RIGHT TO JURY TRIAL IN SHAREHOLDER DERIVATIVE SUITS

While the question of a constitutional right to jury trial in a civil action is infrequently litigated, it presents some of the most evasive issues, both technical and historical, of our merged federal practice.[1] The Supreme Court in *Ross v. Bernhard*,[2] faced with determining the effect of the merger of law and equity upon the right to jury trial in a suit which is historically equitable in nature,[3] held that legal issues in a stockholders' derivative suit are triable to a jury. The right to a jury trial is grounded in the seventh amendment to the Constitution, adopted in 1791, which guarantees that "in suits at common law . . . the right of trial by jury shall be preserved . . . ."[4] In the years immediately subsequent to 1791 it was a relatively simple task to determine whether the constitutional guaranty extended to civil actions, but the constant development and sophistication of our legal system, culminating in the merger of law and equity, has created problems not contemplated by the drafters of the seventh amendment. The result has been a considerable amount of confusion regarding the scope of the seventh amendment, and the stockholder's derivative suit, apparently unknown in 1791,[5] is a paradigm of this uncertainty.

The suit in *Ross* was instituted by two shareholders against the directors of their closed-end investment company and the cor-

1. *See generally* James, *Trial by Jury and the New Federal Rules of Procedure*, 45 YALE L.J. 1022 (1936); James, *Right to Jury Trial in Civil Actions*, 72 YALE L.J. 655 (1963) [hereinafter cited as James]. In contrast to the civil area, there has been a great deal of litigation concerning the right to a jury trial in criminal matters. *See, e.g.*, Williams v. Florida, 399 U.S. 78 (1970); Baldwin v. New York, 399 U.S. 66 (1970); Bloom v. Illinois, 391 U.S. 194 (1968); Duncan v. Louisiana, 391 U.S. 145 (1968); Fucini v. Illinois, 44 Ill. 2d 305, 255 N.E.2d 380 (1970).

2. 396 U.S. 531 (1970), *noted in Derivative Actions and the Seventh Amendment*, 18 WASH. & LEE L.R. 344 (1970).

3. See notes 46-52 *infra* and accompanying text.

4. The seventh amendment reads:

"In suits at common law, where the value in controversy shall exceed twenty dollars, the right of trial by jury shall be preserved, and no fact tried by a jury, shall be otherwise re-examined in any Court of the United States, than according to the rules of the common law." U.S. CONST. amend. VII.

5. Foss v. Horbottle, 67 Eng. Rep. 189, 203 (Ch. 1843), apparently was the first reported ease to recognize the derivative suit as it is known today. The United States Supreme Court acknowledged the suit in 1855. Dodge v. Woolsey, 59 U.S. (18 How.) 331 (1855). Earlier cases allowed shareholders' suits under a trust theory. *See* Robinson v. Smith, 3 Paige 221, 231, 233 (N.Y. Ch. 1832); Hichens v. Congreve, 38 Eng. Rep. 917, 922 (Ch. 1828).

poration's brokers.[6] They contended that the brokers controlled the corporation through an illegally large representation on the board of directors and used this control to extract excessive fees from the corporation. The directors were accused of converting corporate assets, while both they and the brokers were accused of breaches of fiduciary duty.[7] The shareholders requested that the defendants account for and pay to the corporation their profits and gains and the corporation's losses. A jury trial on the corporation's claims was also demanded.[8] On motion to strike plaintiffs' jury trial request, the district court held that a shareholder's right to a jury trial on his corporation's cause of action was to be judged as if the corporation were itself the plaintiff.[9] While recognizing that the complaint employed equitable language in alleging a breach of fiduciary duty and seeking an accounting, the court found the determinative issue to be that the corporation was entitled to judgment for money which should not have been paid out and that such an action was legal in nature, requiring a jury.[10] Convinced that the jury trial issue was sufficiently material to the outcome of the litigation, the district court permitted an interlocutory appeal.[11] The Court of Appeals for the Second Circuit reversed, holding that a derivative action is entirely equitable in nature and that no jury must try any part of it as a matter of right.[12] The court of appeals based its decision on historical grounds, declaring that the characterization of the derivative suit has not been altered by either judicial or procedural developments.[13] Due to a conflict between courts of appeals' determinations[14] on this issue,

6. The suit was brought under the Investment Company Act of 1940, 15 U.S.C. § 80a (1964) which provides in pertinent part:

> . . . it is declared that the national public interest and the interest of the investors are adversely affected—
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> . . . .
>
> 4) when the control of investment companies is unduly concentrated through . . . inequitable methods of control, or is inequitably distributed, or when investment companies are managed by irresponsible persons. *Id.* § 80a-1(b).

7. The directors were also charged with "gross abuse of trust, gross misconduct, willful misfeasance, bad faith, [and] gross negligence." 396 U.S. at 531-32.

8. *Id.* at 532.

9. Ross v. Bernhard, 275 F. Supp. 569, 570 (S.D.N.Y. 1967).

10. *Id.* at 570-71.

11. 28 U.S.C. § 1292(b) (1948) provides for interlocutory appeals where the district court judge believes that a controlling question of law is involved as to which there is substantial ground for disagreement and the resolution of which would materially advance the litigation.

12. Ross v. Bernhard, 403 F.2d 909, 910-11 (2d Cir. 1968).

13. *Id.* at 914.

14. *See* DePinto v. Provident Security Life Ins. Co., 323 F.2d 826 (9th Cir. 1963), *cert.*

the Supreme Court granted certiorari.[15] The Court reversed the decision of the Second Circuit, ruling that the seventh amendment preserves to the parties in a stockholder's suit the same right to a jury trial which historically belonged to the corporation and to those against whom the corporation pressed its legal claims.[16]

The Right to Trial by Jury

Pre-Merger. The mandate of the seventh amendment is founded upon the division of the English and American legal systems into separate law and equity jurisdictions, each with different procedures and remedies. Actions recognized at common law were triable to a jury, while in equity there was no right to a jury trial.[17] Federal courts in the United States retained this distinction, declaring that the right to jury trial existed if the action would have been cognizable at law in 1791,[18] the year the seventh amendment was adopted.[19] Well before the merger of law and equity in 1938, however, it became clear that this once simple distinction between them could not be retained inviolate. With the post-1791 creation of many new rights and remedies, such as the derivative suit, analogies had to be drawn between the new actions and those prior to 1791 in order to determine whether the right to a jury trial existed.[20] Thus, the historical test did not prove infallible in ascertaining the proper existence of a right to jury trial. Even prior to merger the difficulties arising from the apparent exclusiveness of law and equity[21] were recognized. There were double actions whenever

denied, 376 U.S. 950 (1964), which held that a right to jury trial exists under circumstances similar to those in *Ross*, and with which the court of appeals in *Ross* disagreed. *See* notes 58-60 *infra* and accompanying text.

15. 394 U.S. 917 (1969).

16. 396 U.S. at 532-33.

17. 5 J. MOORE, FEDERAL PRACTICE ¶ 38.02[1] (2d ed. 1951) [hereinafter cited as MOORE]. Thus, "legal" denotes a claim, action, question, issue, or remedy cognizable in an action at law, while "equitable" denotes a claim, action, question, issue, or remedy cognizable in an action in equity.

18. *Id.* ¶ 38.02[2].

19. There is no *constitutional* right to a non-jury trial in civil cases. Note, *The Right to a Nonjury Trial*, 74 HARV. L. REV. 1176 (1961). Furthermore, the right to a jury trial may be waived by the parties. FED. R. CIV. P. 38(d). While FED. R. CIV. P. 38(a), *infra* note 30, preserves the right of jury trial as declared by the seventh amendment, any party desiring that right must make proper demand. *Id.* 38(b).

20. 5 MOORE ¶ 38.11[7]; James 655-56. If a new remedy is created which has no common law counterpart, the legislature has considerable latitude in determining whether the action shall carry the right to jury trial. *Id.* at 655.

21. The division between law and equity was not completely clear even in 1791. *See* James 658. *See also* 3 W. BLACKSTONE, COMMENTARIES *434.

both legal and equitable claims were asserted and frequent dismissals of suits brought in the wrong forum.[22] Under rule 23 of the Equity Rules of 1912,[23] provision was made for courts of equity to try matters ordinarily determinable at law if they arose, "according to the principles applicable," rather than sending them to the law side of the court. The applicable principles included the right of jury trial.[24] The Law and Equity Act of 1915[25] provided for the amendment of a claim to conform to the proper practice upon discovery that it had been brought on the wrong side of the court, as opposed to the old procedure of merely dismissing the suit under such circumstances.

Merger and After. A more critical examination of the seventh amendment came with the modern application of the historical test under the merged civil practice provided for by the Federal Rules of Civil Procedure in 1938. The new rules abolished the procedural distinctions between law and equity,[26] but the established legal and equitable remedies remained undisturbed.[27] Thus, under the new rules, no distinction is made between law and equity in the formulation of issues;[28] indeed, all legal and equitable issues pertaining to a single claim must be presented in one action.[29] While merger has not impaired any substantial rights to jury trial,[30] it has raised troublesome problems as to when such rights may be asserted.

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22. James 665.

23. Rule 23 provided: "If in a suit in equity a matter ordinarily determinable at law arises, such matter shall be determined in that suit according to the principles applicable, without sending the case or question to the law side of the Court." Rules of Practice for the Courts of Equity of the United States 226 U.S. 629, 654 (1912).

24. Southern Ry. v. City of Greenwood, 40 F.2d 679 (W.D.S.C. 1928).

25. Act of Mar. 3, 1951, ch. 90, § 274a 38 Stat. 956, *amending* Act of Mar. 3, 1911, ch. 231, § 274, 36 Stat. 1087.

26. "There shall be one form of action to be known as 'civil action'." FED. R. CIV. P. 2.

27. 5 MOORE ¶ 38.02[2]. The seventh amendment is the only obstacle to a *complete* procedural union. Thus, the only difference between law and equity under a merged practice is the matter of the mode of trial. James 663.

28. The former distinction between law and equity does not control nor affect the pleading or issue formulating stage of the case, except to the extent that a claimant has a choice of legal or equitable remedies or the cumulative right to legal and equitable remedies and desires so to plead his case that there will be legal issues presented upon which he can obtain a jury trial. James 21.

29. "A pleading shall state as a counterclaim any claim which at the time of serving the pleading the pleader has against any opposing party, if it arises out of the transaction or occurrence that is the subject matter of the opposing party's claim and does not require for its adjudication of the presence of third parties of whom the court cannot aequire jurisdiction. . . ." FED. R. CIV. P. 13(A).

30. "The right of trial by jury as declared by the Seventh Amendment to the Constitution or as given by a statute of the United States shall be preserved to the parties inviolate." FED. R. CIV. P. 38(a).

The primary difficulty lies in the fact that many civil actions today are more complex than any action brought before merger. Normally, when a modern action has a historical analogue or counterpart, it can be ascertained as an action at law or in equity, and the mode of trial may be determined accordingly. Most of the difficult jury trial problems under the merged practice, therefore, have resulted from the combination of legal and equitable claims in a single action, since the Federal Rules encourage the joinder of claims[31] and require the assertion of a counterclaim when it relates to the facts of the original claim.[32] Thus, the unitary civil action created situations which not only forced courts to deal with legal and equitable issues simultaneously[33] but which also taxed the ability of the courts to determine the scope of the seventh amendment. The result has been that merger has not only restored the right to a jury trial where it once existed but also where it had previously been denied due to the procedural differences between legal and equitable actions. Among the situations in which complexities arise are these: civil actions where the plaintiff injects both legal and equitable claims; civil actions involving an equitable defense to a legal claim; and civil actions wherein the complaint presents equitable issues and a counterclaim presents legal issues.[34] In such cases the guaranty of the seventh amendment must be separately applied to each element of the modern action which would have been a separate suit at law or in equity, and a determination must then be made as to the sequence of trial. Early practice under the Federal Rules dictated that the order of trial court sequence be left to the trial court's discretion, with the historical pattern for guidance.[35] Two Supreme Court decisions, however, have overruled the authority for such a proposition and, by doing so, have expanded the scope of the seventh amendment guaranty.

In *Beacon Theaters, Inc. v. Westover*,[36] the plaintiff sought an injunction preventing the defendant from instituting an antitrust action and a declaratory judgment that certain movie distribution

31. "A party asserting a claim of relief as an original claim, counterclaim, cross-claim, or third-party claim, may join, either as independent or as alternate claims, as many claims, legal, equitable, or maritime, as he has against an opposing party." FED. R. CIV. P. 18(a).

32. *Id.*

33. See notes 29 and 31 *supra* and accompanying text.

34. *See* James 669-85.

35. *Id.* at 669-73.

36. 359 U.S. 500 (1959).

contracts were not in violation of the antitrust laws. The defendant filed an answer and a counterclaim seeking treble damages against the plaintiff and demanded a jury trial on the factual issues relating to the question of the violation of the antitrust laws. Both the trial court and the appellate court looked at the complaint as a whole to determine the jury question and declared that the complaint was predominantly equitable.[37] The case thus fits the historical pattern of cases in which A seeks equitable relief before B institutes an action at law and B interposes a legal counterclaim. Under such circumstances, the rule had been that although the legal claim was triable before a jury, the trial judge had discretion in determining the trial sequence and could hear the equitable claim first, thus estopping relitigation on all facts common to both the equitable and legal claims.[38] The Supreme Court refused to apply this rule, however, and held that because the counterclaim presented a cause of action cognizable at law the parties had a right to jury trial on any factual issues common to the prayer for equitable relief and the legal counterclaim.[39] In stating that the right to jury trial of legal issues could be lost through prior determination of equitable issues only under "the most imperative circumstances,"[40] the Court effectively eliminated any use of discretion which removes a legal issue from jury trial.

In *Dairy Queen, Inc. v. Wood*,[41] the Court, in even more sweeping language, held that "the constitutional right to trial by jury cannot be made to depend upon the choice of words used in the pleading."[42] The plaintiff had attempted to create equitable jurisdiction by asking for injunctive relief and an accounting, although the claim for relief was essentially for damages resulting from a breach of contract. The Court reasoned that even where legal issues could properly be

37. Beacon Theaters v. Westover, 252 F.2d 864 (9th Cir. 1958).

38. James 683. *See* Ameriean Life Ins. Co. v. Stewart, 300 U.S. 203 (1937).

39. 359 U.S. at 508. The Court could have held that the plaintiff was merely trying to circumvent the defendant's right to jury trial, that the claim was not cognizable in equity, and that the trial judge's order to try the common issue to the court was an abuse of discretion. Instead, it assumed that the equitable claim was valid, allowing for much broader grounds upon which to base its decision. The rule in American Life Ins. Co. v. Stewart, 300 U.S. 203 (1937), that an equity court had discretion to enjoin a lawsuit in order to provide a full determination of a case in a single court was acknowledged by the Court, but it held that a trial judge's order of trial sequence which denied jury trial of a legal counterclaim through collateral estoppel could be reversed on the grounds of abuse of discretion. 359 U.S. at 505-06.

40. 359 U.S. at 510-11.

41. 369 U.S. 469 (1962).

42. *Id.* at 477-78.

characterized as *incidental* to equitable issues, the right to jury trial of legal issues could not be lost.[43]

Both *Beacon Theaters* and *Dairy Queen* demonstrate that the expansion of adequate legal remedies provided by the Federal Rules has necessarily affected the scope of equity, since in the federal courts equity has acted only when legal remedies are inadequate.[44] Because *any* legal issue must now be tried to a jury, equity has been deprived not only of those legal issues which could not previously be tried to a jury but also of those equitable issues which are so related to the legal issues that they must simultaneously be tried to the jury. Thus, the historical test for jury trial may well be anachronistic. While it is generally agreed that procedural reform was never meant to extend the right to jury trial,[45] this does not foreclose the possibility that an extension of the seventh amendment is inextricably linked with the merger of law and equity.

Development of the Derivative Suit

The shareholder's derivative suit arose primarily out of corporate managers' abuse of the concept that a corporation is a legal entity distinct from its shareholders.[46] The logical conclusion to be drawn from this "corporate entity" concept was that harm to the corporation conferred no right of action upon a shareholder. While courts of law therefore refused to permit stockholders to call corporate managers to account for harm brought to the corporation, equity assumed jurisdiction to enforce rights running to the corporation.[47] Because the "corporate personality" of the shareholder was in issue rather than his individual personality, the notion developed that the shareholder was exercising a corporate right in a secondary or derivative manner.[48] Viewing the shareholder's right as

43. *Id.* at 473.

44. Professor James questions this premise, pointing to an increasingly large overlap between law and equity which results from a "borrowing from one jurisdiction by the other." James 658.

45. *Id.* at 667.

46. Prunty, *The Shareholders' Derivative Suit: Notes On Its Derivation*, 32 N.Y.U.L. REV. 980, 981 (1957) [hereinafter cited as Prunty]; *see* 2 G. HORNSTEIN, CORPORATION LAW AND PRACTICE § 711 (1959) [hereinafter cited as HORNSTEIN]; N. LATTIN, CORPORATIONS ch. 2, § 1 (1959).

47. Cohen v. Beneficial Indus. Loan Corp., 337 U.S. 541, 547-48 (1949); Prunty 980.

48. Prunty 990-91. The first method of providing the individual stockholder with a method for invoking judicial power to curb managerial abuse was to label the relationship between director and stockholder as one of trust. *See* Robinson v. Smith, 3 Paige 221, 222 (N.Y. Ch.

derivative or representative served to integrate "the concept of the corporation as a separate right-holding entity . . . with the idea that the shareholder had a right to judicial protection of his interests when jeopardized by a defaulting management."[49] As such, derivative suits are generally regarded as having a dual nature: the shareholder's equitable right to sue on behalf of the corporation and the merits of the corporate claim itself.[50] Notwithstanding this apparent duality, the derivative suit has been traditionally viewed as the exclusive creature of equity with concomitant exclusive jurisdiction in that system.[51] Since the derivative suit is generally considered a unitary action, assuming its equitable nature from the right of the shareholder to sue on the equitable claim, there has heretofore been agreement that no right to trial by jury exists in such cases on any issues.[52]

The Court's Rationale

Notwithstanding historical evidence to the contrary, the Court in *Ross* argued that a right to trial by jury may exist in a derivative suit. The Court predicated its result on the alleged dual nature of the suit, reasoning that if the corporate claim were legal, the suit involved legal claims which should be triable to a jury, notwithstanding the equitable nature of the shareholder's right to sue.[53] Relying on the premise that the seventh amendment preserves the litigants' right to jury trial in suits in which legal rights are to be ascertained,[54] the Court found a mandate for jury trial based on the legal nature of the corporate claim for money damages. Since "law" would not hear a suit by a shareholder before merger in 1938, it was recognized that

1832). The trust theory, however, was inadequate to extend the shareholders' right to recovery beyond the management group to application against extracorporate defendants. To meet this need, the derivative concept was developed. Prunty 994.

49. Prunty 992. In order to bring a derivative suit, a shareholder generally must show that the corporation has refused to enforce the right being sued upon. FED. R. CIV. P. 23.1.

50. H. BALLANTINE, CORPORATIONS § 151, at 359 (rev. ed. 1946); 2 HORNSTEIN § 711. *See* Koster v. Lumbermens Mut. Cas. Co., 330 U.S. 518, 522-23 (1947); Ashwander v. TVA, 297 U.S. 288 (1936). *See also* 2 HORNSTEIN § 716.

51. 2 HORNSTEIN § 711.

52. *Id.* § 730; N. LATTIN, *supra* note 46, at ch. 8, § 3; 5 MOORE ¶ 38.38[4].

53. 396 U.S. at 538-39. See note 50 *supra* and accompanying text.

54. The right is recognized in:

> . . . not merely suits, which the common law recognized among its old and settled proceedings, but suits in which legal rights were to be ascertained and determined in contradistinction to those, where equitable rights alone were recognised, and equitable remedies administered. . . . Parsons v. Bedford 28 U.S. (3 Pet.) 433, 447 (1830).

such a suit had to be tried to the equity side of the court. However, the Court in *Ross* found that the effect of merger was to offer a litigant the right to a jury trial for any legal claim he had since actions were no longer brought as actions at law or suits in equity.[55] Merger was thus held to remove "[p]urely procedural impediments" to the presentation of any issue by any party.[56] Further support for this proposition was found in *Beacon Theaters* and *Dairy Queen*, which held that where equitable and legal claims are joined in the same action, there is a right to jury trial on the legal claims which must not be infringed either by trying the legal issues as incidental to the equitable ones or by having a court trial of a common issue existing between the claims.[57]

The Court found judicial precedent for its holding in but a single Ninth Circuit opinion, *DePinto v. Provident Security Life Insurance Co.*,[58] a stockholder's derivative suit strikingly similar to *Ross* on its facts. In that 1963 decision it was held that a right to trial by jury on legal issues cannot be denied a litigant on the grounds that the case reached the court through equity. The reasoning of the *DePinto* court paralleled that of the Court in *Ross* and was premised on the notion that the merged federal practice expanded the protective ambit of the seventh amendment. The appeals court stressed "the necessity of scrutinizing, with utmost care, any seeming curtailment of the right to a jury trial"[59] and concluded that such a curtailment might be present if trial by jury were not granted. Thus, the seventh amendment was found to require a jury trial *whenever* any part of the corporate claim sued upon involves a legal issue. The basis of the *DePinto* decision was that a derivative suit should be treated as a combination rather than a unitary action, and language in the court's opinion indicates an implicit reliance on the *Beacon Theaters* and *Dairy Queen* rationale.[60]

55. 396 U.S. at 539; *see* FED. R. CIV. P. 2. While the Court consistently relied on merger as having made a jury available to try legal issues in a derivative suit, it did recognize the impact of the Equity Rules and the Law and Equity Act of 1915, reasoning that the same conclusion "could" have been reached under those provisions. 396 U.S. at 539 n.12. See notes 29-32 *supra* and accompanying text. Strangely, however, the Court did not choose to rely on such grounds for any part of its decision.

56. 396 U.S. at 539.

57. See notes 36-43 *supra* and accompanying text.

58. 323 F.2d 826 (9th Cir. 1963), *cert. denied*, 376 U.S. 950 (1964). *See generally* Note, *Corporations: Procedure: Right to a Jury Trial on Question of Negligence in a Shareholder's Derivative Action*, 49 CORNELL L.Q. 664 (1964); Note, *The Right to a Jury Trial in a Stockholder's Derivative Action*, 74 YALE L.J. 725 (1964).

59. 323 F.2d at 837.

60. Thus, except under most imperative circumstances, a right to a jury trial on legal

While *DePinto* serves as the only precedent in the federal courts for the Supreme Court's decision, useful analogy was drawn from two derivative suits for treble damages under the antitrust laws. The first was a pre-merger case, *Fleitmann v. Welsbach Street Lighting Co.*,[61] in which Mr. Justice Holmes dismissed a bill brought in equity on the grounds that the bill did not state a good equitable cause of action since actions for treble damages must be brought at law. The *Ross* Court interpreted this result to mean that a derivative suit for damages must be triable to a jury.[62] Further support for this proposition was found in a similar post-merger case, *Franchon & Marco, Inc. v. Paramount Pictures, Inc.*[63] In that case, the plaintiff was allowed to bring a derivative action for treble damages under the antitrust laws, and the court stated that "[t]he two major issues of right of the shareholder to sue and of violation of the antitrust laws causing damage to the corporation can be tried side by side or otherwise as may be convenient; that one may go to the jury while the other does not causes no difficulty."[64] The dilemma raised in *Fleitmann* was held to have been resolved by the Federal Rules in *Franchon & Marco*, and the solution clearly lay in an unarticulated expansion of the right to jury trial.

Careful not to overstate the effect of the Federal Rules, the three dissenting justices[65] rejected the Court's conclusion that merger destroyed "purely procedural impediments" to a jury trial in a derivative suit, pointing out that such impediments were eliminated, not in 1938, but in 1912 by Equity Rule 23 which provided that legal issues arising in equitable cases could be determined according to legal principles.[66] On the basis of a 1917 Supreme Court decision, the dissent found that rule 23 did not extend the right to jury trial to a

issues may not now be denied to a federal litigant on the ground that the case reached court only through equity, or because equitable rights are involved, or because legal issues are "incidental" to the equitable issues, or because substantive equitable remedies are sought, or by the device of trying the equitable issues first. *Id.* at 835-36.

61. 240 U.S. 27 (1916). *See also* United Copper Sec. Co. v. Amalgamated Copper Co., 244 U.S. 261 (1917). *See generally* Comment, *Federal Antitrust Law—Stockholders' Remedies for Corporation Injury Resulting from Antitrust Violations: Derivative Antitrust Suit and Fiduciary Duty Action*, 59 MICH. L. REV. 904 (1961).

62. 396 U.S. at 536.

63. 202 F.2d 731 (2d Cir. 1953).

64. *Id.* at 735.

65. The three dissenting judges were Burger, Stewart, and Harlan. Harlan and Stewart dissented in *Beacon Theaters*, and both concurred in the *Dairy Queen* decision.

66. See notes 22-23 *supra* and accompanying text.

derivative action.[67] Excepting to the "dual nature" of a derivative suit as being purely artificial, the minority insisted that the historically equitable character of the derivative suit has in no way been altered by the development of the federal practice and that the seventh amendment cannot be read to enlarge the right to jury trial.[68] Thus, the minority contended, the basis upon which *Fleitmann* was dismissed was *not* that a derivative suit for damages must be triable to a jury but that a derivative suit is wholly equitable in nature, and that therefore there is no right to a jury trial. The concern over possible abuse of the derivative suit was demonstrated to be paramount; Mr. Justice Holmes earlier recognized that derivative rather than corporate actions could be brought in order to deprive the defendant of his right to jury trial and thus held that derivative actions could not be brought for treble damages under the antitrust laws.[69] The minority ignored the resolution of this problem inherent in *Franchon & Marco*, devoting its attention to an alleged misapplication of *Beacon Theaters* and *Dairy Queen*. Alluding to the fact that both of the latter suits involved a combination of historically separable suits, one in law and one in equity, the minority refused to "force the facts of [*Ross*] into the mold of *Beacon Theaters* and *Dairy Queen*."[70] The derivative suit, as a single, unitary, equitable cause of action was found not to fit the historical pre-merger pattern of cases factually similar to *Beacon Theaters* and *Dairy Queen* where the equity court would have disposed of the equitable claim and would then have either retained jurisdiction over the suit, despite the availability of legal remedies, or enjoined a subsequent legal action between the same parties involving the same controversy. The minority thereby concluded that the historic division between law and equity survived the earlier Supreme Court cases untrammelled. The majority's alleged reliance on a distinction between inherently legal issues and inherently equitable issues was faulted on the grounds that all issues are factual in nature, "taking their color from surrounding circumstances."[71] The circumstances of a shareholder's derivative suit were held to prescribe that *all* issues

67. 396 U.S. at 547. The decision relied on by the dissent was United Copper Sec. Co. v. Amalgamated Copper Co., 244 U.S. 261 (1917), where the Court determined that an shareholders' derivative suit must be brought in an equitable forum.

68. 396 U.S. at 543-45.

69. *Id.* at 547-48.

70. *Id.* at 549.

71. *Id.* at 550. *See* James 692; 5 MOORE ¶ 38.04[1] n.40.

presented therein are equitable and to proscribe a constitutional right to have those issues tried to a jury.[72]

Shortcomings of the Ross *Rationale*

The Court recognized the logical inconsistency which inheres if a legal corporate claim may be tried to a jury when the corporation itself sues but not if a shareholder sues.[73] It further implied that there is no justification for presenting different modes of trial depending on whether the corporation is willing to sue.[74] In its zeal to overcome this inconsistency, however, the Court failed to devote sufficient scrutiny to several factors which should be central to its analysis. It did not even raise the issue of the constitutional right of the defendant to a jury trial on legal issues presented in a derivative suit, a matter warranting at least superficial examination, notwithstanding the fact that the *plaintiff* shareholder's right to trial by jury is the issue raised in *Ross*. It was, after all, the possible infringement of a defendant's right to a jury trial in a derivative suit brought under the antitrust laws which caused Mr. Justice Holmes to dismiss the derivative suit in *Fleitmann*, a case upon which the Court heavily relied.[75]

A possible explanation for such an omission lies in the fact that the Court's reliance on *Fleitmann* was erroneous, as the minority pointed out.[76] A careful reading of the *Fleitmann* opinion clearly discloses judicial concern, not that legal issues in a derivative suit be tried to a jury, but that a derivative suit not be brought under the antitrust laws. In order that the defendant's right to a jury trial on the matter of damages be at all times preserved, the *Fleitmann* Court held that only the corporation itself could bring a treble damage action under the antitrust laws.[77] Had the *Ross* Court raised the matter of preserving the defendant's right to a jury trial, it would have impaired

72. The minority concluded by stating: "The Court's decision today can perhaps be explained as a reflection of an unarticulated but apparently overpowering bias in favor of jury trials in civil actions. It certainly cannot be explained in terms of either the Federal Rules or the Constitution." 396 U.S. at 551. While the remark may be unfair, it demonstrates the extent to which policy considerations might have swayed both the majority and the minority.

73. *See id.* at 538-39.

74. "[i]t is no longer tenable . . . to deny legal remedies to a corporation, merely because the corporation's spokesmen are its shareholders rather than its directors." *Id.* at 540.

75. See notes 61-62 *supra* and accompanying text. Under FED. R. CIV. P. 38(b), *any* party may demand a jury trial on any legal issue. The defendant did not do so in *Ross*, but this does not diminish the importance of the issue as it relates to *Fleitmann*.

76. See note 69 *supra* and accompanying text.

77. 240 U.S. at 29.

its construction of the *Fleitmann* opinion; the minority clearly demonstrated the inadequacy of this aspect of the Court's rationale.

Sufficient attention was not devoted by the Court to the historical developments presaging merger, notably the promulgation of the Equity Rules in 1912 and the Law and Equity Act of 1915.[78] These measures were precipitated by a recognition that law and equity were constantly overlapping and that each had acquired certain characteristics of the other.[79] Thus, certain "procedural impediments" to the presentation of legal issues were certainly minimized, if not eliminated, prior to merger. The dissenting judges articulated this fact,[80] but the Court chose to disregard it, indicating instead that the appearance of the Federal Rules in 1938 was the event which altered the traditional distinction between law and equity.[81] While merger certainly was the culmination of efforts to facilitate practice in the federal system, a discussion of the events leading to merger would have added crucial emphasis to the Court's argument that any legal issue is now triable before a jury. Such a discussion is necessary both to demonstrate a logical development in the law and to reinforce the fact that the erosion of procedural distinctions between law and equity was a gradual process. The combination of the failure to recognize developments in the law prior to merger and the almost exclusive reliance upon the *Beacon Theaters-Dairy Queen* analogy creates the impression that the Court, predisposed toward jury trials, was searching for a suitable justification for a preconceived result.

The dissenters were quick to find fault with this analysis. Certainly they were correct in their recognition that the derivative suit is wholly a creature of equity and that, as a historical matter, it cannot artificially be broken down into separable elements. Thus the minority reasoned that *Beacon Theaters* and *Dairy Queen* would not apply to the facts of *Ross* for the simple reason that a derivative suit is not one in which separate legal and equitable claims are being asserted. This distinction, however, ignores the same developments that the majority omitted and demonstrates an unreasonable delineation between law and equity. While the Court did not examine

78. See notes 21-22 *supra* and accompanying text.

79. James 658-60. While there was a continuous process of borrowing by one jurisdiction from the other, there was little equivalent sloughing off of functions. This led to the large overlap between law and equity. *Id.* at 659.

80. See notes 65-66 *supra* and accompanying text.

81. See note 55 *supra*.

historical evidence sufficiently to justify its result, the minority refused to recognize that developments in the law, designed to facilitate federal procedure, have placed the distinction between law and equity in a different perspective.

Conclusion

While the Court's rationale in *Ross* may not lend substantial support to its position, the holding is legally justifiable. The effect of the Equity Rules, the Law and Equity Act, and the Federal Rules has not been to extinguish legitimate historical distinctions between law and equity but, rather, to ensure the right to a jury trial on legal matters, a right which has existed since 1791 but which has not always been honored due to the early history of legal and equitable procedures. Thus, any legal issues arising in a shareholder's derivative suit are triable to a jury.

The Court's holding raises the question of whether the static historical test for jury trial is at all viable under the merged practice. Other tests have been proposed and found inadequate, primarily because they fall short of the safeguard of the seventh amendment.[82] A primary difficulty in formulating a new test lies in the confusion involved in defining "legal" and "equitable" matters. It is the circumstances surrounding a factual matter which convey a legal or equitable taint;[83] a factual issue may be legal in one set of circumstances and equitable in another, depending on the relief sought and the questions of law involved.[84] Thus, if any "test" must still control the area, it would lie in a definition of the relief sought *and* the issues involved, combined with a recognition that merger has enforced rights which always existed but were formerly denied. In other words, one must apply the 1791 historical test to a lawsuit as if the Federal Rules existed in 1791.[85] Applying this "test" to a shareholder's

82. While both a "basic nature of the issue" test, 5 MOORE ¶ 38.16, and a "judicial discretion" test, James 692, have been proposed as alternatives to the "historical" test, neither contains vitality since *Beacon Theaters* and *Dairy Queen*, which preserve the right to jury trial for legal issues in *all* possible situations. Thus, legal issues "incidental" to a suit basically equitable in nature are protected by the seventh amendment, and a federal judge may not remove a legal issue from a jury trial as a matter of discretion.

83. James 692; 5 MOORE ¶ 38.04[1] n.40. See note 7 *supra*.

84. But the issue of breach of contract should be triable to a jury in a suit for specific performance, just as the issue of money damages must be tried to a jury in a shareholders' derivative suit.

85. One may raise the criticism that this test is still historical in nature and that *no* historical test is applicable to the united procedure. The only alternative to some form of historical test,

derivative suit which, at least in part, alleges a breach of contract and seeks money damages, it is clear that both a legal issue, breach of contract, and a legal remedy, money damages, are involved. With courts under the Federal Rules having both legal and equitable powers, legal issues arising in a shareholder's derivative suit, which formerly had to be tried to the judge in equity because of purely procedural impediments, are now triable to a jury.

Judicial rulings justify such an approach; its background lies in pre-merger developments. Interpretations of Equity Rule 23 prior to 1938 urged the conclusion that the seventh amendment can be so interpreted as to extend the constitutional right of jury trial beyond the strict historical pattern. In a 1928 district court decision, *Southern Railway Co. v. City of Greenwood*,[86] the constitutional right to a jury trial on a legal issue was recognized in a suit brought in equity. The relief sought was an injunction, but the legal issue of title was involved, and the court stated that the seventh amendment guarantee was not to be abridged merely because the suit arose in equity.[87] While merger should not be used as a mechanism for extending jury trial in a way that the framers of merger did not contemplate, cases since 1938 strengthen the conclusion that the test for jury trial must recognize that the law is not static. As interpreted by *Beacon Theaters* and *Dairy Queen*, merger did not make a jury trial available to hear legal issues in a suit brought in equity but merely facilitated the process of preserving the constitutional right to a jury trial on such matters, a right recognized as early as 1928 and induced by the adoption of the

however, is resort to policy. This is favorable to jury trial and has been suggested as a solution. C. WRIGHT, LAW OF FEDERAL COURTS § 92, at 407 (2d ed. 1970). The problem with such a suggestion is that it does not insure the constitutional guaranty, despite the favorable policy enunciated.

86. 40 F.2d 679 (W.D.S.C. 1928).

87. It is by no means declared, however, in any decision of the Supreme Court of the United States, . . . that even in an equity case in which the fundamental issue is dependent upon a question of fact triable to a jury, and in which that right has been guaranteed by the Constitution of the state and the United States, that equity would be permitted to determine such [a] question without the jury's decision at law upon such question first being had. *Id.* at 682.

We think [Equity Rule 23] means that, where in an equity case a matter triable by jury arises, the court shall not refuse to try it, and shall not go through the form of sending it to the law side of the court, but shall determine it according to all the principles applicable—one of which is the right of trial by jury. *Id.* at 686, *citing* Colleton Merchandile & Mfg. Co. v. Savannah River Lumber Co., 280 F. 358, 363 (4th Cir. 1922).

Equity Rules in 1912 and the Law and Equity Act of 1915. This pattern has subsequently been reinforced:

> It is therefore immaterial that the case at bar contains a stronger basis for equitable relief than was present in Beacon Theaters. It would make no difference if the equitable cause clearly outweighed the legal cause so that the basic issue of the case taken as a whole is equitable. As long as any legal cause is involved the jury rights it creates control.[88]

Thus, legal issues which arise when the equitable devices of the class action, interpleader, and intervenor are utilized are triable to a jury.[89] In its mandate for jury trial of legal issues, the seventh amendment must be considered in light of present practice. The notion that merger artificially extends the right to jury trial in derivative suits is untenable. Similarly, any contention that the right to jury trial was frozen in 1791 seems unrealistic, and the historical test appears outmoded.

One must be diligent not to introduce policy arguments into the issue of the *constitutional* right to trial by jury. *Ross* stands for the proposition that the Constitution guarantees the right to a jury trial of the legal issues involved in a derivative suit. Suggestions that the *privilege* of jury trial may be legislatively or judicially extended[90] do not bear on the matter of constitutionality. Any indication on the part of the Court that its decision is justified because it remedies the inconsistency between shareholder and corporate suits is unwarranted;[91] it cannot be argued that a constitutional right to trial by jury does not exist because a jury trial is expensive and time consuming or because jurors are incapable of understanding the complex issues involved in derivative suits.

While policy considerations may militate against extending the right to a jury trial,[92] the seventh amendment demands a jury trial of

88. Thermo-Stitch, Inc. v. Chemi-Cord Processing Corp., 294 F.2d 486, 491 (5th Cir. 1961). *See also* Halladay v. Verschoor, 381 F.2d 100 (8th Cir. 1967); Richland v. Crandall, 259 F. Supp. 274 (S.D.N.Y. 1966).

89. *See* 396 U.S. at 541 n.15 and cases therein cited.

90. *See* James 656-57.

91. While the Court's result should not be justified on policy grounds, this does not mean that the Court's result is unjustified on policy grounds. If we accept the corporation as the true plaintiff, unable to sue on its own only because the wrongdoing directors control it, then those directors, as defendants in the action, should not be allowed to defeat the corporation's right to a jury trial on a legal claim. Such a justification is completely in accord with *Beacon Theaters* and *Dairy Queen* which establish that a defendant can employ no device to defeat the plaintiff's right to a jury trial.

92. *See* 5 MOORE ¶ 38.02[1]; James, *Trial by Jury and the New Federal Rules of Civil Procedure*, 45 YALE L.J. 1022, 1026 (1936).

legal issues, and it is no defense that a jury could not hear the claims when the derivative suit was in its nascent stages. In view of the adoption of the Equity Rules in 1912, the Law and Equity Act of 1915, and of the promulgation of the Federal Rules of Civil Procedure in 1938, legal issues, whether sounding in equity or law, must be tried to a jury. The seventh amendment question depends on the nature of the issue to be tried rather than the character of the overall action.[93] As long as a derivative suit can be brought under the Federal Rules, there is a constitutional right to trial by jury of any legal claims involved—those claims which the corporation, had it sued, would have presented as legal claims. The constututional right to a jury trial may not be frustrated on antiquated historical grounds; while *Ross* indicates an increased demand on the jury system, undesired by some, it is certainly a proper application of the seventh amendment to our federal practice.

93. Simler v. Conner, 372 U.S. 221, 223 (1963).