

# CAFA: Seventh Circuit's Interpretation of the Home-State Controversy Exception

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## The Takeaway

The Seventh Circuit has again clarified the home-state controversy exception to federal court jurisdiction under the Class Action Fairness Act (CAFA), holding that one non-resident individual defendant among nearly 50 individuals does not support federal diversity jurisdiction. The court also found the rare internal-affairs exception to CAFA removal required remand.

Class action defendants should be aware of these exceptions as class plaintiffs may attempt to avoid removal by pleading themselves within the exceptions.

## Case Background

Plaintiffs, who are policyholder members of defendant Country Mutual, filed a class action in St. Clair County, Illinois (*Sudholt v. Country Mutual Insurance Co. et al.*), naming the insurance company and 46 directors and officers. They alleged that the insurer retained excess surplus of over \$3.5 billion in profits resulting from premium revenues exceeding the cost of claims. Plaintiffs attributed the excess accumulation to Country Mutual's directors and officers seeking to enrich themselves with excessive compensation and benefits in violation of their fiduciary duties. They asserted claims against Country Mutual for breach of contract, unjust enrichment, and violation of the Illinois Consumer Fraud and Deceptive Business Practices Act (ICFA). Plaintiffs also alleged breach of fiduciary duty claims against the individual officers and directors. Forty-five of the individual defendants are citizens of Illinois, and one, Robert Bateman, is a citizen of Massachusetts.

Country Mutual invoked CAFA and removed the case to the United States District Court for the Southern District of Illinois based on the size of the putative class, the amount in controversy, and the minimal diversity created by Mr. Bateman's Massachusetts citizenship. The plaintiffs then moved to remand the case, arguing that the action satisfied exceptions supplied by CAFA: the home-state controversy exception in 28 U.S.C. § 1332(d)(4)(B) and the internal-affairs exception in § 1332(d)(9)(B).

Regarding the home-state controversy exception, the district court concluded that plaintiffs targeted not only Country Mutual but also Mr. Bateman as a "primary defendant." Because Mr. Bateman was not a citizen of Illinois, where the action was filed, the class action did not qualify as a home-state controversy, making jurisdiction proper in federal court. The district court therefore denied Plaintiffs' motion to remand.

## Analysis of Appellate Court Ruling

On appeal, the Seventh Circuit reversed the district court's ruling, holding that the home-state controversy exception applies. Under this exception, a district court "shall decline to exercise jurisdiction" when "two thirds or more of the members of all proposed plaintiff classes are in the aggregate, and the primary defendants, are citizens of the State in which the action was originally filed." 28 U.S.C § 1332(d)(4)(B).

Country Mutual contended that Mr. Bateman is a "primary defendant" within the meaning of the home-state controversy exception. Noting that Congress left the term undefined, the Seventh Circuit observed that the plain import of "primary defendant" required identifying the "gravamen of the complaint." The Seventh Circuit saw the inquiry as one requiring an assessment of the plaintiffs' complaint as a whole, with an eye toward examining whether the defendant in question, Mr. Bateman, is a principal focus of the class action.

Given that Plaintiffs' complaint focused primarily on Country Mutual, which allegedly retained over \$3.5 billion in excess surplus, the Court of Appeals identified it as the main target. While this observation did not make Country Mutual the *only* "primary defendant," the Court noted that when considering the plain objective of the action, it did not see the 46 directors and officers as equal defendants alongside Country Mutual.

The complaint identified Mr. Bateman as the company's chief financial officer for two years of the decade-long surplus accumulation. It lacked allegations that he played a particular or significant role in the complained-of conduct. As nothing differentiated Mr. Bateman from the other 46 director and officer defendants, the Seventh Circuit held that he was not a "primary defendant" within the meaning of the home-state controversy exception and reversed the district court's ruling with instructions to remand the case to state court.

Additionally, the Seventh Circuit held that the class action fits within the internal-affairs exception to CAFA, which also mandated a remand to state court. Under this exception, federal jurisdiction otherwise supplied by CAFA does not apply to class actions solely involving claims relating to the internal affairs or governance of a business entity and arising under the laws of the state where such business is incorporated or organized. The Court reasoned that Plaintiffs' complaint "solely involved" claims that root themselves in contentions that directors and officers benefited themselves and harmed policyholders in their exercise of discretion to set capital levels and determine dividend distributions.

**Tags:** CAFA, Class Action Fairness Act, Federal Jurisdiction, Home-State Controversy Exception to CAFA, Internal-Affairs Exception to CAFA