St. John's Law Review

Volume 49, Winter 1975, Number 2 Article 14

Standard Established for Precluding Pendent Jurisdiction (Kavit v. A.L. Stamm & Co.)

Edgar J. Royce

Follow this and additional works at: https://scholarship.law.stjohns.edu/lawreview

This Note is brought to you for free and open access by the Journals at St. John's Law Scholarship Repository. It has been accepted for inclusion in St. John's Law Review by an authorized editor of St. John's Law Scholarship Repository. For more information, please contact selbyc@stjohns.edu.

exhaustion of state remedies before federal injunctive or declaratory relief could be obtained, a requirement which has been explicitly rejected in other circumstances.[52]

In *Salem Inn*, the Second Circuit resolved an issue left unanswered by the Supreme Court in *Younger*. By ruling that federal injunctive relief was proper where a state criminal proceeding was initiated subsequent to the commencement of the federal action, the court moved away from a strict interpretation of *Younger* and, instead, reaffirmed the important role federal courts should play in protecting constitutional rights. While the majority may have precipitated a race to the courthouses, far more importantly it insured that the federal courts will remain, in most instances, the prime protectors of federal rights.[53]

Stephen Fox

STANDARD ESTABLISHED FOR PRECLUDING PENDENT JURISDICTION

Kavit v. A. L. Stamm & Co.

Article III of the Constitution extends the subject matter jurisdiction of the federal courts to cases "arising under" the Constitution, laws or treaties of the United States.[1] Where a case presents a jurisdictionally sufficient federal question, access to the federal forum will also be available for all related claims, including those of a non-federal nature. This result is achieved through the doctrine of pendent jurisdiction, whereby the federal courts may assert judicial power over state law questions which must be determined in order to resolve the primary federal claim.[2] Pendent jurisdiction will attach where the state and

cation that the bar's management acted contrary to good faith. When the ordinance became effective, the dancers were immediately clothed. After a few weeks, finding itself threatened with financial ruin, M & L Rest instituted the federal action. It would be unjust to deny a speedy resolution by allowing the town to "oust" the federal court of its jurisdiction merely by bringing criminal proceedings.

[52] *See, e.g.*, McNeese v. Board of Educ., 373 U.S. 668, 671 (1963), which expressly rejected this approach in suits involving 42 U.S.C. § 1983 (1970).

[53] The Supreme Court has granted a writ of certiorari. 43 U.S.L.W. 3399 (U.S. Jan. 21, 1975) (No. 74-337). Hopefully, the Court will confirm the Second Circuit's interpretation of *Younger*.

[1] U.S. CONST. art. III, § 2. The constitutional provision has been implemented by § 1331(a) of the Federal Judicial Code. 28 U.S.C. § 1331(a) (1970). Congress has added a requirement that the amount in controversy must exceed $10,000. *Id.* For a thorough discussion of the difficulties in ascertaining whether or not a claim arises under federal law, see Cohen, *The Broken Compass: The Requirement That a Case Arise "Directly" Under Federal Law*, 115 U. PA. L. REV. 890 (1967).

[2] *See, e.g.*, United Mine Workers v. Gibbs, 383 U.S. 715, 725 (1966); Osborn v. Bank of the United States, 22 U.S. (9 Wheat.) 738 (1824).

In *Osborn*, legislation creating the Bank of the United States authorized the Bank to sue or be sued in any federal circuit court. The statute, however, did not limit the authorization to suits involving federal questions. *Id.* at 817. It was contended that Con-

federal claims "derive from a common nucleus of operative fact"[3] and "the entire action before the court comprises but one constitutional 'case.' "[4]

Although a basic understanding of the concept is not inherently difficult, the development of workable standards for its implementation has proven troublesome.[5] Particularly vexing is the situation where the federal claim is merely colorable and asserted only to ensure that a federal forum will hear the predominant state claim. In an attempt to alleviate this problem, Judge Friendly, writing for a unanimous Second Circuit panel in *Kavit v. A. L. Stamm & Co.*,[6] promulgated a new standard:

> If it appears that the federal claims are subject to dismissal [for failure to state a claim] or could be disposed of on a motion for summary judgment . . . , the court should refrain from exercising pendent jurisdiction absent exceptional circumstances.[7]

If the district court determines at the outset that the federal claims are too "flimsy," pendent jurisdiction should not be invoked.[8] Thus, *Kavit* suggests that even though a federal claim is sufficiently substantial to provide subject matter jurisdiction, it may not be substantial enough to confer pendent jurisdiction over a related state claim.[9]

The plaintiff, Dr. Arthur Kavit, maintained an account with the brokerage firm of Stamm & Co.[10] In 1964, through Stamm and its registered representative, Jack Levien, Kavit made two short sales of Texas

gress could not grant federal jurisdiction over cases brought by or against the Bank that derived from general common law principles. *Id.* at 819. Chief Justice Marshall, writing for the Supreme Court, rejected this contention, stating:

> [W]hen a question to which the judicial power of the Union is extended by the constitution, forms an ingredient of the original cause, it is in the power of Congress to give the Circuit Courts jurisdiction of that cause, *although other questions of fact or of law may be involved in it.*

Id. at 823 (emphasis added). *See generally* Note, *The Evolution and Scope of the Doctrine of Pendent Jurisdiction in the Federal Courts*, 62 COLUM. L. REV. 1018 (1962).

3 United Mine Workers v. Gibbs, 383 U.S. 715, 725 (1966).

4 *Id. See* Note, UMW v. Gibbs *and Pendent Jurisdiction*, 81 HARV. L. REV. 657, 658 (1968).

5 *See generally* Note, *The Evolution and Scope of the Doctrine of Pendent Jurisdiction in the Federal Courts*, 62 COLUM. L. REV. 1018 (1962).

6 491 F.2d 1176 (2d Cir. 1974).

7 *Id.* at 1180, *citing* FED. R. CIV. P. 12(b)(6), 56.

8 491 F.2d at 1179.

9 The federal courts have recognized that a purported federal claim might be so thin as to be insubstantial for purposes of sustaining subject matter jurisdiction. Levering & Garrigues Co. v. Morrin, 289 U.S. 103, 105 (1933); Elberti v. Kunsman, 376 F.2d 567 (3d Cir. 1967) (per curiam). Jurisdictional insubstantiality could result in cases where the claim is "obviously without merit" or prior decisions have so foreclosed the issue as to render the claim frivolous. *Ex parte* Poresky, 290 U.S. 30, 32 (1933); Levering & Garrigues Co. v. Morrin, 289 U.S. 103, 105-06 (1933).

10 491 F.2d at 1180.

Gulf Sulphur Co. stock. Unfortunately for Kavit, the price of the stock increased sharply. The short sales were covered at a substantially higher price, resulting in a loss to Kavit of $3,602.26.[11] Subsequently, Kavit brought an action in federal district court against both Stamm and Levien. The complaint stated two claims based on alleged violations of the Securities Exchange Act of 1934.[12] Specifically, the plaintiff maintained that defendants had committed a fraud in the purchase and sale of securities in violation of section 10(b) of the Act and rule 10b-5 of the Securities and Exchange Commission,[13] and that the Act's margin requirements had been violated.[14] In addition, two common law grounds were set forth: one charged the defendants with negligence, the other alleged a conversion.[15]

The defendants moved to dismiss the complaint for failure to state a claim under the Act[16] and, alternatively, for a stay of all court proceedings pursuant to an arbitration clause in the standard customer contract.[17] District Judge Metzner, while conceding that the allegations of securities fraud were "thin," ruled that the requisite elements of a

---

[11] *Id.* at 1180-81. News of a mineral strike by Texas Gulf Sulphur Co. caused a sharp rise in the price of its stock. Kavit decided to sell short when he became convinced that the value of the stock would not increase any further. Two short sales of 100 shares were made, one at 42⅝ and the other at 39¾. Kavit's prediction turned out to be erroneous, and the short sales were covered at 58¾ per share. *Id.*

[12] *Id.* The federal district courts have been given exclusive subject matter jurisdiction over cases involving violations of the Act. 15 U.S.C. § 78aa (1970).

[13] *See* 15 U.S.C. § 78j(b) (1970); 17 C.F.R. § 240.10b-5 (1974). *See also* Ruder, *Civil Liability Under Rule 10b-5: Judicial Revision of Legislative Intent?*, 57 Nw. U.L. REV. 627 (1963). Kavit contended that Levien had made reckless forecasts as to the future value of Texas Gulf stock. It was also alleged that one of the two short sales was made without Kavit's consent. 491 F.2d at 1181.

[14] 491 F.2d at 1181. Section 7 of the Act authorizes the Board of Governors of the Federal Reserve System to prescribe regulations as to the amount of credit that can be extended on any security purchase. 15 U.S.C. § 78g (1970). Section 29 provides that any contract made in violation of the Act is void. *Id.* § 78cc(b). Kavit asserted that during the period embracing the relevant transactions, his account was substantially undermargined in violation of section 7, and thus, the sales and purchases made from the account were void. 491 F.2d at 1181.

[15] 491 F.2d at 1181. Kavit supported these counts with the same allegations which supported his 10b-5 claim. *See* note 13 *supra*. In addition, he alleged that Levien had failed to comply with Kavit's instructions to cover the sales in the range of 43-44 per share in the event the price of shares went up. 491 F.2d at 1181.

[16] 491 F.2d at 1181. Kavit urged that, even if pendent jurisdiction were thus inapplicable, the federal court should nevertheless adjudicate his state law claims because of the diverse citizenship of the parties. Kavit was a citizen of Virginia and both defendants were citizens of New York. However, the defendants moved to dismiss for failure to satisfy the jurisdictional amount of $10,000. *See* 28 U.S.C. § 1332 (1970). The Second Circuit agreed with the defendants, stating that it appeared "'to a legal certainty' that plaintiff's claim was 'really less' than the required jurisdictional amount." 491 F.2d at 1179, n.3, *citing* Saint Paul Mercury Indem. Co. v. Red Cab Co., 303 U.S. 283, 289 (1938).

[17] 491 F.2d at 1181. *See* 9 U.S.C. §§ 2, 3 (1970); FED. R. CIV. P. 81(a)(3). The arbitration clause provided that "[a]ny controversy between you [the broker] and the undersigned [customer] arising out . . . of this contract or the breach thereof, shall be settled by arbitration . . . ." 491 F.2d at 1178 n.2.

rule 10b-5 violation had been sufficiently asserted.[18] Subsequently, the district court refused to grant the requested stay on the ground that an arbitration clause could not bind the plaintiff to arbitrate a 10b-5 claim.[19] After a trial on the merits, District Judge Bonsal, who heard the case without a jury, determined that the securities law claims were unfounded.[20] Nonetheless, exercising pendent jursidiction over the state common law claims, he awarded $2,949.08 in damages to Kavit based on Levien's failure to follow Kavit's instructions to cover the short sales within a given price range in the event the price increased.[21] Thus, the action, which had been "knocking around" the federal courts since 1966,[22] resulted in a judgment for a relatively minor sum, grounded entirely in state common law.

On appeal, the Second Circuit, although expressing its disagreement with the assertion of jurisdiction over the state law claims, declined to reverse the judgment.[23] Judge Friendly found the case to be a disturbing abuse of pendent jurisdiction. Federal jurisdiction had been asserted over an essentially state law claim that would otherwise have gone to arbitration.[24] Furthermore, the judge expressed dismay that such a nominal common law claim had consumed a large and undue

---

18 491 F.2d at 1181; *see* Kavit v. A.L. Stamm & Co., Civil No. 66-1775 (S.D.N.Y., Apr. 3, 1967). Judge Metzner relied on A.T. Brod & Co. v. Perlow, 375 F.2d 393 (2d Cir. 1967). The *Brod* court ruled that a plaintiff asserting a 10b-5 claim need not prove in his complaint that he will ultimately recover in order to state a claim sufficient for jurisdictional purposes. 375 F.2d at 398.

19 491 F.2d at 1181. Section 29(a) of the Securities Exchange Act provides that any provision binding any person to waive compliance with the requirements of the Act or rules promulgated pursuant to the Act is void. 15 U.S.C. § 78cc(a) (1970). The Supreme Court has held that a similar statute contained in the Securities Act of 1933 voids any agreement to arbitrate a dispute arising under the 1933 Act. Wilko v. Swan, 346 U.S. 427, 434-35, 438 (1953). Judge Metzner had previously applied the holding of *Wilko* to the provisions of the Securities Exchange Act in Pawgan v. Silverstein, 265 F. Supp. 898, 901 (S.D.N.Y. 1967). However, the *Pawgan* court refused to apply the non-waiver provisions of section 29(a) to pendent state claims, thereby rendering the state claims arbitrable. The *Kavit* defendants, by contrast, did not make a motion limited to arbitration solely of state claims. 491 F.2d at 1181.

20 491 F.2d at 1183; *see* Kavit v. A.L. Stamm & Co., Civil No. 66-1775 (S.D.N.Y., July 7, 1972).

21 491 F.2d at 1183. The judge disbelieved Kavit's testimony that he had not authorized one of the short sales, but credited Kavit's claim that he had given instructions when to cover the sales. On appeal, Judge Friendly felt Kavit's testimony strained credulity, but was compelled to give "due regard" to the trial court's evaluation of the testimony. *Id., citing* FED. R. CIV. P. 52(a).

22 491 F.2d at 1178 n.1. The court noted there had been "unconscionable delays" by counsel for both sides. *Id.*

23 *Id.* at 1183-84.

24 *Id.* at 1178. Judge Friendly stated:

> Permitting a plaintiff to try such claims on the basis of pendent jurisdiction not only adds to the burdens of the federal courts and deprives the parties of the opportunity to obtain in a more fitting tribunal "a surer-footed reading of applicable law," . . . but it strips the defendant of its contractual right to arbitration.

Id. at 1178-79, *quoting* United Mine Workers v. Gibbs, 383 U.S. 715, 726 (1966).

quantity of scarce federal judicial resources. In particular, the court was distressed by the "flimsy nature" of the federal grounds used to support pendent jurisdiction.[25] The federal claims were extremely weak and "should have been dismissed on motion."[26] Nonetheless, the district court had permitted the claims to be brought to trial. Since a reversal for want of jurisdiction would completely destroy the value of the not insubstantial efforts of the district judges, the Second Circuit felt compelled to affirm the judgment, albeit "without enthusiasm."[27]

In *Kavit*, Judge Friendly, adopting a narrow construction of *United Mine Workers v. Gibbs*,[28] the leading case concerning pendent jurisdiction, declared that the weakness of the federal claims may call for dismissal of the charges grounded on state law.[29] In *Gibbs*, the Supreme Court had recognized that the federal courts have a broad constitutional power to exercise jurisdiction over state law causes of action so closely related to an asserted federal claim as to comprise "one constitutional case."[30] While so holding, Justice Brennan stated:

> The federal claim must have substance sufficient to confer subject matter jurisdiction on the court. . . . The state and federal claims must derive from a common nucleus of operative fact. But if, considered without regard to their federal or state character, a plaintiff's claims are such that he would ordinarily be expected to try them all in one judicial proceeding, then, assuming substantiality of the federal issues, there is *power* in federal courts to hear the whole.[31]

---

25 491 F.2d at 1179, *citing* McFaddin Express, Inc. v. Adley Corp., 346 F.2d 424 (2d Cir. 1965), *cert. denied*, 382 U.S. 1026 (1966). In *McFaddin*, the court affirmed a refusal to entertain jurisdiction over pendent state law grounds after the federal causes of action had been dismissed for failure to state a claim. *But see* Galella v. Onassis, 487 F.2d 986, 996 (2d Cir. 1973), *discussed in* note 52 *infra*.

26 491 F.2d at 1178.

27 *Id.* at 1183-84; *see* note 47 and accompanying text *infra*.

28 383 U.S. 715 (1966). Paul Gibbs alleged that the union had conducted a secondary boycott prohibited by section 303 of the Labor Management Relations Act, 29 U.S.C. § 187 (1970), and had conspired against him in violation of Tennessee state law. *Id.* at 720. The trial court permitted a recovery on the state claim only. The Supreme Court affirmed notwithstanding the absence of any independent ground for jurisdiction over the state-based conspiracy claim.

29 491 F.2d at 1179.

30 383 U.S. at 725.

31 *Id.* (citation omitted) (emphasis in original). This standard is generally read conjunctively, requiring that the federal and state claims both "derive from a common nucleus of operative fact" and be the type typically tried "in one judicial proceeding." *See* C. WRIGHT, LAW OF FEDERAL COURTS § 19 (2d ed. 1970). *But see* Baker, *Toward a Relaxed View of Federal Ancillary and Pendent Jurisdiction*, 33 U. PITT. L. REV. 759, 764-65 (1972), wherein the author suggests that the element of expectation was intended to be an alternative to the "common nucleus of operative fact test." The author contends that the expectation requirement "ties the doctrine of pendent jurisdiction to the Federal Rule of Civil Procedure, with all their liberal provisions for joinder of claims and parties." *Id.* at 765. Thus, the exercise of pendent jurisdiction could be proper even though the

The Court characterized the prior case law as "unnecessarily grudging."[32] The primary considerations were held to be those of "judicial economy, convenience and fairness to litigants."[33] Accordingly, the exercise of pendent jurisdiction is discretionary,[34] each case presenting two distinct issues: (1) whether the federal court has the power to hear the state claim and, (2) assuming it does, whether that power ought to be exercised.[35]

Kavit represents an attempt to place limits on the liberal exercise of this discretionary power by drawing from the "cautionary" segment of the *Gibbs* opinion.[36] Although the general thrust of *Gibbs* was to encourage a broader use of pendent jurisdiction,[37] the Court did indi-

asserted state claim does not derive from the same "nucleus of operative fact" as the federal claim. *Id.* at 764.

It should be noted, however, that the American Law Institute (ALI) has suggested the more popular cumulative construction of the *Gibbs* formula in its proposed revision of the federal question jurisdiction statute. ALI, STUDY OF THE DIVISION OF JURISDICTION BETWEEN STATE AND FEDERAL COURTS, proposed § 1313(a) and comment at 210 (1969).

[32] 383 U.S. at 725. The Court set aside the test previously established in Hurn v. Oursler, 289 U.S. 238 (1933). In *Hurn*, pendent jurisdiction was said to exist in "a case where two distinct grounds in support of a single cause of action are alleged, one only of which presents a federal question . . . ." *Id.* at 246. However, the federal courts would not have jurisdiction where two separate causes of action were alleged and only one arose under federal law. *Id.* The *Gibbs* Court rejected this test because of the confusion generated by attempts to determine when "a single cause of action" was present, as opposed to "two separate and distinct causes of action." 383 U.S. at 722, 724. For some examples of the difficulties in applying this standard, see Note, *The Evolution and Scope of the Doctrine of Pendent Jurisdiction in the Federal Courts*, 62 COLUM. L. REV. 1018, 1026-30 (1962).

[33] 383 U.S. at 726. Other relevant considerations include the desire to avoid needless rulings on state law issues, whether the state claims are "closely tied" to the federal grounds, and the likelihood of confusing the jury with presentations of conflicting legal theories. *Id.* at 726-27. *See* Note, UMW v. Gibbs *and Pendent Jurisdiction*, 81 HARV. L. REV. 657, 658 (1968).

[34] 383 U.S. at 726.

[35] Almenares v. Wyman, 453 F.2d 1075, 1084 (2d Cir. 1971) (Friendly, C.J.), *cert. denied*, 405 U.S. 944 (1972); Leather's Best, Inc. v. S.S. Mormaclynx, 451 F.2d 800, 809 (2d Cir. 1971).

[36] 491 F.2d at 1179-80. In *Gibbs*, Justice Brennan declared:

> [R]ecognition of a federal court's wide latitude to decide ancillary questions of state law does not imply that it must tolerate a litigant's effort to impose upon it what is in effect only a state law case. Once it appears that a state claim constitutes the real body of a case, to which the federal claim is only an appendage, the state claim may fairly be dismissed.

383 U.S. at 727.

[37] For examples of the liberalized approach fostered by *Gibbs*, see Rosado v. Wyman, 397 U.S. 397, 402-05 (1970) (jurisdiction over pendent state claim upheld even though federal claim had been mooted before trial); Forest Laboratories, Inc. v. Pillsbury Co., 452 F.2d 621, 629 (7th Cir. 1971) (pendent jurisdiction affirmed although federal claim dismissed after trial).

The *Kavit* court itself indicated that the Second Circuit had not been "grudging" in applying the *Gibbs* principles. 491 F.2d at 1179. *See, e.g.*, Almenares v. Wyman, 453 F.2d 1075, 1083-85 (2d Cir. 1971), *cert. denied*, 405 U.S. 944 (1972); Leather's Best, Inc. v. S.S. Mormaclynx, 451 F.2d 800, 809-11 (2d Cir. 1971); Astor-Honor, Inc. v. Grosset & Dunlap, Inc., 441 F.2d 627, 629-30 (2d Cir. 1971).

cate that if the federal claims were dismissed before trial, the state claims should also be dismissed.[38] *Kavit* moved a step further by adding that if the federal claims could not withstand a motion for summary judgment, pendent jurisdiction should not be exercised over any state causes of action.[39]

The commentators have also argued that *Gibbs* loosened the strictures on the application of pendent jurisdiction. *See* C. WRIGHT, LAW OF FEDERAL COURTS § 19 (2d ed. 1970); Baker, *Toward a Relaxed View of Federal Ancillary and Pendent Jurisdiction*, 33 U. PITT. L. REV. 759 (1972); Note, UMW v. Gibbs *and Pendent Jurisdiction*, 81 HARV. L. REV. 657 (1968). *But see* Shakman, *The New Pendent Jurisdiction of the Federal Courts*, 20 STAN. L. REV. 262 (1968), wherein the author suggests that the broad exercise of pendent jurisdiction fostered by *Gibbs* unnecessarily encroaches on state court jurisdiction. *Id.* at 285.

38 383 U.S. at 726. The Court stated, "if the federal claims are dismissed before trial, even though not insubstantial in a jurisdictional sense, the state claims should be dismissed as well." 383 U.S. at 726 (footnote omitted). In *Kavit*, Judge Friendly interpreted this language as being "mandatory" in nature. 491 F.2d at 1179. However, the Supreme Court has indicated that the *Gibbs* language might not be obligatory. In Rosado v. Wyman, 397 U.S. 397, (1970), the Court refused to consider

> [w]hether or not the view that an insubstantial federal question does not confer jurisdiction—a maxim more ancient than analytically sound—should now be held to mean that a district court should be considered without *discretion*, as opposed to *power*, to hear a pendent claim . . . .

Id. at 404 (emphasis in original).

The Sixth Circuit, in Nash & Associates, Inc. v. Lum's of Ohio, Inc., 484 F.2d 392 (6th Cir. 1973), stated that where the federal issues were dismissed before trial, a district court decision to decline jurisdiction was "proper." *Id.* at 395-96. However, the language of the court could be interpreted as either denying the existence of jurisdictional power or as affirming the district court's use of discretion to decline utilizing the power.

In a case that arose prior to *Gibbs*, Judge Aldrich of the First Circuit wrote that Hurn v. Oursler, 289 U.S. 238 (1933), *see* note 32 *supra*, did not require that "state claims which are, at best, dubious on their face" be retained after the federal claim is dismissed on the pleadings. Robinson v. Stanley Home Products, Inc., 272 F.2d 601, 604 (1st Cir. 1959). However, the validity of this statement may be questioned in light of the liberalizing effect of *Gibbs* and the disparaging reference in *Gibbs* to prior case law. *See* 383 U.S. at 725.

The ALI study reports:

> [i]f the federal element that is the basis for jurisdiction is disposed of early in the case, as on the pleadings, it smacks of the tail wagging the dog to continue with a federal hearing of the state claim.

ALI, STUDY OF THE DIVISION OF JURISDICTION BETWEEN THE STATE AND FEDERAL COURTS, proposed § 1313(c), commentary at 213 (1969). However, the ALI proposes a pendent jurisdiction statute which would leave "discretion in the trial judge to refuse to hear the state claim after dismissal of the federal claims where judicial economy would not be served by entertaining the non-federal claim." *Id.* Thus, the ALI study leans away from the mandatory approach suggested in *Kavit.*

39 491 F.2d at 1180. The court would exempt "exceptional circumstances" from the application of the general rule. *Id.* Three sets of such circumstances were suggested. *Id.* at 1180 n.4. Pendent jurisdiction might be warranted if a defendant neglects to raise the issue of the weakness of the federal claim until the court has invested a substantial amount of time in the case. *Id.*, *citing* A.H. Emery Co. v. Marcan Products Corp., 389 F.2d 11, 19-21 (2d Cir.), *cert. denied*, 393 U.S. 835 (1968). Secondly, pendent jurisdiction might properly attach when the pendent state claim "significantly invokes questions of federal policy." 491 F.2d at 1180 n.4, *citing* United Mine Workers v. Gibbs, 383 U.S. 715

Judge Friendly stated that the securities fraud claim was too "thin" and did not contain the requisite allegations of fraudulent activities.[40] As to the alleged margin violations, the panel ruled that although the complaint stated facts sufficient to defeat a motion to dismiss for failure to state a claim, subsequent affidavits made it clear that the allegations would not have withstood a motion for summary judgment.[41] Additionally, the court, sensitive to the presence of the arbitration provision in the standard customer contract, voiced concern that the exercise of pendent jurisdiction "stripped" the defendants of their contractual right to arbitrate.[42] The *Kavit* court indicated that where jurisdiction

---

(1966), and Almenares v. Wyman, 453 F.2d 1075, 1083-85 (2d Cir. 1971), *cert. denied,* 405 U.S. 944 (1972). Finally, the court recognized that the exercise of pendent jurisdiction might be justified if the dismissal of the pendent claims "would otherwise sharply clash with the directive in *Gibbs* that pendent jurisdiction serve the ends of 'judicial economy, convenience and fairness to litigants.'" 491 F.2d at 1180 n.4.

40 491 F.2d at 1182. Judge Friendly ruled that the complaint could not be rescued by A.T. Brod & Co. v. Perlow, 375 F.2d 393 (2d Cir. 1967), relied upon by District Judge Metzner. 491 F.2d at 1182; *see* note 18 *supra.* In *Brod,* a stockbroker sought compensation for losses suffered because of the defendants' failure to pay for securities which they had ordered. The plaintiff alleged that the defendants had schemed to defraud various brokers and dealers by ordering securities and intending to pay for them only if their market value had increased by the date payment was due. 375 F.2d at 395. The Second Circuit reversed the district court's holding that federal jurisdiction was lacking. Judge Kaufman, writing for the court, ruled that the plaintiff was not required to prove in its complaint that it would ultimately recover. *Id.* at 398.

The *Kavit* court distinguished *Brod,* noting that the plaintiff in *Brod* had at least alleged fraud in the traditional sense, even though it was doubtful it would recover. In *Kavit,* the complaint failed to aver that Levien did not sincerely believe the predictions he allegedly made, nor did Kavit aver that no reasonable man would have so believed. 491 F.2d at 1182.

41 491 F.2d at 1182. The affidavits showed that with one technical and excusable exception Kavit's account was adequately margined during the period in issue. During this period, Kavit was in the process of having his account transferred to Stamm from the Richmond, Va. office of Francis I. Dupont & Co. *Id.* at 1180. The court concluded that during the period of transfer of plaintiff's account, Stamm, as transferee, had permissibly treated the two accounts as one under § 6(d) of the Federal Reserve Board's Regulation T. 12 C.F.R. § 220.6(d)(1) (1974). This regulation provides that, "[i]n the event of the transfer of a general account . . . from one creditor to another, such account may be treated for the purposes of this part as if it had been maintained by the transferee from the date of its origin . . . ." *Id.*

Secondly, even though it was apparently conceded by defendants that there were violations with respect to specific transactions, the court agreed that they were excusable. The court noted that §§ 3(b) and 3(g) of Regulation T permit "'day-light trades': fluctuations in the customer's balance that would otherwise result in an insufficient margin . . . if the customer is left with sufficient margin in his account at the end of the day." 491 F.2d at 1182, *citing* 12 C.F.R. §§ 220.3(b), (g) (1974).

In addition, the court pointed out that while at one point Kavit's account was undermargined by $36, § 6(k) of Regulation T forgives "innocent mistakes" where, after its discovery, the broker takes practicable action to rectify the mistake. 12 C.F.R. 220.6(k) (1974). Thus, the Second Circuit would have awarded summary judgment to the defendants on the federal claims. 491 F.2d at 1182.

42 491 F.2d at 1178-79.

over otherwise arbitrable state claims is only pendent, the district court should normally dismiss the state claims or stay their trial.[43]

Despite affirmance of the district court's decision, the Second Circuit clearly believed that pendent jurisdiction had been improperly exercised.[44] Judge Friendly went so far as to indicate that an appeal from Judge Metzner's interlocutory orders denying the motions to dismiss or stay the state claims would have led to a reversal.[45] However, since the interlocutory appeal was not perfected[46] and the case did not reach the appellate level until after trial on the merits, the court felt compelled to affirm the judgment. The case had run its full course through the federal courts, the amount in controversy was minor, and the defendants had failed to protect their right to arbitrate by taking an earlier appeal.[47] The court also noted that reversals for improper exercise of pendent jurisdiction are "very rare."[48] Indeed, other circuits

---

[43] *Id.* at 1180. Moreover, while the court indicated a willingness to make an exception in light of special circumstances, it could not think of any circumstances that would apply. *Id.*

[44] *Id.* at 1182-83.

[45] *Id.* at 1182.

[46] *Id.* at 1183. The defendants filed notices of appeal, but failed to pursue them. Accordingly, the appeals were dismissed for lack of prosecution. *Id.* at 1181. The defendants claimed on the instant appeal that no interlocutory appeal was possible inasmuch as the order denying the motion for a stay pending arbitration was not final. Thus, they contended their right to appeal had not been lost. The Second Circuit rejected this contention, stating that "the denial of a stay pending arbitration in an action at law has long been held appealable . . . ." *Id.* at 1181-82. *See* Ettelson v. Metropolitan Life Ins. Co., 317 U.S. 188 (1942); Shanferoke Coal & Supply Corp. v. Westchester Serv. Corp., 293 U.S. 449, 452 (1935) (Brandeis, J.); Enelow v. New York Life Ins. Co., 293 U.S. 379 (1935).

Professor Moore has stated that the rule laid down in *Enelow* and *Ettelson* provides that "[c]ertain orders that do no more than determine the method or timing of trial have nevertheless been held to be 'orders . . . granting . . . or . . . refusing . . . injunctions' within the language of 28 U.S.C. § 1292(a)(1) and thus appealable." 9 J. MOORE, FEDERAL PRACTICE ¶ 110.20[3] (2d ed. 1970). Under this theory, orders granting or denying stays of district court proceedings may be appealed if the action to be stayed is one at law and if the stay is requested in order to permit the prior determination of an equitable defense or counterclaim. Standard Chlorine of Delaware, Inc. v. Leonard, 384 F.2d 304, 308 (2d Cir. 1967) (Kaufman, J.).

[47] 491 F.2d at 1183-84. The court's refusal to void the work of the trial court is supported by Forest Laboratories, Inc. v. Pillsbury Co., 452 F.2d 621 (7th Cir. 1971). The Seventh Circuit therein stated:

> "Considerations of judicial economy, convenience and fairness to litigants" certainly favor the retention of jurisdiction over state law issues, where both state and federal claims were tried together and the latter only dismissed after trial.

Id. at 629, *quoting* United Mine Workers v. Gibbs, 383 U.S. 715, 726 (1966).

The defendant contended that an arbitrator familiar with the practices of the securities industry would have reached a different conclusion than did Judge Bonsal. The Second Circuit responded by pointing out that the defendants should have protected their right to arbitrate the state claims by appealing Judge Metzner's orders or by moving the federal court to dispose of the federal claims only. 491 F.2d at 1183.

[48] 491 F.2d at 1180 n.5, *citing* Brough v. United Steelworkers, 437 F.2d 748 (1st Cir. 1971) (exercise of pendent jurisdiction was inappropriate in action where no federal wrong was alleged in the complaint but which was removed to federal court by defendant

have permitted liberal exercise of pendent jurisdiction even in situations where the federal claims are resolved before trial.[49]

In formulating its own test by which to measure the propriety of the exercise of pendent jurisdiction, the Second Circuit made an implicit shift away from the considerations of fairness and judicial economy emphasized in *Gibbs*.[50] Rather, the *Kavit* court preferred to gauge the thinness or flimsiness of the federal claim. The court was concerned with ascertaining whether the plaintiff has a federal claim truly worthy of vindication in a federal forum.[51] This shift in emphasis seemingly

---

who alleged the action arose under federal law) and Elberti v. Kunsman, 376 F.2d 567, 568 (3d Cir. 1967) (per curiam) (retention of jurisdiction over state claim was inappropriate where complaint itself revealed that federal claim was "unsubstantial and frivolous").

Elberti, however, can be distinguished from *Kavit*. In *Elberti*, there was no federal claim to support jurisdiction over the pendent state claim. In *Kavit*, the Second Circuit was concerned not with federal claims which are insubstantial to support their own jurisdiction, but rather with federal claims which are insubstantial to support pendent jurisdiction. *See* 491 F.2d at 1179.

Brough, however, was somewhat analogous to the problem to which the Second Circuit had addressed itself. In *Brough*, the First Circuit confronted an action which had originally been commenced in a state court and removed to the district court. As the court pointed out, the removal was originally inappropriate because the plaintiff's complaint only contained an allegation of common law negligence. This defect, however, was later waived when, after the district court refused to remand the case, the plaintiff added a second count based on federal law. The district court then granted defendant's motion for summary judgment as to both the state and federal claim.

Facing the appeal from summary judgment, the court pointed out that in removal cases, as in original federal jurisdiction cases, the district court may retain pendent jurisdiction over the state claim or remand it to the state court. 437 F.2d at 750. Citing *Gibbs*, the court concluded that the granting of summary judgment on the federal claim created a situation in which the appropriate exercise of discretion required a remand of the state claim. *Id.* Therefore, the court affirmed the judgment as to the federal claim, vacated the judgment as to the state claim, and remanded that claim to the state court. *Id.*

It cannot be overlooked, however, that in *Brough*, the court had an additional impetus to remand. Initially, the plaintiff had elected the state court as his forum only to be frustrated by what should have been an unsuccessful attempt to remove by the defendant.

49 491 F.2d at 1180 n.5, *citing* Gray v. Local 51, Int'l Ass'n of Heat & Frost Insulators & Asbestos Workers, 447 F.2d 1118, 1120 (6th Cir. 1971) (pendent jurisdiction over breach of contract action by member against union local exercised after actions against the local and international union for violations of the Federal Labor Management Relations Act were dismissed). The *Kavit* court also referred to Springfield Television, Inc. v. Springfield, 462 F.2d 21 (8th Cir. 1972), wherein it was held that the district court properly retained jurisdiction over a pendent state claim notwithstanding the fact that the parties disposed of the federal preemption issue by stipulation prior to trial. *See also* Parrent v. Midwest Rug Mills, Inc., 455 F.2d 123, 129 (7th Cir. 1972), wherein the court dismissed the federal claims and indicated that the district court should have done so before trial because the claims were barred by the applicable statute of limitations. Nonetheless, the court held that the continued retention of jurisdiction over pendent state claims was proper.

50 *See* note 33 and accompanying text *supra*.

51 *See* 491 F.2d at 1178-79, 1183. In Howard v. Furst, 238 F.2d 790 (2d Cir. 1956), *cert. denied*, 353 U.S. 937 (1957), the court stated:

The doctrine of pendent jurisdiction is only applicable when the federal court

attempts to question the good faith of the plaintiff. If the court finds that the plaintiff was merely looking for a federal crutch to support federal jurisdiction over what is an essentially state law claim, pendent jurisdiction would presumably be denied.

Nonetheless, a "thinness" approach should be utilized as but one of several factors to be considered in assessing whether, in a given case, the exercise of pendent jurisdiction would be proper.[52] Although a *Kavit*-type analysis might be fruitful in circumstances where the plaintiff's good faith can be questioned, *Gibbs* remains the controlling Supreme Court precedent. Accordingly, the convenience and fairness factors, cited in *Gibbs*, present the operative considerations.[53] Indeed, in *Rosado v. Wyman*,[54] the Court reaffirmed the broad scope which it accorded the doctrine in *Gibbs*, noting that the proper exercise of jurisdiction over a pendent claim is not dependent on the survival of the federal claim through all stages of the litigation.[55]

> has jurisdiction of a substantial claim to begin with; and the policy is that of avoiding piecemeal litigation.

Id. at 794.

[52] Indeed, the Second Circuit's own position is not entirely consistent. In Galella v. Onassis, 487 F.2d 986 (2d Cir. 1973), decided only four months before *Kavit*, plaintiff filed suit in state court alleging malicious prosecution on the part of Mrs. Onassis and the Secret Service agents assigned to protect her. The case was removed to federal court. The actions against the agents were dismissed because the court found them to be immune from suit. Subsequently, Galella's motion to remand to the state court, made just prior to trial, was denied. *Id.* at 991-92.

The Second Circuit affirmed the district court's assertion of jurisdiction over the state claims. Judge Smith, writing for the court, stated that the dismissal of the action against the agents did not "automatically strip" the court of pendent jurisdiction. The court noted that the motion to remand was made six months after the dismissal and on the eve of the trial, that hearings had already been held by the federal court, a special master had been appointed, a number of motions had been heard, other motions were pending, and the United States Government had intervened in the case. Judge Smith, relying on the *Gibbs* criteria, ruled that

> [a]s no claim of unfairness has been raised, considerations of judicial economy govern and support the court's denial of the motion to remand. A great deal of judicial effort had been expended in covering ground that must be gone over anew had remand been ordered.

Id. at 996.

[53] 383 U.S. at 726; Leather's Best, Inc. v. S.S. Mormaclynx, 451 F.2d 800, 811 (2d Cir. 1971).

It should be noted that Judge Friendly would not completely abandon the *Gibbs* factors. Instead, he would relegate their role to that of an exception to the *Kavit* test. 491 F.2d at 1180 n.4; *see* note 39 *supra*.

[54] 397 U.S. 397 (1970). In *Rosado*, although the federal claim had been mooted, the Court found it proper for a district court to make a decision on the merits of the pendent state claim. *Id.* at 401.

[55] *Id.* at 405. The Court declared:

> We are not willing to defeat the commonsense policy of pendent jurisdiction—the conservation of judicial energy and the avoidance of multiplicity of litigation—by a conceptual approach that would require jurisdiction over the primary claim at all stages as a prerequisite to resolution of the pendent claim.

Id.

The Second Circuit was undoubtedly influenced by the present state of congestion in the federal courts. Accordingly, the *Kavit* test is designed to ensure that the federal courts are not burdened with cases properly cognizable by state courts.[56] The intimations of the court should discourage forum-shopping plaintiffs from seeking out federal causes of action in order to create federal jurisdiction. Nevertheless, the application of *Kavit* to specific cases will present difficulties to the district courts. As a practical matter, a court will experience difficulty in determining when a federal claim is not so "flimsy" as to be denied jurisdiction, but is "flimsy" enough to fall prey to a motion for summary judgment. The *Kavit* opinion offers no suggestions as to what criteria should be applied in making this determination. Since *Kavit* indicates that reversals for improper exercise of pendent jurisdiction may become more prevalent, district judges may tend to refuse jurisdiction over state claims in close cases. Consequently, *Kavit* may mark a return to the more "grudging" approach criticized in *Gibbs*.[57] In addition, incongruities may develop in cases where the pendent state claims are dismissed based upon the "flimsy" nature of the federal claim but the same "flimsy" allegations are retained for trial.[58]

It should be pointed out, however, that *Gibbs* still requires that the issue as to the propriety of exercising pendent jurisdiction remain open throughout the litigation. 383 U.S. at 727. The *Gibbs* court noted that pretrial proceedings or the trial itself could lead to a conclusion that the state law claims predominate or that the jury would be confused—conclusions that could not have been anticipated earlier. *Id.*

Notably, the approach of *Rosado* is consonant with the liberal rules as to joinder of claims and parties. Rule 13 of the Federal Rules of Civil Procedure encourages the assertion of counterclaims and cross-claims which arise out of the same "transaction or occurrence that is the subject matter of the opposing party's claim . . . ." FED. R. CIV. P. 13(a). It has been said that

> [c]ounterclaim practice has been liberalized to encourage the litigation of all claims between the parties in one lawsuit and to avoid multiplicity of litigation with all of its attendant evils—circuity of action, inconvenience, waste of time and expense for both the court and the parties, and possible injustice.

Note, *The Erie Doctrine and Federal Rule 13(a)*, 46 MINN. L. REV. 913, 917 (1962) (footnote omitted). This is analogous to what the Supreme Court had in mind in *Gibbs* when it spoke of "judicial economy, convenience and fairness to litigants." 383 U.S. at 726.

[56] *See* 491 F.2d at 1178-79.

[57] 383 U.S. at 725.

[58] The Second Circuit has declared:

> If it appears that the federal claims are subject to dismissal under F.R.Civ.P. 12(b)(6) or could be disposed of on a motion for summary judgment under F.R. Civ.P. 56, the court should refrain from exercising pendent jurisdiction absent exceptional circumstances.

491 F.2d at 1180.

It must be noted, however, that while the court could, *sua sponte*, dismiss the state claim where it "appears that the federal claims . . . could" fall prey to a motion for summary judgment, it could not, on its own motion, grant summary judgment. Rule 56 of the Federal Rules of Civil Procedure requires a motion by a party. Thus, in such a situation the federal claim would be retained at least until a motion is made and granted. In addition, even if the motion is made—a likely possibility in most instances—the court

The difficulties posed by the application of the *Kavit* rule may lead the district courts to bypass *Kavit* in favor of the more tangible criteria of *Gibbs*.[59] However, even if the standards enunciated in *Kavit* are cast aside, the district courts in the Second Circuit may be influenced by the general tenor of the *Kavit* opinion and be less solicitous towards requests for pendent jurisdiction. In any event, litigants in these courts have been put on notice that their pendent state claims will not be recognized unless the primary federal claim is more than jurisdictionally colorable.

Edgar J. Royce

---

could, based on evidence adduced for or against the motion, decide that summary judgment would be improper and retain the count for trial. Thus, two trials could result, one in the state court and one in the federal court. This is quite arguably a result that taxes the considerations of fairness and judicial economy which were emphasized in *Gibbs*. *See* note 33 and accompanying text *supra*.

59 For a good example of the "real" factors which must be considered in exercising pendent jurisdiction over claims related to the Securities Exchange Act, see Lowenfels, *Pendent Jurisdiction and the Federal Securities Acts*, 67 COLUM. L. REV. 474, 492-93 (1967).