

QUESTION 4

Buyer, who was living in New York, and Seller, who was living in California, entered into a valid contract, agreeing to buy and sell a painting claimed to be an original Rothko, supposedly worth \$1 million, for that amount. In a separate valid contract, Buyer agreed to buy from Seller a parcel of California real property worth \$5 million, for that amount. Buyer and Seller completed the purchase of the painting on June 1; they were to complete the purchase of the real property on June 30.

On June 15, Buyer resold the painting, but obtained only \$200, because the painting turned out to be a fake. Buyer promptly notified Seller of his intent to sue Seller for damages of \$1 million. Seller then informed Buyer that Seller would not go through with the purchase of the real property.

Buyer filed suit against Seller in federal court in California. Buyer claimed fraud as to the painting, alleging only that Seller committed “fraud in the supposed value,” and sought \$1 million in damages. Buyer also claimed breach of contract as to the real property, and sought specific performance. Buyer demanded trial by jury on all issues.

1. May Buyer join claims for fraud and breach of contract in the same suit against Seller? Discuss.
2. Is Buyer’s allegation sufficient to state a claim for fraud involving the painting? Discuss.
3. Does the federal court have subject matter jurisdiction over the suit? Discuss.
4. May the federal court apply California law to decide the breach of contract claim involving the real property? Discuss.
5. On what issues, if any, would Buyer be entitled to a jury trial? Discuss.

QUESTION 4: SELECTED ANSWER A

1. JOINDER OF CLAIMS

Joinder of Claims

Generally, a plaintiff may bring any number of claims against the same defendant, even if they are unrelated or do not have a common nucleus of operative fact, in the same action. If the claims are brought in federal court, at least one of the claims must satisfy the requirements of subject matter jurisdiction.

Here, both the fraud claim with respect to the Rothko painting and the breach-of-contract claim with respect to the real property are being brought by the same plaintiff, Buyer (B), against the same defendant, Seller (S). Therefore, the two claims may be joined, and they may be brought in federal court if one of them satisfies subject matter jurisdiction. (The issue of subject matter is discussed below, in Part 3.)

Abstention

If a state law claim is joined to another claim, the federal court asked to hear those claims may abstain from hearing the state law claim, sever it, and remand it to a state court if the interest of the state in resolving the questions of law that are at issue are particularly high. There is a high threshold for abstention, such as in *Pullman* abstention, where a federal court will decline to address a constitutional question whose adjudication depends on the resolution of an unresolved issue of state law.

Here, the two claims, both based on state law, are for fraud and breach of contract. These are fairly common and ordinary common law (or possibly statutory) causes of action. Neither New York nor California would have a particularly strong interest in

divesting the federal court of the case, since the law is mostly, if not entirely in this case, resolved. Therefore, joinder will survive any abstention challenge, and neither claim will be subject to severance and remand.

Conclusion

The claims may be joined in the same suit.

2. SUFFICIENCY OF PLEADING

Well-Pleaded Complaint

To survive a Rule 12(b)(6) motion to dismiss for failure to state a claim on which relief can be granted, the pleading in a complaint must allege enough facts to give the defendant notice of the cause of action and the facts on which the claim is based. Under *Twombly* and *Iqbal*, a federal court must apply a two-part test to determine whether a complaint is sufficiently well-pleaded. First, the court strikes all conclusory legal allegations. Second, taking all remaining factual allegations as true, the court determines whether the facts as alleged would make it plausible for the plaintiff to succeed in obtaining the relief that is sought.

Here, B's complaint with respect to the Rothko painting alleged only that S committed "fraud in the supposed value." This pleading most likely fails the *Twombly-Iqbal* test. With respect to the first step, the pleading is essentially entirely a conclusory legal allegation. The complaint states only that fraud relating to the value of the painting occurred. Strictly construing *Twombly-Iqbal*, the entire allegation must be stricken when applying the first step of the test. The second step may be applicable if the test were loosely construed, and the court took the phrase "supposed value" to mean that fraud can be proved based on the fact that the painting's value as stated by S was false. But falsity alone does not give rise to an action for fraud. Fraud requires intentional, knowing, or reckless conduct with respect to a falsity. Thus, the pleading must allege,

in addition to the existence of a falsity, some indication of fault on S's part. Because it fails to do so, it is not well-pleaded.

Fraud Pleadings

For claims of fraud, the Federal Rules require fact-pleading, rather than the notice-pleading permitted by *Conley*, and, to a lesser extent, *Twombly* and *Iqbal*. The plaintiff must allege specific facts that made the defendant's conduct fraudulent.

B's cause of action with respect to the painting is one of fraud, meaning that the fact-pleading standard applies. As discussed above, B did not allege specific facts that demonstrate fraud. To meet the required level of specificity, B should have at least alleged that 1) S represented to B that the painting was a genuine Rothko, 2) that the painting was not a genuine Rothko, 3) that S had requisite mental state required for fraud, and 4) that the painting was not worth the value that S placed on it, and which B paid. Because the pleading did not allege any of these things, even if B can successfully defend his complaint from a notice/plausibility-pleading challenge, the complaint will not survive a fact-pleading challenge.

Conclusion

B's allegation is not sufficient to state a claim for fraud.

3. SUBJECT MATTER JURISDICTION

Federal Question Jurisdiction

Federal courts are courts of limited subject matter jurisdiction. Subject matter jurisdiction can be conferred on a federal court either through federal question jurisdiction or diversity jurisdiction. Federal question jurisdiction exists where the cause of action, as stated in the complaint, arise under a federal law or federal issue.

Here, B's claims are for fraud and breach of contract. Neither of these are federal claims, so the court does not have federal question jurisdiction.

Diversity Jurisdiction

Generally, diversity can confer subject matter jurisdiction on a federal court if 1) all plaintiffs are completely diverse from all defendants and 2) the amount-in-controversy exceeds \$75,000.

Complete Diversity

Complete diversity is measured at the time a lawsuit is filed, and exists if no plaintiff is a citizen of a state of which any defendant is a citizen. For individuals, the state of citizenship for diversity purposes is the state of domicile, i.e. the state wherein the individual resides and has expressed or demonstrated an intent to reside permanently.

Here, B lives in New York. Although he sought to purchase real property in California, it is unclear whether he intends to leave New York. At any rate, as of the time the suit was filed, B was domiciled in New York because he was residing there at the time and expressed no intent to leave. Meanwhile, S is domiciled in California because he lives there and no facts suggest that he is domiciled in any other state. Thus, B is a citizen of New York, and S is a citizen of California. Complete diversity exists between all plaintiffs (B) and all defendants (S).

Amount-in-Controversy

The amount-in-controversy must exceed \$75,000 in order for diversity jurisdiction to exist. This requirement is satisfied based on a good-faith pleading that the plaintiff is entitled to at least \$75,000 in damages. In addition, where the relief sought is an injunction or specific performance, the amount-in-controversy may be satisfied if the

court finds that the economic value of the requested relief exceeds \$75,000.

Here, both of B's claims against S satisfy the amount-in-controversy. The claim of fraud alleges damages of \$1,000,000. The allegation is in good faith because the painting that B bought was supposedly worth \$1,000,000, and B paid that much for it, to his loss of \$999,800. Meanwhile, although specific performances rather than a specific monetary amount is sought as a remedy in the breach-of-contract case, the property to be awarded to B if the claim is successful is worth \$5,000,000. Because both causes of action request relief that is worth well over \$75,000, the requirement is satisfied.

Aggregation of Claims

A plaintiff may aggregate multiple claims against the same defendant in order to satisfy the amount-in-controversy requirement.

Had either or both of his claims been worth less than \$75,000, B could have aggregated them in order to plead a total amount-in-controversy in excess of \$75,000. Of course, since both claims independently satisfy the requirement, this rule does not control.

Supplemental Jurisdiction

A court may exercise supplemental jurisdiction over a claim if it arises out of the same transaction or occurrence as a claim, between the same plaintiff and defendant, over which the court already has subject matter jurisdiction.

If one or the other of the two claims B is bringing against S failed to meet the requirements of diversity jurisdiction, B could still argue that the two claims arose out of the same transaction or occurrence. Although S would respond that the contracts for the painting and the real property were completely separate and occurred nearly a month apart, B might counter that the breach of the contract for the sale of real property was causally connected to B's discovery of the allegedly fraudulent sale of the painting.

Indeed, S only informed B that S would not go through with the sale of the property after B notified S of his intent to sue S for \$1,000,000. Both arguments are persuasive, so it is not clear what the result would be if the court were forced to decide the issue of supplemental jurisdiction. However, as analyzed above, the court need not decide this issue because each claim separately falls within the court's diversity jurisdiction.

Conclusion

The court has subject matter jurisdiction.

4. CHOICE-OF-LAW

Erie Doctrine

Generally, in diversity cases, the federal court applies state substantive law, based on the law of the state in which the court sits, and federal procedural law. First, the court must ask whether there is a conflict between state and federal law. If so, then the court must ask whether there is a federal statute or Federal Rule that addresses the issue. If such a federal statute exists, the court must apply it. If a Federal Rule addresses the issue, the court must ask whether the Rule expands, abridges, or modifies a substantive right. If so, then the court may only apply the Rule if its effect on the right is incidental. If there is no federal statute or Rule on point, the court must ask whether the failure to apply state law would change the outcome in the case. If so, then the court must apply the state law. Finally, if the inquiry reaches past this point, the court must consider the relative interests of the state and federal judiciaries in adjudicating the issue, as well as the need to dis-incentivize forum shopping.

That said, here the *Erie* analysis is simple. There is no conflict between state and federal law with respect to the breach-of-contract claim, because there is no federal law of contract. Moreover, the law of contract is inherently substantive. Therefore, because the court sits in California, *Erie* dictates that it should apply California substantive law to

resolve the claim.

Law of the Situs

The default choice-of-law for determining disputes over real property is to apply the choice-of-law (or the substantive law, if the choice-of-law is silent) of the state in which the property is located.

Based on this default rule, the federal court should apply California law to decide the breach-of-contract claim because the real property at issue is located in California.

Conclusion

The federal court may, and probably should, apply California law to decide the breach-of-contract claim.

5. JURY TRIAL

Right to Jury Trial

In federal cases, a plaintiff is entitled to a jury trial, per the Seventh Amendment of the Constitution, in any action at law. However, there is no entitlement to a jury trial in an equity action. Whether a case is one of law or equity is a purely federal question, and must be decided by the court according to federal law.

Here, the action for fraud is an action at law. The remedy sought is monetary damages amounting to \$1,000,000. Therefore, B is entitled to a jury trial on that claim. Meanwhile, the action for breach-of-contract is an action in equity, because the remedy sought is the equitable remedy of specific performance. If B amended the complaint such that, in the alternative to seeking specific performance, it requested money damages, then the action would be at least in part at law and therefore subject to his

right to a jury trial.

Conclusion

As pleaded, B is entitled to a jury trial on the fraud claim but is not entitled to one on the breach-of-contract claim.

QUESTION 4: SELECTED ANSWER B

Joinder of Buyer's Claims Against Seller

Joinder of claims in federal court is governed by the Federal Rules of Civil Procedure, regardless of whether or not the original claim was filed under diversity. This is because the FRCP are affirmative federal law under the Supreme Court's decision in *Hanna*, and they act to pre-empt any contravening state law, even if that state law is purely procedural and otherwise would govern under the Erie Doctrine.

Under the Federal Rules, a plaintiff may join any and all claims that he has against the defendant, regardless of whether or not they arise out of the same transaction or occurrence, a common nucleus of operative fact, or any other shared basis in law or fact. The plaintiff, in other words, is the master of his complaint. Here, the plaintiff has joined claims against this specific defendant. Regardless of whether or not they arise out of the same CNOOF they nevertheless satisfy the requirement for joinder of claims.

Sufficiency of Buyer's Allegation to State a Claim

Under Federal Rule 12(b)(6), which controls in a state law diversity action properly brought in federal court, the Supreme Court has held that a plaintiff must allege specific facts that operate to push the allegations over the line from speculative to plausible. This comes from the *Twombly and Iqbal* line of cases. This does not move the requirements for pleading from the traditional notice pleading requirement that only requires the plaintiff to provide a short and plain statement of the allegation to fact pleading requiring a detailed list of all facts in the case that make the claim likely to survive, which is what is required under California. Again, what is required to survive a Rule 12(b)(6) motion to dismiss for failure to state a claim upon which relief can be granted is that the complaint does not allege sufficient facts to make the allegation of fraud plausible.

Fraud Requirements

In determining whether or not sufficient allegations exist to find that there was fraud in a contract, a federal court sitting in diversity in California will apply California law. In California, the common law of contracts applies. Fraud in contract requires that the plaintiff 1) knowingly 2) misrepresent 3) a material term in the contract.

12(b)(6) Analysis

Here, the facts demonstrate that the painting was claimed to be an original Rothko, supposedly worth \$1 million, which the Buyer bought for \$1 million. However, the Seller will argue in his 12(b)(6) motion that the complaint does not state factual allegations that tend to show that the plaintiff knew that the Rothko painting was a fake, nor even that if he did represent the Rothko as an original, that he had any reason to suspect it was false. Unless the Buyer is able to amend his complaint, which he is eligible to do once as of right within 21 days of the service of a motion to dismiss (or, under California law, before an answer is served) to allege facts with sufficient specificity that a reasonable finder of fact could conclude that the allegations were plausible, then the Buyer's allegation is likely not sufficient to state a claim for fraud involving the painting.

Subject Matter Jurisdiction

Federal courts are courts of limited subject matter jurisdiction. Unlike California state courts, which may hear any claims that are brought before it subject to other limits (including personal jurisdiction), there must be an affirmative grant of federal subject matter jurisdiction that allows for each claim to be properly heard.

Federal Question Jurisdiction

Federal courts have jurisdiction over any claim that arises under the Constitution, statutes, or treaties of the United States. Furthermore, they also have federal question jurisdiction where either there is an important federal interest at stake that effectively supersedes state law (such as in the foreign relations domain) through the application of the modern federal common law, as well as in state law questions that require the interpretation of federal law under the *Merrell Dow* and *Grable* doctrine.

In this case, the court is adjudicating claims of fraud and breach of an obligation to purchase real property. These are not federal questions; they do not arise under federal positive law, federal common law, nor do they contain substantial federal questions that must be answered in order to resolve state law claims. Therefore, there is no federal question jurisdiction over either claim.

Diversity Jurisdiction

In order for there to be diversity jurisdiction over a state law claim, the claim must both satisfy the diversity requirements and the amount-in-controversy requirement. Multiple claims can be aggregated in order to satisfy the amount in controversy requirement. I first consider diversity; then move on to the amount-in-controversy for each claim.

Diversity

Under a standard state law claim brought in diversity jurisdiction, there must be complete (so-called "*Strawbridge*") diversity between all plaintiffs and defendants. Each plaintiff must be a citizen of a separate state from each defendant. Citizenship for individuals, which is the fact pattern in question here, is determined by domicile, which is where a person resides with intent to remain. The facts state that Buyer lives in New York, and Seller lives in California. There are no other parties to the suit. Assuming that both Buyer and Seller intend to remain in their states indefinitely and are therefore citizens of separate states, the requirement of complete diversity is satisfied.

Amount-in-Controversy

In order for diversity jurisdiction to exist over state law claims, the total amount in controversy must exceed \$75,000. A plaintiff may aggregate all the claims that they have, even unrelated claims, to satisfy the amount in controversy requirement against the defendant. The amount-in-controversy claimed must have been arrived at in good faith, though it does not need to be precise.

Here, the amount in controversy substantially exceeds \$75,000. The Buyer, in his fraud action, is alleging in good faith that he expected to receive a painting valued at \$1

million dollars but instead received a painting valued at only \$200 due to the defendant's fraud. That is a difference of \$999,800, well over \$75,000, and that would be the plaintiff's recovery in expectation damages. And the real estate property in question is valued at \$5 million, alleged in good faith, and given that the title to that property is in dispute, the amount in controversy requirement there is also satisfied. Therefore, independently and together, the plaintiff has properly alleged an amount in controversy in excess of the federal requirement for diversity jurisdiction.

Therefore, the federal court has subject matter jurisdiction over these claims through diversity.

Supplemental Jurisdiction

Supplemental jurisdiction allows a state law claim that does not otherwise have jurisdiction to be attached to a federal claim that has subject matter jurisdiction. This is so-called pendent party or ancillary jurisdiction. Here, both state law claims together and independently meet the requirements for diversity jurisdiction, so supplemental jurisdiction does not apply.

Application of California Law to Decide Breach of Contract Claim

Erie

Under the Erie doctrine, there is no general or federal common law. A court sitting in diversity instead applies the substantive law of the state in which it sits, including choice-of-law law, in order to decide questions of law. A federal court sitting in California should apply California law to decide what law to apply.

California Choice of Law

The federal law should therefore apply California choice-of-law law to decide what substantive law to apply. California choice-of-law law for real property in state court requires that a California court use the law of the jurisdiction in which the property is located (as opposed to a contract, where the court will determine whether or not the contract itself has a choice-of-law provision - if that choice-of-law provision is not

contrary to public policy, it will apply it. If the choice-of-law provision is contrary to public policy or there is no choice-of-law provision, the California court will apply a governmental interest analysis to determine what law to apply. That analysis essentially queries the relative interests of the governments in question in order to decide what law to apply.)

Real Property

Here, because the situs of the property in question is located in California, a California court would apply its choice-of-law law to use California substantive law to adjudicate the claim as to the real property contract, unless there is a choice-of-law provision in the land sale contract that requires the application of the law of a different state. However, this fact pattern does not suggest any such choice-of-law provision, and so I do not assess this any further.

Contract

In the event, that the choice-of-law question is adjudicated according to contract principles, a federal court applying California choice-of-law law should proceed to balance the interest of the governments in having their law apply. The two states whose laws are implicated here are California and New York. California has an interest in protecting its citizens from claims of fraudulent sales; New York has an interest in protecting its citizens from fraudulent sales. These are relatively equal interests. However, the Buyer filed in California, which may indicate his willingness to have California law applied; the painting was also with the seller in California at the time the alleged contract was signed and fraud committed. These weigh in favor of imposing California law.

Therefore, in either case, the federal court, properly applying California choice-of-law law, may apply California law to decide the claim.

Issues in Which Buyer is Entitled to Jury Trial

Traditionally, under the Erie Doctrine, procedural questions are decided under federal

law and substantive questions are decided under state law (unless the procedural dispute is outcome-determinative between filing in a state or federal court, in which case the state procedural law trumps federal law). However, questions of jury procedure are Constitutional in basis and therefore federal law always trumps state jury procedural law.

The Seventh Amendment to the Constitution guarantees a jury trial upon timely demand to litigants in questions of law. There is no right to a jury trial for questions of equity. While under the Federal Rules of Civil Procedure, actions are no longer brought exclusively in law or equity - there is instead only the "civil action" - the application of the right to a jury trial is determined by whether or not the cause of action contained in the complaint would have qualified for a jury trial in 1789.

Fraud and Damages: Remedy at Law

Damages are a remedy at law. Therefore, the Buyer is entitled, upon timely demand, to a jury trial on the issue of damages (provided that the claim survives the various hurdles earlier laid out).

Real Property and Specific Performance: Remedy at Equity

Specific performance is a version of an injunction, which is a remedy at equity. A litigant is not entitled to a jury trial on an issue of equity; it may instead be decided by a bench trial.

Mixed Issues of Law and Equity

When a complaint alleges both legal and equitable remedies and demands a jury trial, the court should separate the questions and hold a jury trial on the legal question first. It can then move to a bench trial on the equitable question.

Therefore, in this case, Buyer is entitled to a jury trial on the question of his damages in fraud. That should be held first; the court can then move to his demand for specific performance on the real estate contract.