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Federal Court Allows Lloyd's Underwriters to Bring Class Action to Establish Diversity Jurisdiction

In a case of first impression involving the Class Action Fairness Act of 2005 ("CAFA"), the U.S. District Court for the Southern District of New York has allowed Certain Underwriters at Lloyd's, London and London Market Insurance Companies to cure a jurisdictional defect in their declaratory judgment action by restructuring their lawsuit as a class action. Judge Loretta Preska's ruling may open the door to other federal class actions on behalf of Lloyd's Underwriters, providing another avenue for London insurers to establish diversity jurisdiction to litigate state law claims in federal court where the citizenship of one or more Lloyd's syndicate members is not diverse from an adversary. Even where a class action is not available, London insurers may be able to maintain state law claims in federal court by excluding from the suit individual syndicate members whose presence would destroy diversity. Lewis Baach appeared in the case for the Lloyd's Underwriters and London Market Companies after defendants moved to dismiss, and cross-moved for leave to file an amended complaint asserting jurisdiction under CAFA.

The London insurers commenced the suit in 2009 against other excess insurers of a New York City construction project, for which the excess limits total $25 million. The London insurers include 1217 individual members, or Names, of the Atrium Syndicate. In 2011 it was discovered that two Atrium Names were New York residents and thus not diverse with certain defendants; and that none of the Atrium Names individually met the $75,000 amount in controversy needed for diversity jurisdiction. Two defendants, the Insurance Company of the State of Pennsylvania ("ICSOP") and Continental Casualty Company ("Continental"), then moved to dismiss on the grounds that the Atrium Names who destroyed diversity jurisdiction were indispensable parties.

The London insurers argued that the Atrium Names were not indispensable, and moved to amend their complaint to drop the non-diverse Names as named parties and, if necessary, proceed as a class action under CAFA. CAFA does not require all class members to have diverse citizenship from all defendants, and it applies an aggregated amount in controversy threshold of $5 million. In this week's ruling, Judge Preska allowed the London insurers to file their amended complaint asserting claims as a class action.

The court first observed that it could drop non-diverse parties so long as they were not indispensable to the action, and rejected the notion that the Atrium Names were indispensable simply because they subscribed to the insurance contracts at issue. Rather, the court applied a four-prong test under the Federal Rules of Civil Procedure: whether the absence of a party would prejudice that party or other litigants; whether such prejudice could be lessened or avoided; whether an adequate judgment could be obtained without the party; and whether the plaintiffs would have an adequate remedy if the federal action were dismissed.

Applying those factors, the court concluded that the Atrium Names were not indispensable. It found that they would not be prejudiced since the Atrium Names themselves sought to be dropped from the case, that any dropped plaintiff could sue in state court to vindicate its rights, and that the prospect that defendants would be prejudiced by multiple proceedings is "remote and minor." The court also found that the remaining London insurers could obtain an adequate judgment: a declaration of rights as to their several shares of the policies at issue. Although the court acknowledged that London insurers could pursue an alternative remedy in state court, that factor was not determinative.

While not finding the Atrium Names to be indispensable, the court nonetheless remedied the jurisdictional defects not by dropping them from the case altogether but allowing London insurers to amend the complaint such that the Atrium Names would not be named plaintiffs but would be part of a class of subscribers to the policies. The class meets CAFA's jurisdictional requirements because there is "minimal" diversity of citizenship – at least some class members are diverse from the defendants – and the aggregated amount in controversy satisfies the $5 million threshold. The court also found that the class satisfies the four class action requirements under the Federal Rules of Civil Procedure: (1) the class of more than 1200 members is sufficiently numerous; and because each class member's claim is essentially identical (2) there are questions of law or fact common to the class; (3) the class representatives' claims are typical of the class; and (4) the representatives will fairly represent the interests of the class.

Judge Preska's decision thus approves a new way for London insurers to establish federal jurisdiction for state law claims in appropriate cases: the formation of a class consisting of subscribers of the insurance contracts at issue. If a class action is not available – for instance, if class membership is not sufficiently numerous or the aggregated amount in controversy is less than $5 million – the ruling also provides a basis to argue that Lloyd's Names who would destroy diversity jurisdiction could be left out of the suit and not be deemed "indispensable."

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