Washington and Lee Law Review

Volume 27 | Issue 1 Article 12

Spring 3-1-1970

Application Of The Doctrines Of Ancillary And Pendent Jurisdiction To Third-Party Practice In Federal Courts

The court in *Jefferson Standard,* by extending the rule in *Atlas* to apply to intercorporate distributions between companies filing consolidated returns, affirmed the line of decisions which hold that the character of tax-exempt income is not such that it must be absolutely eliminated from any consideration in the system of federal income taxation.[44] While tax-exempt income may not be directly taxed or be used as the basis for increasing the total tax, it may be considered in the determination of taxable income if done in a non-discriminatory manner.

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APPLICATION OF THE DOCTRINES OF ANCILLARY AND PENDENT JURISDICTION TO THIRD-PARTY PRACTICE IN FEDERAL COURTS

After a defendant to a lawsuit has impleaded a third-party defendant, the plaintiff, pursuant to Rule 14(a) of the Federal Rules of Civil Procedure, may amend his complaint to assert a claim, arising out of the "same transaction or occurrence" which was the subject matter of the principal action, directly against the third-party defendant.[1] However, in order to obtain federal jurisdiction over the plaintiff's third-party claim, the majority of federal courts require that the claim be supported by independent jurisdictional grounds.[2] For many years

[44]Helvering v. Independent Life Ins. Co., 292 U.S. 371 (1934); Denman v. Slayton, 282 U.S. 514 (1931); National Life Ins. Co. v. United States, 277 U.S. 508 (1928).

[1]FED. R. CIV. P. 14(a) provides:

(a) *When Defendant may Bring in Third Party.* At any time after commencement of the action a defending party, as a third-party plaintiff, may cause a summons and complaint to be served upon a person not a party to the action who is or may be liable to him for all or part of the plaintiff's claim against him.... The plaintiff may assert any claim against the third-party defendant arising out of the transaction or occurrence that is the subject matter of the plaintiff's claim against the third-party plaintiff, and the third-party defendant thereupon shall assert his defenses as provided in Rule 12 and his counter-claims and cross-claims as provided in Rule 13....

[2]Friend v. Middle Atlantic Transp. Co., 153 F.2d 778 (2d Cir.) *cert. denied,* 328 U.S. 865 (1946); Illinois *ex rel.* Trust Co. of Chicago v. Maryland Cas. Co., 132 F.2d 850, 853 (7th Cir. 1942) (concurring opinion); Palumbo v. Western Md. Ry., 271 F. Supp. 361 (D. Md. 1967); McDonald v. Dykes, 6 F.R.D. 569 (E.D. Pa.), *aff'd per curiam,* 163 F.2d 828 (3rd Cir. 1947); Hoskie v. Prudential Ins. Co. of America, 39 F. Supp. 305 (E.D.N.Y. 1941); *cf.* McPherson v. Hoffman, 275 F.2d 466 (6th Cir. 1960); Baltimore & O.R.R. v. Saunders, 159 F.2d 481 (4th Cir. 1947); Pasternack v. Dalo, 17 F.R.D. 420 (W.D. Pa. 1955).

both commentators[3] and a significant number of federal courts[4] have questioned whether this requirement is desirable.

In *Ayoub v. Helm's Express, Inc.*[5] the United States District Court for the Western District of Pennsylvania denied a motion to amend plaintiff's original complaint to include a direct claim against a third-party defendant on two primary grounds.[6] First, since there was no deversity of citizenship between the plaintiff and the third-party defendant, the court declared that the requirement for an independent jurisdictional basis had not been met. Second, the court declined to invoke the doctrine of pendent jurisdiction, which permits federal courts to hear non-federal claims asserted by the plaintiff in an action grounded on a federal question as long as the non-federal claims meet a requisite relation to the federal claim.[7]

By requiring diversity of citizenship between the plaintiff and the third-party defendant, the court aligned itself with those jurisdictions which are reluctant to play "fast and loose" with the jurisdictional limitations placed on the federal judiciary by the Constitution[8] and congressional enactment.[9] Although these courts concede that Rule 14 of the Federal Rules of Civil Procedure was promulgated in order to provide federal courts with liberal third-party practice provisions,[10] they are also aware of the strict prohibitions of Rule 82, which forbids the Federal Rules from being construed so as to "extend or limit the jurisdiction of the United States district courts . . . ."[11] They fear

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[3]*E.g.*, Fraser, *Ancillary Jurisdiction and the Joinder of Claims in the Federal Courts*, 33 F.R.D. 27, 38 (1964); Holtzoff, *Entry of Additional Parties in a Civil Action*, 31 F.R.D. 101, 109 (1963).

[4]*E.g.*, Buresch v. American LaFrance, 290 F. Supp. 265 (W.D. Pa. 1968); Olson v. United States, 38 F.R.D. 489 (D. Neb. 1965); Myer v. Lyford, 2 F.R.D. 507 (M.D. Pa. 1942); Sklar v. Hayes, 1 F.R.D. 594 (E.D. Pa. 1941); Malkin v. Arundel Corp., 36 F. Supp. 948 (D. Md. 1941).

[5]300 F. Supp. 473 (W.D. Pa. 1969). The confusion surrounding the requirement of an independent jurisdictional basis is well illustrated by the fact that less than a year before the *Ayoub* decision, the very same district court had reached the opposite result in Buresch v. American LaFrance, 290 F. Supp. 265 (W.D. Pa. 1968).

[6]There is also a third ground for the denial of the motion; each count of the proposed amended complaint demanded judgment for a large specific sum of money for unliquidated damages. The court criticized this as "surplusage and unnecessary in a federal pleading." 300 F. Supp. at 473.

[7]For a discussion of the doctrine of pendent jurisdiction see text accompanying notes 29-45 *infra*.

[8]U.S. CONST. art. III, § 2.

[9]28 U.S.C. §§ 1331-32 (1964).

[10]*See, e.g.*, Friend v. Middle Atlantic Transp. Co., 153 F.2d 778 (2d Cir. 1946).

[11]FED. R. CIV. P. 82 provides:

> These rules shall not be construed to extend or limit the jurisdiction of the United States district courts or the venue of actions therein . . . .

the possibility of a federal court having jurisdiction over a claim by a citizen of one state against a co-citizen of the same state by the circuitous means of a third-party claim—thus permitting the plaintiff to recover by indirect means a judgment which he could not, under the doctrine of *Strawbridge v. Curtiss*,[12] have recovered directly.

While these courts express great apprehension of circumstances of federal jurisdictional statutes when a plaintiff makes a third-party claim, they continue to apply the doctrine of ancillary jurisdiction[13] in order to permit the original defendant's third-party claim to be heard. This doctrine is applied even when the third-party defendant is a citizen of the same state as the original defendant[14] or a citizen of the same state as the plaintiff.[15] A number of commentators find this inconsistency absurd and suggest that the ancillary jurisdiction doctrine should apply to *all* third-party claims.[16]

As first conceived in the early case of *Freeman v. Howe*,[17] the doctrine of ancillary jurisdiction merely provided a means by which a federal court could adjudicate claims against property already under its custody or control due to original jurisdiction over the principal action.[18] In that case, a United States marshall attached certain railroad cars. The mortgagees of the railroad demanded the return of the cars by writ of replevin in a state court proceeding. The United States Supreme Court held that the state court could not interfere with the

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[12]7 U.S. (3 Cranch) 267 (1806). According to *Strawbridge*, if there are several parties on one or both sides, there is no diversity jurisdiction if one of the parties on either side is a citizen of a state of which a party on the other side is also a citizen.

[13]One authority has defined ancillary jurisdiction in the following terms:

> [A] district court acquires jurisdiction of a case or controversy as an entirety, and hence may, as an incident to disposition of a matter properly before it, possess jurisdiction to decide other matters raised by the case of which it could not take cognizance were they independently presented.

1 W. BARRON & A. HOLTZOFF, FEDERAL PRACTICE AND PROCEDURE § 23 (C. Wright ed. 1960).

[14]Dery v. Wyer, 265 F.2d 804 (2d Cir. 1959); Waylander-Peterson Co. v. Great Northern Ry., 201 F.2d 408 (8th Cir. 1953); Lesnik v. Public Indus. Corp., 144 F.2d 968 (2d Cir. 1944); Lewis v. United Air Lines Transp. Corp., 29 F. Supp. 112 (D. Conn. 1939).

[15]Illinois *ex rel.* Trust Co. of Chicago v. Maryland Cas. Co., 132 F.2d 850, 853 (7th Cir. 1952) (concurring opinion); William v. Keyes, 125 F.2d 208 (5th Cir.), *cert denied*, 316 U.S. 699 (1942); Crum v. Appalachian Elec. Power Co., 27 F. Supp. 138 (S.D. W.Va. 1939).

[16]*E.g.*, Holtzoff, *Entry of Additional Parties in a Civil Action*, 31 F.R.D. 101, 110 (1963).

[17]65 U.S. (24 How.) 450 (1860).

[18]*See* Note, *Ancillary Jurisdiction of the Federal Courts*, 48 IOWA L. REV. 383, 384-85 (1963).

seized property which was under the exclusive control of the federal court. If the mortgagees had desired to dispute the title to the property, they could have proceeded to assert their claim in a federal court as a claim "ancillary" to the principal action. No showing of diversity of citizenship was required.

An important expansion of the doctrine of ancillary jurisdiction occurred in *Moore v. New York Cotton Exchange*.[19] The plaintiff in *Moore* had obtained federal jurisdiction by alleging a violation of the Sherman Anti-Trust Act.[20] By compulsory counter-claim, which did not involve a federal question, the defendant was awarded an injunction in spite of the fact that the plaintiff's claim had been dismissed on its merits. Thus the Court began to use the doctrine of ancillary jurisdiction as a means of resolving multi-claims arising out of the same "transaction or occurrence"[21] even though one of those claims might not have an independent federal jurisdictional basis.[22] However, only those claims whose resolution was required in order for the federal court to render a complete, effective, and equitable adjudication of the issue in the principal proceeding would be considered ancillary.[23] Following the adoption of the Federal Rules of Civil Procedure, the federal courts employed the *Moore* interpretation of the doctrine of ancillary jurisdiction in order to provide jurisdictional justification for their liberal provisions regarding compulsory counter-claims,[24] cross-claims,[25] interpleader,[26] intervention,[27], and, as already noted, some aspects of impleader.[28]

The court in *Ayoub* also rejected the plaintiff's assertion that his third-party claim should be allowed under the doctrine of pendent

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[19]270 U.S. 593 (1926).

[20]15 U.S.C. §§ 1-7 (1964).

[21]For an excellent analysis of the term "transaction or occurrence," see, Wright, *Estoppel by Rule: The Compulsory Counterclaim under Modern Pleading*, 39 IOWA L. REV. 255, 270-78 (1954).

[22]Cases cited notes 14 and 15 *supra;* cases cited notes 24-26 *infra.*

[23]Note, *Ancillary Jurisdiction of the Federal Courts*, 48 IOWA L. REV. 383, 384 (1963).

[24]Moore v. New York Cotton Exch., 270 U.S. 593 (1926); Great Lakes Rubber Corp. v. Herbert Cooper Co., 286 F.2d 631 (3d Cir. 1961).

[25]R. M. Smythe & Co. v. Chase Nat'l Bank, 291 F.2d 721 (2d Cir. 1961); Childress v. Cook, 245 F.2d 798 (5th Cir. 1957).

[26]*See, e.g.*, Walmac Co. v. Isaacs, 220 F.2d 108 (1st Cir. 1955).

[27]Cases involving intervention as of right under FED. R. CIV. P. 24(a) require no independent grounds of jurisdiction. *See, e.g.*, East v. Crowdus, 302 F.2d 645 (8th Cir. 1962). However, most jurisdictions require independent grounds of jurisdiction for permissive intervention under FED. R. CIV. P. 24(b). *See, e.g.*, Hunt Tool Co. v. Moore, Inc., 212 F.2d 685 (5th Cir. 1954).

[28]Cases cited notes 14 and 15 *supra.*

jurisdiction. According to this judicially created doctrine,[29] "original jurisdiction vesting on the basis of a plaintiff's federal claim extend . . . to any non-federal claim that the plaintiff may have against the same defendant, so long as it bears the requisite relationship to the federal claims."[30] If such a relationship does exist, the doctrine of pendent jurisdiction gives a federal court discretion to exercise its jurisdiction over the non-federal claim in light of the degree of judicial economy and convenience to the parties which would be achieved.

Until recently, *Hurn v. Oursler*[31] governed the application of pendent jurisdiction to cases in federal courts. In *Hurn,* plaintiffs sought, under a federal statute, to enjoin infringement of their copyrighted play by the defendants and, under a state statute, to recover damages for unfair competition.[32] The trial court dismissed both claims—the federal claim on its merits and the state claim for lack of jurisdiction.[33] The court of appeals affirmed.[34] However, the United States Supreme Court found the district court in error. It held that the unfair competition claim, founded on a state statute, should have been dismissed on its merits rather than for lack of jurisdiction.[35] In other words, the Court concluded that the federal copyright claim had provided a sufficient basis for the adjudication of the state claim regarding unfair competition. Perhaps even more significant was the adoption of a two-part test for determining the existence of a pendent claim. First, the federal claim must not be "plainly wanting in substance."[36] Second, the federal and state claims must constitute "two distinct grounds in support of a single cause of action" rather than "two separate and distinct causes of action."[37]

For more than three decades, lower federal courts had great difficulty interpreting the *Hurn* "single cause of action" test. While some

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[29]UMW v. Gibbs, 383 U.S. 715 (1966); Hurn v. Oursler, 289 U.S. 238 (1933). However, in 1948, Congress enacted a law to govern the application of pendent jurisdiction with regard to copyright, patent, and trademark cases. 28 U.S.C. § 1338(b) (1964) (originally enacted as Act of June 25, 1948, ch. 646, § 1338(b), 62 Stat. 931).

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

[31]289 U.S. 238 (1933).

[32]A third count alleged infringement and unfair competition of a revised uncopyrighted version of the play. The Supreme Court affirmed the district court's jurisdictional dismissal of this claim.

[33]289 U.S. at 239-40. The district court opinion appears not to have been reported.

[34]Hurn v. Oursler, 61 F.2d 1031 (2d Cir. 1932) (per curiam).

[35]289 U.S. at 147-48.

[36]*Id.* at 246.

[37]*Id.*

courts required almost complete proof of identical facts in order to apply pendent jurisdiction,[38] others required merely a substantial overlapping of proof.[39] The 1966 case of *UMW v. Gibbs*[40] provided the Court with an opportunity to discard the highly controversial *Hurn* tests. The Court, endeavoring to clarify the requisite relationship between state and federal claims, proposed the following standard:

> 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.[41]

Gibbs emphasized that although the trial court may find that the claims are so related as to grant power to hear the entire case, the trial court may nevertheless refuse to employ the pendent jurisdiction doctrine in situations where little "judicial economy, convenience and fairness to litigants" would result.[42]

The *Gibbs* court, striving not only to assure the rational exercise of discretion under the doctrine of pendent jurisdiction, but also to provide a measure of predictability for the plaintiff who desires to assert parallel federal and state rights, suggested certain guidelines for determining whether or not a non-federal claim should be deemed pendent. In formulating such standards, the Court recognized that federal courts should not, in the interest of comity between state and federal courts, determine issues which might more appropriately be left to state courts.[43] Thus,

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[38]*See, e.g.*, Armstrong Paint & Varnish Works v. Nu-Enamel Corp., 305 U.S. 315 (1938) ("substantially identical"); Brown v. Bullock, 194 F. Supp. 207 (S.D.N.Y. 1961); Darwin v. Jess Hickey Oil Corp., 153 F. Supp. 667 (N.D. Tex. 1957).

[39]This is the majority view in the patent, copyright, and trademark cases due to the provisions in 28 U.S.C. § 1338(b) (1964). *See, e.g.*, Travel Magazine, Inc. v. Travel Digest, Inc., 191 F. Supp. 830 (S.D.N.Y. 1961). The best expression of this interpretation of the *Hurn* "single cause of action" test is in the following opinions by Judge Clark: Kleinman v. Betty Dain Creations, Inc., 189 F.2d 546, 549 (2d Cir. 1951) (dissent); Musher Foundation, Inc. v. Alba Trading Co., 127 F.2d 9, 11 (2d Cir.) (dissent), *cert. denied*, 317 U.S. 641 (1942); Treasure Imports Inc. v. Henry Amdur & Sons, Inc., 127 F.2d 3 (2d Cir. 1942).

[40]383 U.S. 715 (1966).

[41]*Id.* at 725. It appears that pendent jurisdiction ("common nucleus of operative fact") and ancillary jurisdiction ("same occurrence or transaction") require virtually the same factual relationship among claims.

[42]*Id.* at 726.

[43]*Id.*

> [where] state issues substantially predominate, whether in terms of proof, of the scope of the issues raised, or of the comprehensiveness of the remedy sought, the state claims may be dismissed without prejudice and left for resolution to state tribunals.[44]

However, if the state issues turn on principles well-settled under state law, a federal court should be less hesitant to apply pendent jurisdiction. On the other hand, if there is some uncertainty as to the state law, the federal court should limit its adjudication to the federal claim since the state courts are best equipped to explore new areas of state law.[45] Finally, the *Gibbs* court indicated that federal courts may consider such extra-jurisdictional problems as the possibility of jury confusion in treating the "divergent legal theories of relief" that under Federal Rule 42(b) would justify separating the state and federal claims for trial.[46] If there is the likelihood of such confusion, the federal court should decline to exercise pendent jurisdiction. By proposing such criteria, the *Gibbs* court moved to replace the rigid dual requirement of *Hurn* with a more flexible means of determining the existence of pendent claims.

Using the *Gibbs* analysis, the *Ayoub* court found it could deny plaintiff's motion to amend his complaint to assert a claim directly against the third-party defendant on two grounds. First, *Gibbs* required that the original action involve a federal claim. Since the principal action in *Ayoub* was based on diversity of citizenship, there was no *power* to invoke the doctrine of pendent jurisdiction.[47] In the alternative, even if pendent jurisdiction were determined by a higher court to extend to diversity actions, the *Ayoub* court would nevertheless decline to exercise its *discretion* to apply the doctrine since it would be adjudicating claims which belonged in state courts.

Thus, neither the doctrine of ancillary jurisdiction nor the doctrine of pendent jurisdiction convinced the *Ayoub* court to grant plaintiff's motion. Although *Gibbs* has precluded the use of pendent jurisdiction in a federal court in order to permit plaintiff to assert a direct claim against a co-citizen, third-party defendant where the original action is based on diversity of citizenship, it is likely that future courts might allow third-party claims in such a situation if the plaintiff presses the persuasive arguments in favor of the doctrine of ancillary juris-

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[44] *Id.* at 726-27.

[45] *See,* Wechsler, *Federal Jurisdiction and the Revision of the Judicial Code,* 13 LAW & CONTEMP. PROB. 216, 223 (1948).

[46] 383 U.S. 715 (1966).

[47] *See, e.g.,* Olivieri v. Adams, 280 F. Supp. 428 (E.D. Pa. 1968).