount in controversy requirement because of inflation. *See, e.g.*, Act of March 3, 1911 § 24, 36 Stat. 1087, 1091 ($3000); Act of July 25, 1958, 72 Stat. 415 ($10,000); Judicial Improvements and Access to Justice Act § 201, 102 Stat. 4642, 4646 (1988) ($50,000). In 1996, it raised the amount in controversy requirement from $50,000 to $75,000, which is the current jurisdictional threshold. Federal Courts Improvement Act of 1996 § 205, 110 Stat. 3847-3850. *See also* Jordan F. Miller Corp. v. Mid-Continent Aircraft Serv., Inc., No. 98-5104, 1999 WL 164955, at *3 (10th Cir. March 24, 1999) ("We recognize that the legislative history of § 1332(b) demonstrates an intent to deter plaintiffs from filing cases in federal court when the amount in controversy is, or is likely to be, less than the jurisdictional amount.").

[7] *See* 28 U.S.C. § 1332(a) (2006) (establishing no guidelines for determining amount in controversy).

[8] 303 U.S. 283 (1938).

[9] *Id.* at 288-89 (establishing "legal certainty" test for diversity jurisdiction).

[10] *See* Adams v. Reliance Standard Life Ins. Co., 225 F.3d 1179, 1182 (10th Cir. 2000) (asserting "open-ended prayer for recovery . . . is not an allegation that diversity jurisdiction exists . . . ."); *see also* Jimenez-Puig v. Avis Rent-A-Car Sys., 574 F.2d 37, 40 (1st Cir. 1978) (holding plaintiff's claim not controlling when, viewed objectively, could not exceed jurisdictional amount).

holding that only the plaintiff's good faith claim controls.[11] Under the majority approach, however, circuit courts have held that courts sitting in diversity may look beyond the pleadings to determine whether subject matter jurisdiction is present.[12] To date, the Supreme Court has not resolved this split, and therefore a lawsuit that could be heard in one circuit on diversity grounds could be dismissed in another circuit for want of jurisdiction.[13]

This Note will argue that a limited application of the majority approach is the sound analytical method for determining whether the amount in controversy exceeds the jurisdictional threshold.[14] Part I will examine the historical interpretation of the amount in controversy requirement, focusing on attempts by the Supreme Court to establish guidelines for lower federal courts to follow.[15] Part II will discuss the competing applications of the *Red Cab* standard, and the inconsistency inherent in the circuit court split.[16] Part III will argue that a limited application of the majority rule is the logical solution to resolving the current split among the circuits.[17] Specifically, this Note will argue that where subject matter jurisdiction depends on the court's determination of the enforceability of a state statutory or contractual limitation on damages, federal courts sitting in diversity should dismiss these cases for want of jurisdiction.[18] In all other cases, the *Red Cab* standard should control, and federal courts should not consider other defenses to defeat diversity

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[11] *See* Ochoa v. Interbrew Am., Inc., 999 F.2d 626, 630 (2d Cir. 1993) (declining to consider valid defense disclosed in complaint when determining if amount in controversy satisfied); *see also* Anderson v. Moorer, 372 F.2d 747, 750 (5th Cir. 1967) (holding res judicata defense could not defeat diversity jurisdiction). In this regard, some federal courts have refused to consider the validity of state laws that, if upheld, would limit recovery below the jurisdictional threshold. *See* Crawford v. Martin Marietta Corp., 622 F.2d 339, 341 (8th Cir. 1980) ("federal courts are not to overrule settled state law and predict that a state court would do so without strong indications from the state itself").

[12] *See* Pratt Cent. Park Ltd. P'ship v. Dames & Moore, Inc., 60 F.3d 350, 354 (7th Cir. 1995) (dismissing diversity case on grounds that contractual clause limited recovery to $5000); *see also* Valhal Corp. v. Sullivan Assocs., Inc., 44 F.3d 195, 209 (3d Cir. 1995) (dismissing diversity case because contract provision limited recovery to $50,000).

[13] *Compare* Pachinger v. MGM Grand Hotel-Las Vegas, Inc., 802 F.2d 362, 365 (9th Cir. 1986) (affirming dismissal of diversity suit for want of jurisdiction because statute limited recovery to $750), *with* Zacharia v. Harbor Island Spa, Inc., 684 F.2d 199, 202 (2d Cir. 1982) (refusing to consider affirmative defense that statute limited recovery to $1000 for jurisdictional determination).

[14] *See Pratt Cent.*, 60 F.3d at 354 (affirming dismissal where contractual clause limited plaintiff's recovery below jurisdictional threshold).

[15] *See infra* Part I (discussing evolution of amount in controversy requirement).

[16] *See infra* Part II (analyzing competing applications of *Red Cab* standard).

[17] *See infra* Part III (proposing solution to current circuit court split).

[18] *See infra* Part III (arguing interpretations of state law should be left to state courts).

jurisdiction.[19] Ultimately, this Note will advocate that adopting this limited application of the majority rule would resolve the split among the courts and eliminate the inconsistent outcomes of diversity actions in the circuit courts.[20]

I. HISTORICAL DEVELOPMENT OF THE AMOUNT IN CONTROVERSY REQUIREMENT

The United States Constitution contains no requirement that diversity cases exceed a minimum monetary threshold.[21] The expansive jurisdictional grants conferred in Article III, § 2 of the Constitution, however, established the outer boundaries of federal court jurisdiction, and Article III, § 1 granted Congress the power to narrow the reach of that jurisdiction.[22] Indeed, Congress has limited the jurisdiction of federal courts sitting in diversity by enacting 28 U.S.C. § 1332 ("Section 1332").[23]

While it is not entirely apparent from the legislative history of Section 1332, the conventional rationale for its enactment was to allow foreign plaintiffs access to a forum that would be free of the potential prejudice of state courts.[24] Congress did not intend to grant an unlimited right of access, however, and thus included additional restrictions in the diversity statute.[25] This Note focuses on one such limitation—the amount in controversy threshold that a plaintiff must satisfy to invoke diversity jurisdiction.[26]

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[19] *See* Ochoa v. Interbrew Am., Inc., 999 F.2d 626, 630 (2d Cir. 1993) (refusing to consider valid defense disclosed in complaint in determining whether amount in controversy satisfied); *see also* Anderson v. Moorer, 372 F.2d 747, 750 (5th Cir. 1967) (holding res judicata defense could not defeat diversity jurisdiction).

[20] *See* Valhal Corp. v. Sullivan Assocs., Inc., 44 F.3d 195, 204 (3d Cir. 1995) (dismissing diversity case where liability clause limited recovery below jurisdictional threshold).

[21] U.S. CONST. art. III, § 2, cl. 1 (authorizing federal courts to hear cases "between Citizens of different States").

[22] U.S. CONST. art. III, § 1 (establishing federal judiciary "in one Supreme Court, and in such inferior Courts as the Congress may from time to time ordain and establish").

[23] 28 U.S.C. § 1332 (2006) (establishing requirements for federal diversity jurisdiction).

[24] *See* CHARLES ALAN WRIGHT, LAW OF FEDERAL COURTS § 142 (5th ed. 1994) (discussing purpose of Section 1332); *see also* Henry Jacob Friendly, *The Historic Basis of Diversity Jurisdiction*, 41 HARV. L. REV. 483, 487-91 (1928) (discussing alternate justifications for diversity jurisdiction).

[25] *See, e.g.*, 28 U.S.C. § 1332(a) (2006) (defining amount in controversy and diversity of citizenship); 28 U.S.C. § 1332(b) (2006) (allowing district court to deny costs to plaintiff if actual recovery is less than threshold amount); 28 U.S.C. § 1332(c) (2006) (defining corporate and legal representative of estate citizenship for purpose of establishing diversity); 28 U.S.C. § 1332(d) (2006) (establishing diversity requirements for class actions).

[26] 28 U.S.C. § 1332(a) (2005) (establishing threshold amount in controversy for federal diversity jurisdiction).

Since the enactment of Section 1332, and specifically the inclusion of an amount in controversy requirement, scholars have promulgated numerous bases for its existence.[27] The early prevailing view was that Congress wanted to ensure that out-of-state plaintiffs could not subject defendants to suit in distant forums for insignificant claims.[28] A more modern and perhaps more practical justification for the monetary requirement is to maintain a manageable caseload in the federal courts.[29] The inability of the parties to waive subject matter jurisdiction may provide additional support for this latter explanation.[30]

Subject matter jurisdiction is a fundamental tenet of the American judicial system, and its significance is reflected in the fact that either of the litigating parties may raise the issue or a court may raise it *sua sponte*.[31] In diversity cases, however, whether subject matter jurisdiction exists is not always clear from the pleadings or even during the early stages of trial.[32] For instance, the state citizenship of a litigating party may be unclear, which could defeat the complete diversity requirement established in *Strawbridge v. Curtiss*.[33] While some of this confusion has been resolved through judicial interpretation and Congressional legislation, the method of determining whether the litigation exceeds the jurisdictional threshold remains a conflict among the circuit courts that has lingered for over a century.[34] To date, the Supreme Court has yet to adopt a uniform rule for federal courts to apply in making this determination.[35]

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[27] *See* HENRY M. HART & HERBERT WECHSLER, THE FEDERAL COURTS AND THE FEDERAL SYSTEM 786 (2d ed. 1973) (discussing various bases argued for diversity jurisdiction).

[28] *See id.* (arguing amount in controversy requirement protected defendants from traveling far to defend small claims).

[29] *See* Note, *Federal Jurisdictional Amount: Determination of the Matter in Controversy*, 73 HARV. L. REV. 1369, 1370 (1960) (discussing other historical justifications for diversity jurisdiction).

[30] *See* FED. R. CIV. P. 12(h)(3) ("[I]f the court determines at any time that it lacks subject-matter jurisdiction, the court must dismiss the action.").

[31] *See* FED. R. CIV. P. 12 (allowing either party or court to raise issue of subject matter jurisdiction).

[32] *See,* Deutsch v. Hewes St. Realty Corp., 359 F.2d 96, 100 (2d Cir. 1966) (discussing difficulty in determining amount in controversy at outset of case).

[33] 7 U.S. 267, 267-68 (1806) (establishing complete diversity rule).

[34] *Compare* Anderson v. Moorer, 372 F.2d 747, 750 (5th Cir. 1967) (holding res judicata defense could not defeat diversity jurisdiction), *with* Jimenez-Puig v. Avis Rent-A-Car Sys., 574 F.2d 37, 40 (1st Cir. 1978) (holding plaintiff's good faith claim not controlling when, viewed objectively, could not exceed jurisdictional amount).

[35] *See* Alice M. Noble-Allgire, *Removal of Diversity Actions When the Amount in Controversy Cannot be Determined from the Face of Plaintiff's Complaint: The Need for Judicial and Statutory Reform to Preserve Defendant's Equal Access to Federal Courts*, 62 MO. L. REV. 681, 685 (1997) (discussing confusion among federal courts in determining amount in controversy).

Since the enactment of Section 1332, the Court repeatedly has addressed the difficulty in determining whether the cause of action exceeds the amount in controversy, and has provided some guidelines for analyzing the issue.[36] In *Mississippi & Missouri Railroad Co. v. Ward*,[37] the Court faced the question of whether the cause of action satisfied the jurisdictional amount where the relief sought was injunctive rather than monetary.[38] In *Ward*, the plaintiff steamboat owner sought an abatement of a bridge that he argued was a nuisance.[39] The Court concluded that to determine whether the action seeking injunctive relief exceeded the amount in controversy, "the value of the object must govern."[40] Without any further substantive analysis as to what it meant by the "value of the object," however, the *Ward* Court provided little guidance for future determinations of amount in controversy disputes.[41]

The seminal Supreme Court decision concerning the amount in controversy requirement for diversity jurisdiction came down in 1938 in *Red Cab*, nearly eight decades after the Court decided *Ward*.[42] In *Red Cab*, the respondent, an Indiana corporation, contracted with the petitioner, a Minnesota corporation, whereby the petitioner agreed to insure against losses or expenses incurred for claims of compensation for a thirty-day period.[43] The original complaint sought $4000 in damages, but after the defendant removed the case to federal court the plaintiff filed an amended complaint with an exhibit attached listing injuries totaling approximately one-third of that amount.[44] The District Court found for the plaintiff in the amount of $1162.98, but on appeal the Circuit Court of Appeals for the

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[36] *See* Mississippi & Missouri R.R. Co. v. Ward, 67 U.S. 485, 492 (1862) (announcing "value of the object" test).

[37] 67 U.S. 485 (1862).

[38] *Id.* at 492 (discussing difficulty of assessing monetary amount to injunctive relief prayed).

[39] *Id.* at 491 (detailing facts giving rise to nuisance action). The bridge in dispute extended over the Mississippi River, and the plaintiff alleged that it interrupted the navigation of the river, which was "a necessity of trade, and almost the only means of transportation between Wisconsin, Northern Iowa, Minnesota, and the upper Mississippi." *Id.* at 487. The plaintiff further alleged that several of his boats had been damaged because of the rapid current caused by the erection of the bridge at that particular point on the river, and that he had to pay higher insurance premiums because of the risk caused by the bridge. *Id.*

[40] *Id.* at 492 (adopting "value of the object" test).

[41] *See id.* (failing to further explain "value of object" test).

[42] *See* St. Paul Mercury Indem. Co. v. Red Cab Co., 303 U.S. 283 (1938) (announcing "legal certainty" test).

[43] *Id.* at 284 (explaining terms of contract in dispute).

[44] *Id.* at 285 (detailing facts of case). The amended complaint still sought $4000 in damages, even though the exhibit listed a lesser amount. *Id.* In 1937, the amount in controversy requirement for diversity jurisdiction was $3000. Act of March 3, 1911 § 24, 36 Stat. 1087, 1091.

Seventh Circuit remanded to the state court for want of jurisdiction because the claims on the record did not satisfy the amount in controversy.[45] In reversing the Seventh Circuit, the Supreme Court held that where the plaintiff's claim is made in good faith, "it must appear to a legal certainty that the claim is really for less than the jurisdictional amount to justify dismissal."[46] The Court reasoned that the respondent had a good faith claim on the face of the pleadings to invoke federal jurisdiction, and a subsequent reduction after initial filing did not eliminate that jurisdiction.[47]

II. THE CURRENT COMPETING INTERPRETATIONS OF THE RED CAB STANDARD AMONG THE FEDERAL CIRCUITS

While the "legal certainty" test adopted in *Red Cab* is seemingly straightforward in its language, it has proven markedly convoluted in its application among the circuit courts.[48] Circuit courts of appeals continually have struggled with which viewpoint is controlling in the litigation, and three further approaches have developed: the "plaintiff-viewpoint" approach, the "either-party" approach, and the "party-invoking jurisdiction" approach.[49] Under the plaintiff-viewpoint approach, which was essentially the approach taken by the *Red Cab* Court, courts look only to the plaintiff's complaint.[50] Courts following the "either-party" approach look to see if either the plaintiff's requested recovery or the defendant's potential cost to comply therewith exceeds the monetary threshold.[51] Finally, a small number of courts following the "party-invoking jurisdiction" approach look only to the interest of the party invoking federal jurisdiction, either to the plaintiff's filing in federal court or to the defendant's removal to federal court, to see if the jurisdictional threshold is satisfied.[52]

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[45] *See* St. Paul Mercury Indem. Co. v. Red Cab Co., 90 F.2d 229, 230 (7th Cir. 1937) (remanding to state court for lack of diversity jurisdiction), *rev'd*, 303 U.S. 283 (1938).

[46] *Red Cab*, 303 U.S. at 288-89 (establishing "legal certainty" test).

[47] *See id.* at 296 (holding that initial good faith claim controls).

[48] *See* CHEMERINSKY, *supra* note 3, § 5.3 (discussing different approaches taken by federal courts in diversity cases).

[49] *See generally* Evan A. Creutz, Note, *Two Sides to Every Story: Measuring the Jurisdictional Amount in Federal Courts*, 68 FORDHAM L. REV. 1719, 1726-34 (2000) (discussing evolution of three competing viewpoints).

[50] *See Red Cab*, 303 U.S. at 288-89 (holding plaintiff's good faith claim determines whether jurisdiction exists).

[51] *See* McCarty v. Amoco Pipeline Co., 595 F.2d 389, 395 (7th Cir. 1979) (applying "either-party" approach in upholding diversity jurisdiction).

[52] *See* Panama Transport Co. v. Greenberg, 290 F.2d 125, 126 (1st Cir. 1961) (applying "party-invoking jurisdiction" approach in dismissing for lack of jurisdiction).

The competing interpretations of the *Red Cab* decision have led to a further split among the circuit courts regarding the extent to which courts should consider factors beyond the plaintiff's good faith pleading.[53] Specifically, there is disagreement as to whether a court sitting in diversity should consider an affirmative defense in the pleadings which, if valid, would defeat diversity jurisdiction.[54] To this end, the circuit courts have taken two distinct positions: the minority approach, proponents of which generally do not consider affirmative defenses in ascertaining whether diversity jurisdiction exists; and the majority approach, proponents of which look beyond the pleadings to determine whether jurisdiction is proper.[55]

A. The Minority Approach

Federal courts following the minority approach have applied the *Red Cab* standard strictly and have held that only the plaintiff's claim controls.[56] The 1967 Fifth Circuit case of *Anderson v. Moorer*[57] is an early illustration of the minority approach.[58] In *Anderson*, the plaintiff owned certain freehold and leasehold interests in mineral land in Alabama pursuant to a decree of the Circuit Court of Mobile County, Alabama.[59] The plaintiff then brought suit in federal court, claiming that she was entitled to a larger share than she had received from the Alabama court decree.[60] The defendants sought to dismiss the case on jurisdictional grounds, arguing that the Alabama decree was res judicata and therefore the plaintiff's claim could not exceed the monetary threshold even though

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[53] *Compare* Pachinger v. MGM Grand Hotel-Las Vegas, Inc., 802 F.2d 362, 365 (9th Cir. 1986) (dismissing diversity suit for want of jurisdiction because statute limited recovery to $750), *with* Zacharia v. Harbor Island Spa, Inc., 684 F.2d 199, 202 (2d Cir. 1982) (declining to consider affirmative defense that statute limited recovery to $1000 for jurisdictional determination).

[54] *See* Anderson v. Moorer, 372 F.2d 747, 750 (5th Cir. 1967) (holding res judicata defense could not defeat amount in controversy if satisfied in plaintiff's pleading).

[55] *See id.* (providing illustration of the minority approach); *see also* City of Boulder v. Snyder, 396 F.2d 853, 856 (10th Cir. 1968) (providing illustration of majority approach).

[56] *See, e.g.*, Scherer v. Equitable Life Assurance Soc'y of the U.S., 347 F.3d 394, 397 (2d Cir. 2003) (refusing to consider pleaded defense of preclusion in determining amount in controversy); Ochoa v. Interbrew Am., Inc., 999 F.2d 626, 630 (2d Cir. 1993) (asserting valid defense disclosed in complaint not considered in determining if amount in controversy satisfied); Deutsch v. Hewes St. Realty Corp., 359 F.2d 96, 100 (2d Cir. 1966) (holding tort claim for unliquidated damages did not justify dismissal for lack of jurisdiction).

[57] 372 F.2d 747 (5th Cir. 1967).

[58] *See id.* at 750 (holding res judicata defense could not defeat amount in controversy if satisfied in plaintiff's pleading).

[59] *Id.* at 749 (discussing background of case).

[60] *See id.* (detailing plaintiff's claim for additional damages).

she had claimed more than $10,000.[61] The Fifth Circuit upheld jurisdiction over the matter, asserting that "the probability of a valid factual defense . . . is not sufficient to diminish the amount in controversy and to oust the court of jurisdiction, even if that defense appears on the face of the complaint."[62]

Courts following the minority approach also apply the "legal certainty" test liberally when encountering a case for unliquidated damages.[63] These courts, however, will still dismiss a cause of action for lack of jurisdiction if, during the course of the litigation, it becomes readily apparent that the plaintiff's claim could not have exceeded the threshold.[64] While these interpretations might appear inconsistent on the surface, they are distinguishable.[65] In a case for unliquidated damages, courts following the minority approach will not dismiss for lack of jurisdiction.[66] The rationale for conferring jurisdiction in such a case is that a dismissal would amount to a judicial finding as to what damages the plaintiff could recover, thereby invading the province of the jury.[67] In a diversity case where the

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[61] *Id.* at 750. In 1967, the amount in controversy threshold was $10,000. Act of July 25, 1958, 72 Stat. 415-416.

[62] Anderson v. Moorer, 372 F.2d 747, 750 (5th Cir. 1967).

[63] *See* Deutsch v. Hewes St. Realty Corp., 359 F.2d 96, 100 (2d Cir. 1966) (finding diversity jurisdiction in tort action for unliquidated claim). In *Deutsch,* the Second Circuit Court of Appeals faced precisely this issue when the plaintiff brought a negligence action against the defendant corporation seeking to recover $25,000 for personal injuries. *Id.* at 97. In its answer, the defendant denied that the plaintiff's damages exceeded $10,000, which was the statutory minimum at that time for diversity actions, and moved to dismiss the action. *Id.* at 98. The district judge dismissed the action for lack of jurisdiction, stating that there was a "remote unlikely possibility that a jury would return a verdict in the amount of $10,000 or more . . . ." *Id.* On appeal, the Second Circuit reversed, holding that the district judge could not attempt to predetermine the value of an unliquidated damages claim, and therefore federal diversity jurisdiction was proper. *Id.* at 100.

[64] *See* Tongkook Am., Inc. v. Shipton Sportswear Co., 14 F.3d 781, 785 (3d Cir. 1994) (dismissing for lack of jurisdiction when discovery revealed amount in controversy not satisfied). In *Tongkook*, a clothing manufacturer brought a breach of contract claim against one of its distributors, initially alleging damages of more than $100,000. *Id.* at 782. During discovery, however, the parties determined that the actual amount in controversy was below the statutory threshold. *Id.* at 785. The district court concluded that jurisdiction was proper because the parties believed that the dispute exceeded the threshold amount at the time of filing. *Id.* at 783. On appeal, the Second Circuit reversed, holding that because discovery revealed that the claim was for less than the jurisdictional amount, "Tongkook could not properly claim the required statutory jurisdictional amount, and this was true when the action was commenced . . . ." *Id.* at 785.

[65] *See Tongkook*, 14 F.3d at 785 (distinguishing fact pattern in *Deutsch* from fact pattern in *Tongkook*).

[66] *See Deutsch*, 359 F.2d at 100 (asserting unliquidated damages difficult for judge to quantify).

[67] *See id.* (reasoning "to allow a district court judge to value a plaintiff's claim in a case which involves a demand for unliquidated damages and in which the jurisdictional issue is inextricably bound up with the merits of the controversy is tantamount to depriving the plaintiff of his present statutory right to a jury trial").

parties ascertain the actual amount of damages incurred prior to trial, however, courts will dismiss because the plaintiff's claim never could have exceeded the statutory threshold.[68] Thus, while a court following the minority approach will look only to the plaintiff's claim to determine whether it exceeds the statutory amount, it will still dismiss the case for lack of jurisdiction if the pre-trial record demonstrates that the amount is not satisfied.[69]

B. The Majority Approach

Under the majority approach, federal courts look beyond the pleadings and instead focus more closely on the underlying cause of action to determine if the amount in controversy indeed exceeds the statutory threshold.[70] The conservative nature of this approach emerged in *City of Boulder v. Snyder*.[71] The plaintiff in *Snyder* sought damages against the City of Boulder, Colorado for the governmental taking of certain water rights caused by a street-paving project.[72] The plaintiff sought damages of $25,000 in her complaint, and the district judge held diversity jurisdiction to be proper.[73] At trial, the plaintiff testified to damages of $13,500, but five expert witnesses testified that her damages were significantly less than this amount.[74] On appeal from a judgment in favor of the plaintiff, the Tenth Circuit reversed and remanded to the district court to dismiss on the grounds that, in light of the testimony at trial, the plaintiff never could have recovered above the threshold amount.[75]

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[68] *See Tongkook*, 14 F.3d at 785 (discussing reasoning for dismissal on grounds of lack of jurisdiction).

[69] *Id.* (stating determination of amount below statutory requirement during discovery justified dismissal).

[70] *See, e.g.*, Pratt Cent. Park Ltd. P'ship v. Dames & Moore, Inc., 60 F.3d 350, 354 (7th Cir. 1995) (dismissing claim where contractual provision limited recovery below statutory threshold); Jimenez-Puig v. Avis Rent-A-Car Sys., 574 F.2d 37, 40 (1st Cir. 1978) (finding no basis for punitive damages claimed and therefore amount in controversy not satisfied); City of Boulder v. Snyder, 396 F.2d 853, 857 (10th Cir. 1968) (dismissing for lack of jurisdiction when expert testimony at trial suggested action did not exceed statutory amount).

[71] 396 F.2d 853, 857 (10th Cir. 1968) (holding jurisdiction improper when evidence at trial demonstrated potential recovery below threshold amount).

[72] *See id.* at 855 (discussing nature of taking claim). The paving project extended in front of the plaintiff's residence, and caused the destruction of a waterway that abutted and served her property. *Id.* Several others similarly situated joined the plaintiff, alleging the same damages. *Id.*

[73] *See id.* (finding jurisdiction based on plaintiff's good faith claim).

[74] *Id.* at 856 (detailing testimony of witnesses of damages). While the opinions of the experts differed as to the amount of actual damages, the highest opinion assessed the total damages suffered by the plaintiffs at $3000. *Id.*

[75] *See id.* at 857 (remanding with instructions to dismiss for want of jurisdiction).

The *Snyder* case is representative of the majority trend of rigorously analyzing diversity cases to determine whether federal jurisdiction is proper.[76] Courts following the majority approach consider affirmative defenses to a plaintiff's claims, other defenses stated in a plaintiff's complaint, and statutory or contractual limitations to recovery.[77] Moreover, even when a case goes to trial, these federal courts are more likely to continue to examine rigorously a plaintiff's claims, and to dismiss if the evidence indicates that the amount in controversy could not have satisfied the jurisdictional threshold at the commencement of the action.[78]

C. The Irreconcilability of the Minority and Majority Approaches: An Illustration

The Second Circuit case *Zacharia v. Harbor Island Spa, Inc.*[79] and the Ninth Circuit case *Pachinger v. MGM Grand Hotel-Las Vegas*[80] illustrate the incompatibility of the majority and minority views. These cases both involved a breach of contract claim in which state law expressly limited the recovery to an amount below the jurisdictional threshold.[81] In *Zacharia*, the plaintiff sued the Harbor Island Spa Hotel in federal court when valuables were stolen from one of the hotel safety deposit boxes that she had rented.[82] When she rented the box, however, she had signed a "Statement of Value" card which stated that the renter waived "any claim against said hotel, its agents, servants and employees, in excess of One Thousand ($1,000.00) Dollars".[83] The district court, relying on this

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[76] *See id.* at 856 (analyzing witness testimony as basis for dismissal for lack of subject matter jurisdiction).

[77] *See, e.g.*, Delvecchio v. Conseco, Inc., 230 F.3d 974, 980 (7th Cir. 2000) (dismissing on grounds that ratio of punitive damages to actual damages was excessive); Adams v. Reliance Standard Life Ins. Co., 225 F.3d 1179, 1182 (10th Cir. 2000) (asserting "open-ended prayer for recovery . . . is not an allegation that diversity jurisdiction exists"); Rexford Rand Corp. v. Ancel, 58 F.3d 1215, 1218 (7th Cir. 1995) (holding plaintiff must have "competent proof" to justify diversity jurisdiction).

[78] *See* Jiminez-Puig v. Avis Rent-A-Car Sys., 574 F.2d 37, 40 (1st Cir. 1978) (holding jurisdiction improper when plaintiff's claim, objectively viewed, could not exceed jurisdictional amount).

[79] 684 F.2d 199 (2d Cir. 1982).

[80] 802 F.2d 362 (9th Cir. 1986).

[81] *See Pachinger*, 802 F.2d at 365 (involving statutory limitation on recovery of $750); *Zacharia*, 684 F.2d at 202 (involving statutory limitation on recovery of $1000). In both cases, the petitioners were challenging the validity of the contractual provisions limiting the liability of the respondents. *See Pachinger*, 802 F.2d at 365; *Zacharia*, 684 F.2d at 202.

[82] *Zacharia*, 684 F.2d at 200-01 (discussing facts of case).

[83] *Id.* at 201 n.1 (outlining terms of safe deposit box agreement).

contract provision, dismissed *sua sponte* for want of jurisdiction.[84] On appeal, the Second Circuit reversed, holding that a district judge could not consider a defense on the merits in determining if the cause of action exceeded the statutory threshold and remanded the case to the lower federal court.[85]

The facts of the *Pachinger* case were remarkably similar to the facts of *Zacharia*, yet the court reached a contrary result.[86] In *Pachinger*, the plaintiff, a jewelry salesman, gave some jewelry to the bellhop at the MGM Grand Hotel-Las Vegas to place in a safe deposit box.[87] The bellhop, in exchange, gave him a claim check which stated that MGM's liability was limited to $250.[88] Some of the jewelry disappeared and Pachinger brought a diversity action against the hotel alleging the missing jewelry had a value of $19,000.[89] The hotel moved to dismiss on the grounds that Nevada state law, which controlled the action, limited MGM's liability to $750, which was well below the statutory threshold for diversity jurisdiction.[90] Agreeing with MGM that the statute limited Pachinger's recovery to $750, the district judge dismissed the case, and the Ninth Circuit affirmed on the same grounds.[91]

III. A PROPOSAL FOR SOLVING THE CURRENT CIRCUIT COURT SPLIT

The pro-plaintiff minority approach and the more stringent majority approach are inconsistent and irreconcilable.[92] There is, however, a relatively modest compromise that could end the split among the circuits while still ensuring that the *Red Cab* standard remains the starting point in all federal diversity cases. This Note proposes a solution based on a two-part analysis: first, a determination of whether the plaintiff's claim, *viewed*

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[84] *See id.* at 202 (dismissing on grounds that liability was limited by statute to $1000).

[85] *See id.* at 203 (declining to consider state statutory limitation on recovery in amount in controversy determination).

[86] *See Pachinger*, 802 F.2d at 365 (dismissing for lack of jurisdiction because statute limited recovery to $750).

[87] *Id.* at 363 (outlining facts of case).

[88] *Id.* (detailing limitation of liability in hotel claim check).

[89] *Id.* (discussing plaintiff's claim for damages). In 1986, the amount in controversy requirement for diversity jurisdiction was $10,000. Act of July 25, 1958, 72 Stat. 415.

[90] *Pachinger*, 802 F.2d at 363 (discussing Nevada statute that limited innkeeper liability to $750).

[91] *See id.* at 365 (affirming district court dismissal for lack of diversity jurisdiction because amount in controversy not satisfied).

[92] *See supra* Part II(C) (demonstrating inconsistency of circuit split).

objectively, is for an amount that could exceed the jurisdictional threshold; and second, whether satisfaction of the jurisdictional amount depends on the enforceability of a state statutory or contractual limitation on recovery.[93]

The first part of the analysis is a relatively straightforward application of the *Red Cab* standard: whether the plaintiff's good faith claim is for an amount that *could* exceed the statutory threshold.[94] Consistent with the "legal certainty" test, this initial analysis should be fairly liberal, allowing a plaintiff access to federal courts so long as it appears possible that he could recover an amount that exceeds the jurisdictional threshold.[95] The notice pleading system under which our judicial system operates warrants a liberal application of this standard.[96]

Presumably, courts that apply the majority approach initially might object to this liberal approach as opening the federal courts to numerous trivial claims, thus overloading the federal courts' dockets.[97] This concern, while warranted, is alleviated somewhat by the provisions of the diversity statute allowing for the denial of costs to plaintiffs who recover less than the jurisdictional amount.[98] Moreover, the statute also grants federal courts the discretion to impose costs on plaintiffs in such cases.[99] With this

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[93] *See Pachinger*, 802 F.2d at 363 (dismissing case where outcome depended on enforceability of state statutory limitation); *see also Zacharia*, 684 F.2d at 202 (holding jurisdiction proper even though dispute grounded in enforceability of state statute).

[94] *See* St. Paul Mercury Indem. Co. v. Red Cab Co., 303 U.S. 283, 289 (1938) (explaining "legal certainty" test).

[95] *See id.* at 288-89 (asserting that "sum of plaintiff controls if the claim is apparently made in good faith"); *see also* CHARLES ALAN WRIGHT & ARTHUR R. MILLER, FEDERAL PRACTICE & PROCEDURE § 3702 (3d ed. 1998) ("[E]ven when the complaint discloses a valid defense to the plaintiff's action, the sum claimed by the plaintiff controls, since the defendant may not assert that defense or may not ultimately prevail on it.").

[96] *See* FED. R. CIV. P. 8 (outlining notice pleading requirements); *see also Red Cab*, 303 U.S. at 289 (noting that courts should determine jurisdictional amount "from the face of the pleadings").

[97] *See* Pratt Cent. Park Ltd. P'ship v. Dames & Moore, Inc., 60 F.3d 350, 352 (7th Cir. 1995) (stressing liberal standard would "attract new claimants for the limited time and resources of the federal bench").

[98] *See* 28 U.S.C. § 1332(b) (2005). This provision of the statute reads as follows:

> Except when express provision therefor is otherwise made in a statute of the United States, where the plaintiff who files the case originally in the Federal courts is finally adjudged to be entitled to recover less than the sum or value of $75,000, computed without regard to any setoff or counterclaim to which the defendant may be adjudged to be entitled, and exclusive of interest and costs, the district court may deny costs to the plaintiff and, in addition, may impose costs on the plaintiff.

28 U.S.C. § 1332(b) (2006).

[99] *See id.* (granting district court authority to deny costs to plaintiff or impose costs on

potential for additional costs, plaintiffs presumably will be hesitant to bring a diversity action where the amount sought is uncertain or unlikely to exceed the jurisdictional threshold.[100]

Moreover, the initial liberal analysis applies only to those actions which assert a claim that, *viewed objectively*, could exceed the statutory amount.[101] To be sure, many lawsuits brought in diversity do not satisfy this objective standard.[102] For these more questionable cases, the analysis should proceed a step further to determine the nature of the underlying claim.[103] Such a situation arises in cases like *Pachinger* and *Zacharia*, where the determination of whether the lawsuit exceeds the amount in controversy depends on the court's determination at trial of the enforceability of a state statutory or contractual limitation on damages.[104] In such cases, federal courts should dismiss these causes of action for lack of jurisdiction, notwithstanding whether the court might find the statutory or contractual limitation unenforceable.[105] Rather than try to predict whether a particular state's highest court would find the limitation on damages enforceable or unenforceable, a sound solution in such a case is to dismiss for lack of jurisdiction, and let the parties litigate the action in state court.[106] The resulting state court ruling would then guide federal courts sitting in diversity in the future.[107]

While this two-part analysis potentially would solve the inconsistencies in cases involving the enforceability of state statutory or contractual limitations, there remains the question as to what extent federal courts should consider other affirmative defenses raised in the pleadings.[108]

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plaintiff).

[100] *See* Jordan F. Miller Corp. v. Mid-Continent Aircraft Serv., Inc., 1999 WL 164955, at *3 (10th Cir. March 24, 1999) ("We recognize that the legislative history of § 1332(b) demonstrates an intent to deter plaintiffs from filing cases in federal court when the amount in controversy is, or is likely to be, less than the jurisdictional amount.").

[101] *See supra* notes 46-47 and accompanying text (discussing "legal certainty" test).

[102] *See supra* notes 32-41 and accompanying text (describing difficulty in determining whether jurisdictional amount satisfied at outset of litigation).

[103] *See infra* notes 105-115 and accompanying text (explaining proposed two-fold analysis for determining whether amount in controversy satisfied).

[104] *See supra* notes 79-91 and accompanying text.

[105] *See* Pratt Cent. Park Ltd. P'ship v. Dames & Moore, Inc., 60 F.3d 350, 353 (7th Cir. 1995) (asserting "district judge possesses the power to eject a case when a contract holds damages below the jurisdictional amount").

[106] *See* Crawford v. Martin Marietta Corp., 622 F.2d 339, 341 (8th Cir. 1980) (". . . Federal courts are not to overrule settled state law and predict that a state court would do so without strong indications from the state itself.").

[107] *See id.* (asserting state court should decide whether to overrule settled state court precedent).

[108] *See supra* note 56 and accompanying text (describing varying approaches to whether courts should consider affirmative defenses in pleadings when determining jurisdictional

In such cases, this Note proposes that federal courts should analyze the plaintiff's claim solely under the *Red Cab* "legal certainty" test, and not look to potential affirmative defenses.[109] This Note argues that this rule should apply even if the plaintiff asserts the existence of a potential affirmative defense in his complaint.[110]

One rationale for federal courts sitting in diversity to disregard these affirmative defenses in determining whether subject matter jurisdiction is present is that many affirmative defenses are waiveable.[111] As such, a court cannot determine from the initial filing of the complaint whether the defendant will plead the defense in its answer.[112] Moreover, and perhaps a more practical rationale for this approach, is that the mere existence of an affirmative defense, either in a complaint or an answer, does not guarantee that the plaintiff's claim will fail.[113] Indeed, as one circuit court noted, if such defenses were considered in determining the jurisdictional amount, "doubt and ambiguity would surround the jurisdictional base of most diversity litigation from complaint to final judgment, and issues going to a federal court's power to decide would be hopelessly confused with the merits themselves."[114] Thus, to consider these affirmative defenses in determining whether the jurisdictional threshold has been met would violate the *Red Cab* principle that the value of the claim must be ascertained "from the face of the pleadings."[115]

CONCLUSION

The limited jurisdiction of federal courts is a central component of the American judicial system, and thus courts should scrutinize closely assertions of and challenges to subject matter jurisdiction. Nevertheless, the murkiness surrounding diversity jurisdiction and the amount in

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amount).

[109] *See* Scherer v. Equitable Life Assurance Soc'y of the U.S., 347 F.3d 394, 397 (2d Cir. 2003) (asserting "affirmative defenses . . . on the merits may not be used to whittle down the amount in controversy" (internal quotations omitted)).

[110] *See* St. Paul Mercury Indem. Co. v. Red Cab Co., 303 U.S. 283, 288-89 (1938) ("Nor does the fact that the complaint discloses the existence of a valid defense [defeat jurisdiction].").

[111] *See Scherer*, 347 F.3d at 399 (holding use of res judicata to reduce amount in controversy impermissible because defense waivable).

[112] *See* Pratt Central Park Ltd. P'Ship v. Dames & Moore, Inc., 60 F.3d 350, 354 (7th Cir. 1995) (Flaum, J., dissenting) ("yet the fact of a defense, and a good defense, too, would not affect the question as to what was the amount in dispute").

[113] *See supra* note 95 and accompanying text.

[114] Zacharia v. Harbor Island Spa, Inc., 684 F.2d 199, 202 (2d Cir. 1982).

[115] *See Red Cab*, 303 U.S. at 289 (holding amount in controversy determined on basis of pleadings).

controversy requirement can often cloud the jurisdictional question. To that end, clear guidelines and uniformity in their application among the circuits is necessary to ensure consistency in diversity jurisdiction determinations. Adopting the analytical approach proposed in this Note is one step toward ensuring consistency among the circuits, and potentially could resolve the current split regarding the limits of diversity jurisdiction. A more consistent application of these principles would make jurisdictional determinations more predictable for the federal bar, and would encourage attorneys to analyze rigorously the grounds for diversity jurisdiction before filing a case in federal court.

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