

1989

Western Capital and Securities v. Knudsvig : Petition for Writ of Certiorari

Utah Supreme Court

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Craig F. McCullough; Callister, Duncan & Nebeker; attorney for respondent.

Gerald S. Wight; Vlahos, Sharp, Wight & Walpole; attorney for petitioner.

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UTAH SUPREME COURT
BRIEF

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DOCKET NO: 890132 IN THE SUPREME COURT OF THE
STATE OF UTAH

Petitioner.

CASE NO:

CASE NO: 890132

(CATEGORY NO. 14)

GERALD S. WIGHT, #3461
VLAHOS, SHARP, WIGHT & WALPOLE
Legal Forum Building
2447 Kiesel Avenue
Ogden, Utah 84401
(801) 621-2464

Attorney for Petitioner

CRAIG F. McCULLOUGH, #2166
185 South State, Suite 520
P.O. Box 11378
Salt Lake City, Utah 84147-0378

Attorney for Respondent

FILED

APR 10 1989

Clerk, Supreme Court, Wash.

IN THE SUPREME COURT OF THE
STATE OF UTAH

WESTERN CAPITAL AND)	
SECURITIES, INC.,)	PETITION FOR A
)	WRIT OF CERTIORARI
Respondent,)	
)	
vs.)	CASE NO: _____
)	
HELEN KNUDSVIG,)	
)	
Petitioner.)	(CATEGORY NO. 14)

Petitioner, Helen Knudsvit's Petition for a
Write of Certiorari to the
Utah Supreme Court

GERALD S. WIGHT, #3461
VLAHOS, SHARP, WIGHT & WALPOLE
Legal Forum Building
2447 Kiesel Avenue
Ogden, Utah 84401
(801) 621-2464

Attorney for Petitioner

CRAIG F. McCULLOUGH, #2166
185 South State, Suite 520
P.O. Box 11378
Salt Lake City, Utah 84147-0378

Attorney for Respondent

LIST OF PARTIES

Helen Knudsvig, an individual, is the Petitioner herein and was the Defendant in the Trial Court and was Respondent in the Utah Court of Appeals.

Western Capital and Securities, Inc. is the Respondent and was the Plaintiff in the Trial Court and the Appellant in the Utah Court of Appeals.

TABLE OF CONTENTS

LIST OF PARTIES.....	i
TABLE OF CONTENTS.....	ii
TABLE OF AUTHORITIES.....	iii
QUESTIONS PRESENTED FOR REVIEW.....	1
GROUND FOR JURISDICTION.....	1
STATEMENT OF THE CASE.....	1
ARGUMENT.....	7
POINT I.	
THIS COURT SHOULD REVIEW BY WRIT OF CERTIORARI THE DECISION OF THE UTAH COURT OF APPEALS IF ONE OF THE CONSID- ERATIONS OF RULE 43 OF THE RULES OF THE UTAH SUPREME COURT IS MET.....	7
POINT II.	
THAT WHETHER A VIOLATION OF ASSOCIATION BROKERAGE RULES GIVES RISE TO A QUESTION OF STATE OR FEDERAL LAW WAS ERRONEOUSLY DECIDED BY THE COURT OF APPEALS.....	9
CONCLUSION.....	10
ADDENDUM.....	A-1
CERTIFICATE OF MAILING.....	11

TABLE OF AUTHORITIES

CASE CITATIONS

<u>Cowen and Co. v. Atlas Stock Trasnfer Co.,</u> <u>695 P.2d 109 (Utah 1984)</u>	8,10
--	------

STATUTES CITED

15 USCS § 78o-3(b)-(6)	9
Securities Exchange Act of 1934, § 15a(b)(6) ..	9
Uniform Commercial Code § 70A-8-315	8
Uniform Commercial Code § 70A-8-319	8
Uniform Commercial Code § 70A-8-401	8
Utah Code Annotated § 78-2-2(3)(a) (1987)	1

RULES CITED

Rule 43 of the Rules of the Utah Supreme Court	1,7,9,10
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IN THE SUPREME COURT OF THE
STATE OF UTAH

WESTERN CAPITAL AND)	
SECURITIES, INC.,)	PETITION FOR A
)	WRIT OF CERTIORARI
Respondent,)	
)	
vs.)	CASE NO: _____
)	
HELEN KNUDSVIG,)	
)	
Petitioner.)	(CATEGORY NO. 14)

QUESTIONS PRESENTED FOR REVIEW

POINT I. Whether a violation of Federal Securities Law can be raised as a mandatory counterclaim in a State Court action.

POINT II. Whether a violation of Securities Dealers Rules gives rise to a federal question or a state court action.

GROUND FOR JURISDICTION

Jurisdiction of this Court is invoked pursuant to Utah Code Annotated §78-2-2(3)(a) and Rule 43 of the Rules of the Utah Supreme Court. The decision of the Court of Appeals was entered on February 7, 1989, and a thirty (30) day extension was granted by this Court March 8, 1989.

STATEMENT OF THE CASE

That the Petitioner is a 61 year old lady who has habitually dabbled in penny stocks, usually in the amount of

a few hundred dollars or less, investing in new issues which would hopefully achieve a quick rise in value. (T. 399) The Respondent attempted to establish that the Petitioner was an experienced and sophisticated investor, but this is contrary to the facts. (T. 555) In 1984 the Petitioner bought \$200.00 worth of penny stocks in a company known as Venture Consolidated, which amounted at that time to 20,000 shares. The particular stock was a new issue and a typical penny stock offering and the corporation Respondent was the market maker of the issue in any market which would follow. (T. 506, 517 and 549) The plan was to sell 100 million shares and insiders eventually captured 23% of the actual 200,000 plus shares which were sold while the public holding was to remain at 200,000. (T. 506, 517, 518 and 549)

The investment was to be held in cash with the plan to be that at a shareholders meeting a merger and consolidation with several other corporations would be made with the resulting entity to be known as Tires, Inc., authorizing a 20 to 1 reverse stock split, taking place immediately thereafter. The particular shareholders meeting to occur on September 19, 1984. (T. 531, 532) In the meantime, Venture Consolidated stock rose from one cent (1¢) to sixteen cents (16¢) or seventeen cents (17¢), the sole reason for the rise

being the proposed merger and the general market making activities of the Respondent brokerage. (T. 531, 532, 577, 600) The result of the activities of the Respondent and others with the consistent rise in value of Venture Consolidated and eventually Tires, Inc. stock. It resulted in the Petitioner's original \$200.00 investment being worth approximately \$30,000.00 and at the time of trial based again upon the general market making activities of the Respondent brokerage and/or other insiders activity. (T. 531, 571, 592-600)

That the Respondent had at all times maintained an Ogden office with an account executive in that office by the name of Lou Babcock who was well acquainted with the Respondent. (T. 461-471, 557) That Mr. Babcock visited with the Petitioner on September 14, 1984, and advised her of the stock's recent climb in value and offered to sell it for her, (T. 467) and that such a sale would bring on the recording an additional indication of an increase of fixed value for the market making activity and would serve also to pick up the stock in the face of what appeared to be high promotional activity in order to prevent profit taking before the explosion in value which was about to occur. (T. 531, 532, 571) While the motive to sell the stocks on

commission was no doubt present, any such commission would be very small.

That the Petitioner was excited about the potential rise in value and decided to obtain a second opinion by placing a call to the Respondent's Salt Lake office and requesting further information. (T. 443) That the broker who received the call interpreted the conversation to be a request for sale of shares and that he contacted the vice president for instructions on how to handle a sale inasmuch as there was no stock certificate with the Respondent brokerage. (T. 454, 455) In spite of the perceived difficulty, the vice president of the brokerage immediately approved the sale and the brokerage then made an entry that the purchase was made for their own market making account. (T. 451, 452)

That the Respondent failed to give notice of the transaction as required by its own agreement with the Petitioner in addition to other requirements of SEC rules and NASD rules. (T. 404, 459, 471, 435, 505)

That the Petitioner had no intention of making a sale of her shares and was aware of the fact that such a sale could not take place without the presence of a stock certificate. She had in the past had such a sale cancelled as opposed to having a purchase made by the brokerage to cover

what is known as a "short sale". (T. 565) One of the reasons Petitioner never received a stock certificate is that it would serve the personal interest of insiders market making activity to freeze outsiders and prevent their profit taking in interference with the stock's rise by making it more difficult to profit take. (T. 571) That regulations and the broker's contract itself with the Petitioner required a winding up and closing of all transactions within five (5) days after a sale or purchase occurred. (T. 552, 451, 455) That the Respondent made no effort to close in the required five (5) day period and that they in fact preferred not to do so, preferring instead to await further developments. (T. 456-458, 527-529)

That the stock rose uniformly through the next period of time without any drop below the sales price so that the brokerage position would not in any way be threatened. (T. 456-458, 527-529) That after approximately seventy-five (75) days when the Respondent decided to make a transfer purporting to cover the short, making an entry that they had bought from their own profit making account. (T. 523)

That this resulted in a paper calculation that if the sale was made in accordance with the original sales entry, that a short coverage was effected at the repurchase date and that the Petitioner would owe the \$5,400.00 claimed in

Respondent's Complaint because of the steady rise of the market during the intervening seventy-five (75) days and Respondent's daliance. That Respondent knew that it would not be closing within five (5) days, even assuming that the original sale had actually taken place, and let the matter ride at the Petitioner's risk and should now be estopped to make any claim against the Petitioner. (T. 451-459)

That the Respondent brokerage made all such transactions strictly to and from their own market making accounts and records with no threat to their position. (T. 451-459, 523, 524) That Petitioner's shares could not be sold without possession of the certificate. (T. 452-455)

On appeal, the Utah Court of Appeals made a sua sponte finding that the Trial Court lacked jurisdiction to hear or adjudicate any of the issues raised in Petitioner's Counterclaim. The Court found that even though such Counterclaim was a mandatory Counterclaim, that it could not raise a matter of violation of Federal Securities Laws, which it found to be reserved exclusively to the Federal Courts.

That at the same time, the Utah Court of Appeals also found that violation of the NASD Rules governing brokerages and dealers was also an exclusive Federal question since a provision of the Federal Securities Laws required the formulation of such rules. The Utah Court of Appeals

therefore denied any damages as awarded by the Trial Court and found that the Trial Court had no jurisdiction to award the same.

ARGUMENT

POINT I.

THIS COURT SHOULD REVIEW BY WRIT OF CERTIORARI THE DECISION OF THE UTAH COURT OF APPEALS IF ONE OF THE CONSIDERATIONS OF RULE 43 OF THE RULES OF THE UTAH SUPREME COURT IS MET.

This Court can review by Writ of Certiorari a decision of the Utah Court of Appeals when there are special important reasons therefore. Rule 43 lists four different categories of what the Court will consider in granting a Writ of Certiorari and the Petitioner believes that three of the four grounds stated in Rule 43 would apply in this case.

(2) "When a panel of the Court of Appeals has decided a question of state or federal law in a way that is in conflict with a decision of this court;

(3) When a panel of the Court of Appeals has rendered a decision that has so far departed from the accepted and usual course of judicial proceedings or has so far sanctioned such a departure by a lower court as to call for an exercise of this court's power of supervision; or

(4) When the Court of Appeals has decided an important question of municipal, state, or federal law which has not been, but should be, settled by this court.

In this matter, the Utah Court of Appeals denied that a State Court would have jurisdiction to adjudicate a question of Federal law even though such question might be found to be in the nature of a mandatory Counterclaim. The Petitioner is unaware of any other rulings of this Court which have specifically addressed the question and believes it involves an important question to be resolved.

That such question was raised sua sponte on the part of the Court of Appeals as it was not raised by either Respondent or Petitioner during the course of that appeal.

Petitioner believes that the decision of the Court of Appeals is in conflict with this Court's decision in the case of Cowen and Co. v. Atlas Stock Transfer Co., 695 P.2d 109 (Utah 1984), and cases which have interpreted the State of Utah's version of the Uniform Commercial Code as found in §§ 70A-8-315 and 70A-8-319 and 70A-8-401.

That at a minimum, the Utah Court of Appeals should have remanded the matter to the Trial Court to find if any relief could have been granted based upon a State Court question, particularly in view of the Court's decision in Cowen and Co., v. Atlas Stock Transfer Co., Supra.

That the Court of Appeals has decided an important question in the conflict of State and Federal law, which has not been but should be, settled by this Court as to whether

the Courts of this State have the jurisdiction to rule on questions of Federal Securities laws and whether violation of the rules of a particular exchange or brokerage are violated gives rise to a Federal or State Court cause of action.

The Petitioner would request that this Honorable Court grant a review by a Writ of Certiorari of the Utah Court of Appeals case under considerations (2), (3) and (4) as set forth above.

POINT II.

THAT WHETHER A VIOLATION OF ASSOCIATION
BROKERAGE RULES GIVES RISE TO A QUESTION
OF STATE OR FEDERAL LAW WAS ERRONEOUSLY
DECIDED BY THE COURT OF APPEALS.

The Court of Appeals attempts to make an assumption as the basis for excluding the Counterclaim of the Petitioner that is not justified by the law. The Court of Appeals makes reference to "§ 15a(b)(6) of the Securities Exchange Act of 1934, 15 USCS § 78o-3(b)-(6), 1981, as requiring securities associations such as NASD to adopt disciplinary rules. Even if this were to be found to be a specific requirement, it does not give rise to a Federal question.

The Federal Courts are courts of limited jurisdiction and their jurisdiction is limited to those areas specifically prescribed by the Constitution and acts of congress.

Unless a specific and exclusive granting of jurisdiction is to be found in the Constitution or acts of congress, there is no jurisdiction on the part of the Federal Courts.

This Court has previously apparently decided a similar issue on appeal in the case of Cowen and Co. v. Atlas Stock Transfer Co., 695 P.2d 109 (Utah 1984), but not withstanding that, the Court of Appeals attempts to say that neither this Court or any other Court in the State of Utah may adjudicate or rule upon such issues. That such a finding on the part of the Court of Appeals is not justified, particularly in view of the previous rulings of this Court.

CONCLUSIONS

This Court should grant a Writ of Certiorari based upon Subsections (2), (3) and (4) of Rule 43 of the Rules of the Utah Supreme Court to allow this Court to exercise its power of supervision and to resolve important questions regarding conflicts between State and Federal law, and questions of State Court jurisdiction.

DATED this 8th day of April, 1989.

Gerald S. Wight
GERALD S. WIGHT
Attorney for Petitioner

Recorded Book	137
Page	1295
Indexed	

GERALD S. WIGHT, #3461
 VLAHOS & SHARP
 Attorney for Defendant
 Legal Forum Building
 2447 Kiesel Avenue
 Ogden, Utah 84401
 Telephone: 621-2464

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IN THE DISTRICT COURT OF WEBER COUNTY
 STATE OF UTAH

WESTERN CAPITAL AND
 SECURITIES, INC.,

Plaintiff,

-vs-

HELEN KNUDSVIG,

Defendant.

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JUDGMENT

CIVIL NO: 92290

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This matter having come before the Court for trial on the 16th day of October, 1986, at the hour of 9:30 a.m., the Court having taken the matter under advisement at the close of testimony and oral argument, and having previously rendered its Memorandum Decision and entered Findings of Fact and Conclusions of Law, does hereby award judgment as follows:

1. That the Complaint of the Plaintiff is dismissed no cause of action.

2. That the Defendant is the sole owner of the 20,000 shares of Venture Consolidated which has since been

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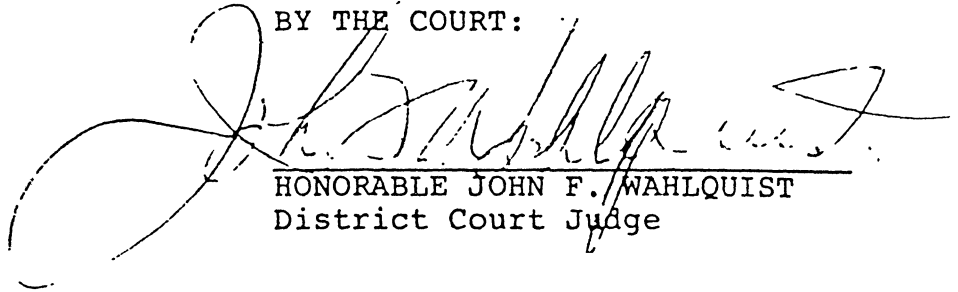
converted by the company to 1,000 shares of Tires, Inc., and has been at all times and places in that the Plaintiff has not and does not have any claim whatsoever on said shares or against the Defendant.

3. That the Plaintiff has acted in violation of Rule 10B(5) and 10B(10) of the Securities Exchange Act of 1934 and the NASD Rules of which the Plaintiff is a member and has further acted in a manner so as to deceive and cheat the public in general and the Defendant in particular by its involvement and hold and control over the subject corporation with the knowledge and inside information of its dealings in up coming business activities, and has used all such to the detriment and damage of the Defendant in attempting to convert her stock, all in violation of all applicable rules and regulations thus entitling the Defendant to judgment against the Plaintiff in the amount of \$10,000.00 punitive damage in addition to costs of Court in the amount of \$35.00.

4. It is further Ordered that Interwest Transfer or any other entity which has previously been served with or notified of any restraining order restraining the obtaining of the certificate by the Defendant shall forthwith release any such certificate and issue the same to the Defendant upon appropriate application.

DATED this 10 day of October, 1986.

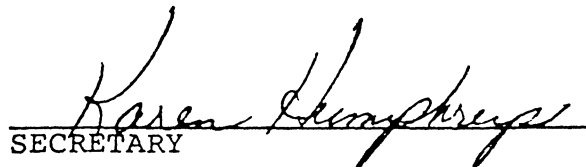
BY THE COURT:


HONORABLE JOHN F. WAHLQUIST
District Court Judge

CERTIFICATE OF MAILING

I HEREBY CERTIFY that on this 20 day of October, 1986, I mailed a true and correct copy of the above and foregoing JUDGMENT by placing same in the U.S. Mail postage prepaid and addressed to the following:

Craig F. McCullough
Attorney for Plaintiff
185 South State Street, #528
Salt Lake City, Utah 84111


SECRETARY

297

TITLE VI. JURISDICTION ON WRIT OF CERTIORARI TO COURT OF APPEALS.

Rule 42. Review of judgments, orders, and decrees of Court of Appeals.

Unless otherwise provided by law, the review of a judgment, an order, and a decree (herein referred to as "decisions") of the Court of Appeals shall be initiated by a petition for a writ of certiorari to the Supreme Court of Utah. (Added, effective April 20, 1987.)

Rule 43. Considerations governing review of certiorari.

Review by a writ of certiorari is not a matter of right, but of judicial discretion, and will be granted only when there are special and important reasons therefor. The following, while neither controlling nor wholly measuring the court's discretion, indicate the character of reasons that will be considered:

- (1) When a panel of the Court of Appeals has rendered a decision in conflict with a decision of another panel of the Court of Appeals on the same issue of law;
 - (2) When a panel of the Court of Appeals has decided a question of state or federal law in a way that is in conflict with a decision of this court;
 - (3) When a panel of the Court of Appeals has rendered a decision that has so far departed from the accepted and usual course of judicial proceedings or has so far sanctioned such a departure by a lower court as to call for an exercise of this court's power of supervision; or
 - (4) When the Court of Appeals has decided an important question of municipal, state, or federal law which has not been, but should be, settled by this court.
- (Added, effective April 20, 1987.)

Rule 44. Certification and transmission of record; filing; parties.

(a) **Appearance, docketing fee, filing, and service.** Counsel for the petitioner shall, within the time provided by Rule 45, pay the certiorari docketing fee and file, with proof of service as provided by Rule 21, ten copies of a petition which shall comply in all respects with Rule 46. The case then will be placed on the certiorari docket of the court. Counsel for the petitioner shall serve four copies of the petition on counsel for each party separately represented. It shall be the duty of counsel for the petitioner to notify all parties in the case of the date of filing and of the certiorari docket number of the case. Service and notice shall be given as required by Rule 21.

(b) **Joint and separate petitions.** Parties interested jointly, severally, or otherwise in a decision may join in a petition for a writ of certiorari; any one or more of them may petition separately; or any two or more of them may join in a petition. When two or more cases are sought to be reviewed on certiorari and involve identical or closely related questions, it will suffice to file a single petition for a writ of certiorari covering all the cases

IN THE UTAH COURT OF APPEALS

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Western Capital and Securities,)
Inc.,)
)
Plaintiff and Appellant,)
)
v.)
)
Helen Knudsvig,)
)
Defendant and Respondent.)

OPINION
(For Publication)

Case No. 880198-CA

FILED

FEB 7 1989
Mary T. Noonan
Mary T. Noonan
Clerk of the Court
Utah Court of Appeals

Second District, Weber County
The Honorable John F. Wahlquist
Attorneys: Craig F. McCullough, Salt Lake City, for Appellant
Gerald S. Wight, Ogden, for Respondent

Before Judges Billings, Garff and Jackson.

GARFF, Judge:

Plaintiff and appellant, Western Capital and Securities, Inc. (Western), filed an action to recover \$5,402.20 damages incurred when defendant and respondent, Helen Knudsvig, failed or refused to deliver a stock certificate after she allegedly requested Western to sell stock for her. Knudsvig counter-claimed, alleging that Western had violated Rules 10b-5 and 10b-10 promulgated under § 10(b) of the Securities and Exchange Act of 1934, and various rules of the National Association of Securities Dealers (NASD). We affirm in part and reverse in part.

Western is a broker-dealer registered with the United States Securities and Exchange Commission and the Utah Securities Division. Knudsvig is a sixty-one-year-old customer who occasionally purchased penny stocks through Western and other brokerage firms. The trial court found that she was not a sophisticated investor and only traded a few hundred dollars worth of stock per year.

The conditions in the brokers' contract between Western and Knudsvig required settlement of all transactions five days after a sale or purchase. The relevant provisions read:

4. All transactions shall be settled by the fifth full business day following the sale or purchase . . . and at your option, if you shall not have received cash for the securities purchased for my account or delivery of the securities sold for my account, appropriately endorsed and in proper negotiable form, on the fifth full business day following the purchase or sale, as the case may be, you shall have the right, either with or without demand upon or notice to me, such demand or notice being expressly waived, to close my account, or any trade or transaction included herein on any such exchange or market, at public or private sale, or by public or private purchase, with or without advertising such sale or purchase, such advertising being hereby expressly waived, and such sale or purchase may be made in one or a series of sales or purchases as you may elect.

5. You are authorized to accept from me oral or telephonic orders for the purchase or sale of securities and in consideration of your acceptance of this agreement, I hereby waive any defense that I may have because any such order was not in writing or evidenced by a memorandum in writing as required by the Statute of Frauds, or other statute.

9. Communications of every kind referring in any way to my account may be sent to me at my address given hereon . . . and all communications so sent, whether by mail, telegraph, messenger or otherwise, shall be deemed given to me personally whether actually received by me or not.

Kim Johnson, secretary/treasurer of Western, testified that this language meant that, on the fifth business day following

the sale or purchase, Western had the option (1) to close the transaction by buying in, or (2) to allow the contract to remain open.

In about June 1983, Knudsvig purchased 20,000 shares of Venture Consolidated, Inc. (Venture) for \$200 through Western. This offering was a new issue of penny stock for which Western was a market maker. Knudsvig claimed that she never received a stock certificate, but had attempted to obtain a duplicate certificate in August or September of 1983 and also in November of 1984.

In July 1984, Venture shareholders approved an acquisition and merger with several Big O Tire franchises. They changed the name of the corporation to Tires, Inc. and approved a 20 to 1 reverse stock split. On September 14, 1984, Louis Babcock, Western's Ogden representative, who was acquainted with Knudsvig through past dealings, notified Knudsvig that her Venture shares had increased in value from \$.01 to \$.17 per share, and asked her if she wanted to sell. Knudsvig declined. Later, excited about the rise in value of her stock, she unsuccessfully attempted to contact Babcock. She then contacted Western's office in Salt Lake City and spoke to Richard Davis. After a lengthy discussion, Davis concluded that Knudsvig wanted to sell her stock and wished to credit the sales commission to Babcock. While Knudsvig was still on the telephone, Davis contacted Richard C. Parker, Western's executive vice president, for instructions on how to consummate the transaction, which was complicated by Knudsvig's confusion, the lack of a stock certificate, and having to credit the commission to Babcock. Parker, in spite of these difficulties, immediately approved the purchase from Knudsvig for \$.16114 per share through Western's market making account. Davis returned to the phone, informed Knudsvig of the sale and selling price, and told her that she had to mail in the stock certificate. He informed her that it was possible for a trade to take place without possession of the certificate since she had ten [sic] days after the trade to bring in the certificate. Parker stated that the sale was handled in this manner because Knudsvig was an established, sophisticated customer who had paid for and delivered stock in a timely manner over a long period of time.

Knudsvig disputes Davis's statements, although her testimony is somewhat unclear. Initially, she denied that this phone call ever took place, but then admitted to making the call. She denied that she ever requested the sale of her

stock. She further testified that she had no intention of making a sale, thought that Western could not sell her stock without possession of the certificate, and in 1983, Western had cancelled a similar sale because she could not find her stock certificate. The trial court found that she had assumed there could be no final sale until she was able to get a stock certificate.

Knudsvig stated that, at this point, she was unaware that her stock had been sold because she never received a written confirmation of the sale. Western, however, stated that, within the five day period following the sale, it had sent a written confirmation to Knudsvig's address. Western did not close Knudsvig's account for seventy-five days after the purported sale, at which time the value of the stock had risen to \$8.00 per share.¹ Johnson testified that Western had waited for this unusually long period of time to cover Knudsvig's short position because she was a good customer, she had indicated that she was replacing the certificate, and Johnson thought that he was acting in Knudsvig's best interest. Western's eventual buy-in resulted in a \$5,402.20 deficit in Knudsvig's account, which is the basis for Western's complaint.

In its memorandum decision, entered on October 23, 1986, the trial court found that Knudsvig continued to be the owner of the stock, that the alleged sale never occurred, and that Western's activity was unconscionable. The trial court dismissed Western's complaint and awarded punitive damages to Knudsvig in the amount of \$10,000.

Appellant asserts that the trial court erred: (1) in finding that Knudsvig did not authorize the sale of her stock; (2) in finding that Western violated Rules 10b-5 and 10b-10 of the Securities Exchange Act of 1934; (3) in finding that Western violated various National Association of Securities Dealers (NASD) rules, and in finding that there is a private right of action for violation of NASD rules; and (4) in awarding punitive damages.

The trial court's findings of fact will not be disturbed on appeal unless they "are against the clear weight of the evidence, or if the appellate court otherwise reaches a

1. At the time of the trial, October 16, 1986, the value of the stock was approximately \$30.00 per share.

definite and firm conviction that a mistake has been made." State v. Walker, 743 P.2d 191, 193 (Utah 1987); see also Cove View Excavating & Const. Co. v. Flynn, 758 P.2d 474, 477 (Utah Ct. App. 1988). Factual findings are given considerable deference because of the trial court's ability to assess the witnesses's credibility. Utah R. Civ. P. 52(a); Power Systems, 97 Utah Adv. Rep. at 36; Southland Corp. v. Potter, 760 P.2d 320, 321 (Utah Ct. App. 1988). Findings of fact are clearly erroneous if the appellant can show that they are without adequate evidentiary foundation or if they are induced by an erroneous view of the law. State v. Walker, 743 P.2d 191, 193 (Utah 1987).

In carefully examining the record, we note that there is much conflicting evidence and inconsistent testimony, especially regarding Knudsvig's telephone call to Western, in which Knudsvig purportedly authorized the sale of her stock, and regarding whether or not Knudsvig received written confirmation of the alleged sale from Western. The trial court found that Knudsvig had no intention of selling her stock, that she was the rightful owner of the 20,000 shares of Venture stock, and that Western failed to establish, by a preponderance of the evidence, that written notice of the transaction was mailed to Knudsvig.

In essence, Western argues that the trial court should have believed its evidence rather than Knudsvig's. However, the clear weight of the evidence supports the trial court's findings that the sale was not authorized and did not take place, and we defer to the trial court's advantaged position in evaluating the witnesses's demeanor and credibility. We find no error in the court's rulings on this issue.²

JURISDICTION

Western asserts that the trial court erred in finding that it violated Rules 10b-5 and 10b-10 of the Securities Exchange

2. Although Knudsvig raises affirmative defenses to Western's action under Utah Code Ann. § 70A-8-301, the Securities Exchange Act of 1934 § 10b-10, and § 12 of the NASD manual, we do not consider them because: (1) we sustain the trial court's finding that no sale of the securities occurred, thus obviating the need for a defense to the sale, and (2) the parties did not raise the issue on appeal.

Act of 1934 and various NASD rules. Before we examine the merits of this argument, however, we raise sua sponte the issue of subject matter jurisdiction over this claim. As stated in Carreathers v. Carreathers, 654 P.2d 871 (Colo. Ct. App. 1982),

[t]he parties have not raised the issue of . . . subject matter jurisdiction . . . in the trial court or in this appeal. However, the question of subject matter jurisdiction may be raised at any stage of an action without an assignment of error, and an appellate court may decide a question of subject matter jurisdiction where it appears on the face of the record.

Id. at 871; see also Thompson v. Jackson, 743 P.2d 1230, 1232 (Utah Ct. App. 1987). Furthermore, "this Court may, on its own motion, determine lack of jurisdiction." Bailey v. Sound Lab, Inc., 694 P.2d 1043, 1044 (Utah 1984); see also State v. Brandimart, 720 P.2d 1009, 1010 (Haw. 1986). "Jurisdiction cannot be conferred upon this Court by stipulation" of the parties. Bailey, 649 P.2d at 1044.

Exclusive jurisdiction over causes of action stemming from violations of the Securities Exchange Act of 1934 is vested in the federal courts. The 1934 Act, at 15 U.S.C. § 78aa (1981), states in relevant part:

The district courts of the United States . . . shall have exclusive jurisdiction of violations of this chapter or the rules and regulations thereunder. . . . Any suit or action to enforce any liability or duty created by this chapter or rules and regulations thereunder . . . may be brought in any such district or in the district wherein the defendant is found or is an inhabitant

Federal courts generally interpret this statute to mean what it says: federal jurisdiction is exclusive over actions brought to enforce the 1934 Act. See, e.g., Securities Investor Protection Corp. v. Vigman, 764 F.2d 1309, 1313 (9th Cir. 1985); DeHaas v. Empire Petroleum Co., 435 F.2d 1223, 1231 (10th Cir. 1971); Alkoff v. Gold, 611 F. Supp. 63, 66 (S.D.N.Y. 1985); Kinsey v. Nestor Exploration Ltd.--1981A, 604 F. Supp. 1365, 1368-69 (E.D. Wash. 1985); Fradkin v. Ernst, 571 F. Supp.

829, 839 (N.D. Ohio 1983); Kleckley v. Hebert, 464 So. 2d 39, 41 (La. Ct. App. 1985).

There is a split in authority as to whether the 1934 Act can be used as an affirmative defense in state actions. Some jurisdictions assert that state courts do not have jurisdiction to adjudicate federal securities law questions brought under the 1934 Act, even when raised as an affirmative defense. Instead, they "squarely endorse" the proposition that "[w]here exclusive jurisdiction exists, only the federal courts can provide affirmative relief." Alkoff, 611 F. Supp. at 66 (quoting Levy v. Lewis, 635 F.2d 960, 967 (2nd Cir. 1980)).

While recognizing that the statute precludes state court adjudication of direct claims based upon the violation of the 1934 Act, other jurisdictions allow state courts to consider claims based on the 1934 Act which are raised as affirmative defenses in state court actions. Andrea Theatres, Inc. v. Theatre Confections, Inc., 787 F.2d 59, 63 (2nd Cir. 1986); Scope Indus. v. Skadden, Arps, Slate, Meagher & Flom, 576 F. Supp. 373, 379 (C.D. Cal. 1983); Birenbaum v. Bache & Co., 555 S.W.2d 513, 514-15 (Tex. Civ. App. 1977).

Even so, these jurisdictions do not allow state courts to grant affirmative relief to a defendant who prevails on such federal claims, but, instead, force the defendant to go to federal court to seek affirmative relief. Andrea Theatres, 787 F.2d at 63. Further, these jurisdictions distinguish between "cases," wherein state determination is precluded, and "questions," which the state may adjudicate, which arise under the 1934 Act. Scope Indus., 576 F. Supp. at 378-79; Birenbaum, 555 S.W.2d at 515. The Birenbaum court adopted the United States Supreme Court's reasoning regarding jurisdiction over patent claims in making this distinction:

There is a clear distinction between a case and a question arising under the patent laws. The former arises when the plaintiff in his opening pleading--be it a bill, complaint, or declaration--sets up a right under the patent laws as ground for a recovery. Of such the state courts have no jurisdiction. The latter may appear in the plea or answer or in the testimony. The determination of such question is not beyond the competency of the state tribunals.

Birenbaum, 555 S.W.2d at 515 (quoting Pratt v. Paris Gaslight & Coke Co., 168 U.S. 255, 259 (1897) (emphasis in Birenbaum)). The Birenbaum court found that the state court was competent to adjudicate a 10b-5 violation issue because it "only appeared by way of defense, it is merely a question in the case, rather than a claim for relief." Birenbaum, 555 S.W.2d at 515.

Similarly, the Scope Industries court, in determining that the state court had jurisdiction to consider a defense based on the 1934 Act, also distinguished between cases, which the state court could not adjudicate, and questions, which the state court was competent to consider. It stated that whether a "colorable claim existed under the Exchange Act at the commencement of the underlying action is different in kind than the question of whether or not Scope violated the Exchange Act, as alleged in the underlying action." Scope Indus., 756 F. Supp. at 378-79.

We do not find it necessary today to decide which of these lines of cases we will follow. Although Knudsvig asserted Rule 10b-10 as an affirmative defense, her claims under the 1934 Act were brought in the form of a counterclaim for violation of Rule 10b-5 as well as Rule 10b-10. Thus, even under the more liberal authority, she does not qualify jurisdictionally. These claims are in the nature of a case rather than a question and, accordingly, we do not have jurisdiction to consider them.

VIOLATION OF NASD RULES

Section 15A(b)(6) of the Securities Exchange Act of 1934, 15 U.S.C. § 78o-3(b)(6) (1981), requires securities associations, such as the NASD, to adopt disciplinary rules. See Emmons v. Merrill, Lynch, Pierce, Fenner & Smith, Inc., 532 F. Supp. 480, 483 (S.D. Ohio 1982). Section 15 U.S.C. § 78s(g) requires that "[e]very self-regulatory organization shall comply with the provisions of this chapter, the rules and regulations thereunder, and its own rules." Thus, the NASD comes under the regulatory provisions of the Act and is subject to the exclusive jurisdiction provision of 15 U.S.C. § 78o(a). Therefore, any action based on violation of NASD rules must be brought in the federal courts.

That Knudsvig's counterclaim may be construed to be compulsory under Utah R. Civ. P. 13(a) still does not confer jurisdiction upon this Court to hear the merits of her claim. "A party is not required to file a compulsory counterclaim in

the district court if the claim exceeds the jurisdiction of that court." Brewer v. Bradley, 431 So. 2d 544, 545 (Ala. Civ. App. 1983).³

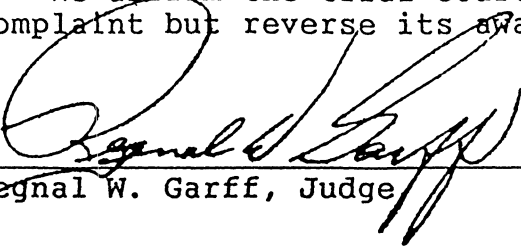
To summarize, Knudsvig's counterclaim relies exclusively upon alleged violations of the 1934 Act and NASD rules, which are regulated under the 1934 Act, all of which come under exclusive federal jurisdiction. Once we have determined that we have no jurisdiction over a claim, all we may do is dismiss the action. See In re Marriage of Passiales, 144 Ill. App. 3d 629, 494 N.E.2d 541, 547, 98 Ill. Dec. 419 (1986); Wells v. Noldon, 679 S.W.2d 889, 891 (Mo. Ct. App. 1984). Therefore, we dismiss Knudsvig's entire counterclaim.

PUNITIVE DAMAGES

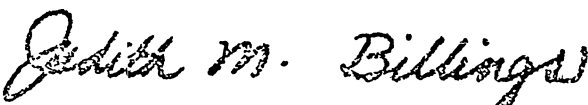
The trial court dismissed Western's complaint and, even though the court failed to find any actual damages stemming from the alleged violations of the Securities Exchange Act of 1934 in Knudsvig's counterclaim, it awarded punitive damages to Knudsvig. Since we have found that the trial court had no jurisdiction to hear the counterclaim, it follows that Knudsvig's associated request for damages fails. See Howard v. Miller, 108 Ill. App. 3d 1, 438 N.E.2d 680, 685, 63 Ill. Dec. 749 (1982); see also DeWitt County Pub. Bldg. Comm'n v. County of DeWitt, 128 Ill. App. 3d 11, 469 N.E.2d 689, 694, 83 Ill. Dec. 82 (1984). Further, "a court without jurisdiction cannot order affirmative relief." Chadwick v. Pillard, 536 F. Supp. 73, 75 (E.D. Tenn. 1982). Therefore, the trial court could not award punitive damages.

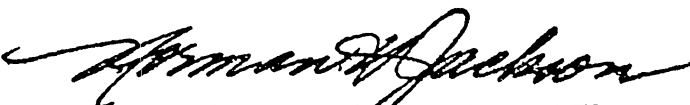
3. Federal practice is similar: If a federal court has jurisdiction over a plaintiff's claim, it will also have jurisdiction over a counterclaim arising from the same action or occurrence. However, "if the counterclaim is entirely beyond the competence of the federal courts, as for example, an action precluded by sovereign immunity or one involving a purely probate matter, the court may not adjudicate it even if the claim would otherwise be treated as compulsory." Wright & Miller, Federal Practice & Procedure, § 1414 at 72 (1971).

We affirm the trial court's dismissal of Western's complaint but reverse its award of punitive damages.


Regnal W. Garff, Judge

WE CONCUR:


Judith M. Billings, Judge


Norman H. Jackson, Judge

CERTIFICATE OF MAILING

I HEREBY CERTIFY that on this 10th day of April, 1989, I mailed four (4) true and correct copies of the above and foregoing PETITION FOR A WRIT OF CERTIORARI by placing same in the U.S. Mail postage prepaid and addressed to the following:

Craig F. McCullough
Attorney for Respondent
185 South State, Suite 520
P.O. Box 11378
Salt Lake City, Utah 84147-0378

Donald A. Wright