

# Supreme Court of the United States

October

TERM 1969

In the Matter of:

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HOWARD ROSS AND BERNARD ROSS,  
AS TRUSTEES FOR LENA ROSENBAUM,

Petitioners

vs.

ROBERT A. BERNHARD, ET AL.,

Respondents.  
-----X

Docket No. 42

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Place Washington, D. C.

Date November 10, 1969

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October  
[REDACTED] TERM 1969

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AS TRUSTEES FOR LENA ROSENBAUM,	)	
	)	
Petitioners	)	
	)	
vs	)	NO. 42
	)	
ROBERT A. BERNHARD, ET AL.,	)	
	)	
Respondents	)	
	)	

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Washington, D. C.  
Monday, November 10, 1969

The above-entitled matter came on for argument at  
10:10 o'clock a.m.

BEFORE:

- WARREN E. BURGER, Chief Justice
- HUGO L. BLACK, Associate Justice
- WILLIAM O. DOUGLAS, Associate Justice
- JOHN M. HARLAN, Associate Justice
- WILLIAM J. BRENNAN, JR., Associate Justice
- POTTER STEWART, Associate Justice
- BYRON R. WHITE, Associate Justice
- THURGOOD MARSHALL, Associate Justice

APPEARANCES:

- WILLIAM E. HAUDEK, Esq.  
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P R O C E E D I N G S

1  
2 MR. CHIEF JUSTICE BURGER: Mr. Haudek.

3 MR. HAUDEK: May it please the Court, this case is  
4 here on certiorari to the Second Circuit, involves a stock-  
5 holders derivative action. The issue is whether the Petitioners  
6 are entitled to trial by jury.

7 Petitioners, who are the plaintiffs below, made a  
8 timely demand for a jury. The Defense motion to strike the  
9 jury demand was denied by the District Court. The Second Circuit,  
10 by a two-to-one vote, reversed on the grounds that there can be  
11 no right of jury trial in a stockholder suit. And that holding  
12 presents the principal issue here.

13 The holding below is in direct conflict with a  
14 decision of the 9th Circuit. It is also, we believe, in  
15 conflict with an earlier decision of the Second Circuit, which  
16 has been widely followed.

17 The facts of the case can be stated briefly:  
18 Petitioners are stockholders of the defendant Lehman Corporation,  
19 a registered investment company. They bring this action on  
20 behalf of the corporation against its director and against the  
21 broker, the defendant Lehman Brothers.

22 The Complaint charges that the directors of the cor-  
23 poration, under the control of the broker, caused the corpora-  
24 tion to pay unnecessary and excessive commissions to the broker.  
25 These improper payments, it alleged, violated various provisions

1 of the Investment Company Act, and constituted conversion and  
2 waste of corporate assets, willful or negligent breach of  
3 fiduciary duties.

4 Q Is this a Federal question of jurisdiction?

5 A It is jurisdiction under the Investment Company  
6 Act, Your Honor; Section 44.

7 Q Not a diversity case?

8 A Not a diversity case. I think the statement to  
9 the contrary in the Opinion below is an error.

10 The Complaint demands judgment in favor of the  
11 corporation for an accounting and for the damages of the cor-  
12 poration, as well as the profits of the Defendants.

13 The action thus falls into the traditional pattern  
14 of the stockholders' derivative suit; the cause of action  
15 belongs to the corporation but the corporation cannot bring  
16 suit of it, because it is under the control of the wrongdoers.  
17 A stockholder is, therefore, committed to bring the action on  
18 behalf of the company.

19 The right of jury trial rests on the Seventh Amend-  
20 ment to the Constitution, which declares that in suits of  
21 common law the right of jury trial shall be preserved.

22 Before discussing the strictly legal questions con-  
23 cerning the scope of the Amendment, I want to say a word about  
24 the fundamental importance of the issue.

25 From the earliest times to the present, this Court

1 has been emphatic that the right to a jury trial occupies a  
2 crucial place in our legal system; so crucial, the Court has  
3 said that any curtailment or seeming curtailment should be  
4 scrutinized with the utmost care.

5 Q We haven't thought of an injunction suit, for  
6 example, or a mandamus as calling for a jury trial, have we?

7 A No, Your Honor, a jury trial applies to legal  
8 issues and we propose to show that these are legal issues. Of  
9 course, the statement that your Court made was addressed to  
10 legal issues.

11 Q Do you suggest that there are never legal  
12 issues in a suit for injunction or a suit for mandamus?

13 A Oh, no; there can be legal issues if a suit  
14 for damages turns up at the same time as the suit for an in-  
15 junction, for instance. And in that case there is your Court's  
16 decision in Dairy Queen against Wood, which holds the legal  
17 issues are decided first by a jury before the equitable issues  
18 go to the Court.

19 Q I see. Thank you.

20 A Now, it is the great virtue of the jury system  
21 to temper the technicalities of the law and the preconceptions  
22 of judges by the common sense which controls laymen, can bring  
23 to the practical problems of life. And this virtue, I believe,  
24 has particularly appropriate place in the stockholder's  
25 action.

1 Q Isn't that also a function of equity to get  
2 away from the rigidities of rules of law?

3 A It is, Your Honor, but I think when we speak  
4 of a jury we speak more of the factual issues rather than the  
5 legal ones. I think an appraisal of the practical problems as  
6 presented by the facts will be for the jury and that it is  
7 there that their practical sense of justice can find applica-  
8 tion.

9 Q What is the real lawsuit in this case?

10 A The real lawsuit -- you mean more details of the  
11 facts?

12 Q Yes.

13 A One of the charges is --

14 Q Well, what's the suit for?

15 A The suit is for damages of the corporation and  
16 for the profits of the defendant derived from the improper  
17 commission payments.

18 Q I understand that's the way you get into  
19 court, but what is the case about? Recovery of what? Damages  
20 -- money damages?

21 A Money damages. There is a prayer for an  
22 accounting which I believe, as I will argue, should be ignored.  
23 But the essence is money damages.

24 Now, small investors consider the stockholders action  
25 as their Magna Carta. It is their main protection, and the only

1 protection against overreaching of management. On the other  
2 hand, from other quarters, the stockholder's action is frequently  
3 attacked for its supposed abuses. Precisely, because the  
4 stockholder's action is controversial, it tends to invoke pre-  
5 conceptions of some judges and precisely because of that  
6 tendency, I urge the Court to consider whether in this critical  
7 area of the law the practical judgment of the jury, its defense  
8 of justice, should be allowed to play the role which the Con-  
9 stitution deems of such paramount importance.

10 Now, the Court below in rejecting the jury right in  
11 stockholder's suits, simply argued that the stockholder's action  
12 is not a suit at common law within the meaning of the Seventh  
13 Amendment. Historically, the Court says that a stockholder's  
14 suit was a creature of equity; it had to be brought in a Court  
15 of Equity so that neither side had a right to jury trial and  
16 still according to the Court below, this historical state of the  
17 law continues to date.

18 With deference I say that the Court below misconceived  
19 the nature of the derivative suit and the impact of the Federal  
20 Rules of Jury Procedures. The stockholder's derivative action  
21 consists of two elements: One is the cause of action of the  
22 corporation; the other is the right standing of the stock-  
23 holder to assert that cause of action.

24 Unquestionably, the second element, the stockholder's  
25 right to act for the corporation, was developed by the Courts

1 of Equity and is a creature of equity. The stockholder's  
2 standing as champion of the corporation's right presents,  
3 therefore, an equitable issue which must be tried by the Court  
4 without a jury.

5 But the other element of the stockholder's action,  
6 the underlying claim of the corporation is a wholly different  
7 thing. This corporate claim is not the creature of equity at  
8 all; it may be a legal cause of action which, in an action by  
9 the corporation, would entitle both parties to a jury trial.  
10 Such a legal claim of the corporation, I submit, does not  
11 change its nature because it is asserted on behalf of the cor-  
12 poration, rather than by the corporation.

13 For instance, a corporate claim for conversion such  
14 as is here alleged is typically and traditionally a claim  
15 at law. In a stockholder's suit it remains what it is; it is  
16 still a claim for conversion; it is still based upon the legal  
17 tort of conversion; it remains legal in origin and nature; and  
18 such a legal claim, we submit is tryable by jury, no matter by  
19 what mechanism the machinery of litigation is set in motion.

20 In summary, it is our contention that in a stock-  
21 holder's derivative action the equitable issues relating to a  
22 stockholder's standing are tried by a Court but the legal  
23 issues relating to the corporation's claim are to be tried by a  
24 jury.

25 Q Are you speaking now of the right to recover or



1 the amount of recovery when you speak of a jury?

2 A Both, Your Honor. But the -- if the claim is  
3 legal, of course the underlying claim might be an equitable  
4 claim and then both elements would be equitable and you would  
5 have no right to a jury trial.

6 But if the corporation's underlying claim is legal,  
7 then both the existence of the claim and the amount of the  
8 claim, we say, must be determined by jury, if a proper demand  
9 is made.

10 Now, this division of the trial functions between  
11 Court and jury is a direct consequence of the merger of law and  
12 equity of the Federal Rules as interpreted by two recent de-  
13 cisions of this Court.

14 I am referring to Your Honors' decision in Dairy  
15 Queen against Wood and its predecessor Beacon Theaters against  
16 Westover. In short, this Court held that if an action involved  
17 both legal and equitable issues, then the legal issues must be  
18 decided by a jury while the equitable issues are passed on by  
19 the Court.

20 Take for instance, the claim for trademark infringe-  
21 ment which was involved in the Dairy Queen case where the  
22 plaintiff asked both for an injunction and for damages. For-  
23 merly, prior to the merger of law and equity, such a suit had  
24 to be brought on the equity side of the District Court and  
25 equity would dispose wof the entire controversy without a jury.

1 Q Including a claim for damages?

2 A The claim for damages was disposed of by virtue  
3 of the Cleanup Doctrine(?)

4 Q But before the union of law and equity this --  
5 particular suit was brought in 1920 -- it had been disposed of  
6 as a suit in equity?

7 A That's right, Your Honor. And that was the  
8 innovation that was brought about by Dairy Queen.

9 Q What was the innovation? You mean that --

10 A It is not brought in equity; it is not brought  
11 at law; it is, of course, the singular form of action declared  
12 by the Federal Rules and the Court sitting neither as a Court of  
13 Equity, nor as a Court of Law, but simply as a Court.

14 Q But, I take it that before -- in the 1920's it  
15 would have been held that this claim for damages was not a --  
16 was an equitable issue and for which there would be no jury  
17 trial. Is that right?

18 A Well, I don't know whether the phrase in terms  
19 of equitable issues --

20 Q Well, how would you phrase it?

21 A No, well, I think if it were --

22 Q If it were a legal claim whether it was 1920 or  
23 any other time it wouldn't make any difference; there would have  
24 been a jury trial.

25 A In 1920, Your Honor, they would have tried the

1 whole thing in equity, not because the claim for damages was  
2 not a legal claim, but because one's equity took jurisdiction;  
3 it cleaned up the whole controversy.

4 Q But you mean that just suspended the Seventh  
5 Amendment?

6 A I think it was the traditional view at that  
7 time that the Seventh Amendment along this equity jurisdiction  
8 and law jurisdiction -- that equity could clean up legal claims.

9 Q Were there -- are there some cases where the  
10 right to jury trial is asserted in those years and the claim was  
11 denied?

12 A We mentioned one specifically, Your Honor,  
13 which involved a stockholder's derivative action, where the  
14 underlying claim of the corporation was legal and the right to  
15 jury trial was asserted. And I think it will be one of my  
16 primary contentions, but insofar as a suit for injunction and  
17 damages based on trademark violations is concerned, while I am  
18 sure that there must have been such cases, I am not presently  
19 ready to cite one.

20 Q At the present time, Mr. Haudek, if the bene-  
21 ficiary of the trust asserts a claim against the trustees for  
22 bad faith in the investment or management or payment of  
23 excessive commissions, what kind of a suit would that be?

24 A I think, Your Honor, we are dealing with a  
25 so-called "genuine trust," where a separation of legal title

1 and beneficial interest, I believe that can be brought in  
2 equity traditionally, because that comes under the traditional  
3 head of equity jurisdiction.

4 Q There would be no jury trial?

5 A There would be no jury trial in that case, but  
6 distinguish the kind of case that you have posed from one  
7 against fiduciaries who are not technically trustees.

8 Q Well, are you saying that the stockholders are  
9 not the beneficial owners of the assets of the corporation,  
10 subject only to creditors?

11 A I think they have a beneficial interest, Your  
12 Honor, but I don't think they are considered as trustees of an  
13 express trust, in the sense in which I at least understood your  
14 first question. I was thinking of the technical trust created  
15 by the trustee or by last will where legal cattel is conferred  
16 to person and the equitable interest to another.

17 Now, so far as the corporation and its officers are  
18 concerned, the stockholders are concerned, I want to emphasize  
19 that the directors certainly do not have legal title. The  
20 title may be vested in the corporation and the stocholders have  
21 a beneficial interest in it, but the directors' position is  
22 different from that of the technical trustees in that the  
23 technical trustee has legal title; the director does not.  
24 And I think that has always been the reason why Courts have  
25 refused to apply technical trust rules to directors. For

1 instance, the statute of limitations concerning express trusts  
2 has always been quite different from the statute of limitations  
3 applicable to directors.

4 Q I gather the corporation claim derives only  
5 from Section 44, doesn't it?

6 A The jurisdiction.

7 Q What about the claim? Would there be a claim  
8 in common law for this money recovery?

9 A No, Your Honor; there is quite a number of  
10 provisions of the Investment Company Act which I enumerated in  
11 our Complaint. For instance, Section 37 of the Act forbids  
12 willful conversion of assets of an investment company. We  
13 claim that there was willful conversion.

14 Q Well, what I am really trying to get at is  
15 whether the corporation's claim for money damages -- would it  
16 exist independently of the Investment Act?

17 A It could also be an asserted point at common law.

18 Q Well, would it have to be assertable at common  
19 law in order to bring the Seventh Amendment into play?

20 A No, Your Honor.

21 Q It would not?

22 A No.

23 Q Any statutory violation would bring the Seventh  
24 Amendment into play?

25 A Any statutory violation, just as much as any

1 common-law violation if it creates a claim for damages. I  
2 think generally the rule has been, as I understand it that even  
3 a particular type of claim did not exist in 1791 so that you  
4 cannot say whether in 1791 it was equitable or legal, you deal  
5 with that by saying: "How would the Courts have dealt with  
6 that claim in 1791 if that type of situation had been known at  
7 the time."

8 Q Have any cases in this Court given this  
9 analysis?

10 A I am quite confident -- well, certainly in  
11 declaratory judgment cases this has been held to be so in  
12 Beacon Theaters against Westover. And declaratory judgments  
13 were unknown in 1791.

14 And, incidentally, also in Beacon Theaters, Your  
15 Honor, was involved a statutory claim for treble damages under  
16 the anti-trust laws and the Court held that the right to jury  
17 trial was constitutional.

18 And so I believe that answers it.

19 And so now, under the Doctrine of the Dairy Queen  
20 case the Trial Court must scrutinize each issue, whether it is  
21 essentially legal or equitable and since in Dairy Queen the  
22 damage issue was of a legal nature it had to go to the jury as  
23 this Court ruled, which the equitable issues relating to the  
24 injunction were reserved for the Courts.

25 Now, I submit that exactly the same principles apply

1 to stockholders' derivative suits. Again, in former days, prior  
2 to the merger of law and equity, such an action was brought on  
3 the equity side of the District Court and equity disposed of  
4 the entire controversy. But again, under Dairy Queen, the  
5 Trial Court must now scrutinize each issue separately for its  
6 legal or equitable character.

7 If the corporation's cause of action is essentially  
8 legal it must be determined by the jury, even though other  
9 issues, such as the standing of the stockholders are equitable  
10 and kept for decision by the Court.

11 Now, it was held that the Court below refused to  
12 apply the principle of Dairy Queen to stockholders' suits. The  
13 Court below did assume, although it did not expressly hold --  
14 it assumed that the underlying corporate claim is legal, rather  
15 than equitable in nature, and that it is this legal claim which  
16 the Petitioners are seeking to enforce here.

17 The Court below held, however, that the stockholder's  
18 action brings about a change in the nature of the cause of  
19 action and converts it from a legal to an equitable claim. I  
20 must say I fail to see by what argument the stockholder's suit  
21 can bring about such a transformation of the claim. After all,  
22 as I have said, a corporate claim for conversion is a legal  
23 claim and if it is asserted by a stockholder for the corpora-  
24 tion, it is still based on the same legal tort of conversion.

25 However, I need not pursue the logic of this

1 transformation theory of the Court below, since this Court has  
2 clearly rejected it. The case is Fleitman against Welsbach  
3 Street Lighting Company, decided in 1916. Mr. Justice Holmes  
4 wrote the opinion for a unanimous Court and since the case  
5 strikes me as probably decisive here, I would like to dwell on  
6 it briefly.

7 Fleitman was a stockholder's derivative action for  
8 total damages under the anti-trust laws. This Court noted  
9 that the cause of action belongs to the corporation and that  
10 if the suit were brought by the corporation the claim would be  
11 at law and triable by jury.

12 Q Would it not be -- would that same thing not be  
13 true if a broker had charged excessive commissions to a  
14 trustee.

15 A Yes, Your Honor.

16 Q And the trustee brought the suit against the  
17 broker; that would be at action at law?

18 A Yes.

19 Q And a jury trial?

20 A Yes, sir.

21 Q But you have previously indicated that if the  
22 beneficiaries of the trust brought that suit -- made that claim  
23 against the trustees for having paid those excessive commissions,  
24 that would necessarily be a suit in equity without a jury?

25 A But, Your Honor, these are two entirely



1 different things which I believe cannot be compared.

2 Q I just want you to clear up that lack of  
3 parallelism which at least appears on the surface.

4 A I think you would have the parallelism, Your  
5 Honor, if your express trustee had paid excessive commissions  
6 to the broker and if he refused to bring an action against the  
7 broker. Then I assume the beneficiary could bring the action  
8 so to say, derivatively, on behalf of the trust and that action  
9 would be just as much triable by jury as an action brought by  
10 the trustee himself.

11 Q Does your case depend upon the right of the  
12 beneficiary to sue the broker directly?

13 A Oh, no, Your Honor. The beneficiary sues the  
14 broker on behalf of the corporation. The beneficiary asserts  
15 the --

16 Q This is now -- I am speaking now of the trust.

17 A In the trust it would be exactly the same.  
18 The claim for the excessive commission would be the property of  
19 the trust. Now, technically, title to the trust assets is  
20 vested in the trustee and a beneficiary can assert that claim  
21 on behalf of the trust only in a -- I will say "derivative  
22 action," just like a corporate derivative action. In other  
23 words, the beneficiary can sue in the right of the trustee be-  
24 cause the trustee is derelict in his duty in asserting the claim.

25 Q And have you cited us any case, or do you know

1 of any in which the beneficiary of the kind of trust we're  
2 talking about now has been able to maintain an action in his  
3 own name against the person in the posture of the broker?

4 A The beneficiary of a trust; no, Your Honor, we  
5 have not, but I could refer you to a case in which the stock-  
6 holder's action was, indeed compared to certain actions by a  
7 beneficiary. It is Goldstein against Grosbeck in the Second  
8 Circuit.

9 I think the late Judge Charles E. Clark said that  
10 a stockholder's derivative action is essentially the same as  
11 or similar to an action by the beneficiary of a trust because  
12 the trustee himself refuses to enforce the cause of action.  
13 This case is not cited in our brief.

14 Q You referred to a case a moment ago -- did you  
15 say Blackman?

16 A Fleitman, Your Honor; F-l-e-i-t-m-a-n.

17 In the Fleitman case the issue before the Court, as  
18 the Court stated it, was whether the defendant's right to a  
19 jury trial should be forfeited because the complaining stock-  
20 holder was unable to induce action by the corporation and in-  
21 stead brought the action on behalf of the corporation.

22 Now, this Court held in Fleitman that the answer to  
23 the question was "no." Now, in other words, the derivative  
24 suit did not change the nature of the cause of action that was  
25 alleged in the Fleitman case. The cause of action remains a

1 legal claim under the anti-trust laws and the parties were  
2 entitled to jury trial.

3 Now, I say that this part of the Fleitman case --  
4 I will presently refer to another -- that this part of the  
5 Fleitman case is directly applicable here. Here, as in  
6 Fleitman, the underlying cause of action is at law. Here, as  
7 there, the stockholder's suit does not change its nature; here,  
8 as there, the parties are entitled to jury trial.

9 Q Although I think a while ago you conceded that  
10 at the time of Fleitman another kind of stockholder's deriva-  
11 tive suit that had been brought did not involve a treble damage  
12 claim; that there would be some kinds of stockholder's deriva-  
13 tive suits in which damages could be recovered without a jury  
14 trial? At the time of Fleitman.

15 A I submit, if at the time of --

16 Q Isn't that right?

17 A That is absolutely right and you will hear that  
18 in Fleitman the plaintiff, likewise, did not succeed in getting  
19 it.

20 Q Of course, do the anti-trust laws provide for  
21 a jury trial?

22 A No, Honor, the Sherman Act and the Clayton Act  
23 are completely silent and I want to repeat, since the Court  
24 below seemed to think that the jury rights under the anti-trust  
25 laws is statutory --

1 Q I thought so, too.

2 A Fleitman did hint at it but we cannot tell for  
3 sure what the Court thought. But, certainly in the Westover  
4 case and the Beacon Theaters case, why, this Court held that  
5 the right of action for treble damages is under the constitu-  
6 tion -- the right to a jury is under the constitution.

7 Now, I must add that Fleitman in another part which  
8 I think is no longer applicable, the action was decided in the  
9 days when law and equity were separate. The action had been  
10 brought on the equity side of the Court and the Equity Courts  
11 in those days, could not administer a jury trial.

12 This case was an impasse that on the one hand, the  
13 parties were entitled to a jury trial and on the other hand,  
14 the Court could not grant it so the Courts saw no other way out  
15 but to dismiss the action in its entirety.

16 This extreme consequence, would, of course, no longer  
17 be applicable today; with the merger of law and equity, the same  
18 Court and the same trial can now submit the legal issues to a  
19 jury while the equitable issues remain with the Courts. A  
20 stockholder's action can no longer be dismissed because it  
21 asserts the legal cause of action that's triable to a jury. On  
22 the contrary, the jury right which was recognized in Fleitman  
23 can now be given its full scope and effect. And I think that  
24 is what should be done here.

25 There is a second issue which the Respondents have

1 raised but since my time has about run out, I would ask the  
2 Court's permission to reserve the rest of my time.

3 MR. CHIEF JUSTICE BURGER: Mr. Schwartz.

4 MR. SCHWARTZ: Mr. Chief Justice, and may it please  
5 the Court: I think the decisive consideration in this case was  
6 was well put by my brother Haudek on oral argument and in his  
7 brief.

8 I think the controlling consideration, in his words,  
9 is that a stockholder's derivative suit is a creature of  
10 equity. That being so, I think it necessarily follows that  
11 there is no right to trial by jury under either the Seventh  
12 Amendment or Rule 38 of the Federal Rules of Civil Procedure.

13 This Court has said on a number of occasions that  
14 the controlling test under the Seventh Amendment is the test of  
15 history. Put in other words: was there a right to trial by  
16 jury in such a case at the time of the enactment of the Seventh  
17 Amendment in 1791?

18 Or, put another way, under Rule 38: Was there a  
19 right to trial by jury which Rule 38, by its own terms,  
20 preserved inviolate?

21 I think the answer to that question, is historically  
22 determinable and is clear. It is clear that a derivative suit  
23 is and always has been a creature of equity so that no right to  
24 trial by jury existed which the Seventh Amendment or Rule 38  
25 could preserve.

1           With only two exceptions that our research has led  
2 us to, De Pinto in the Ninth Circuit and the decision of the  
3 District Court's judgment claim in this case. We know of no  
4 decision in any Federal Court anywhere which has ever intimated  
5 that a stockholder's derivative suit was triable otherwise than  
6 in the Court as an equitable claim.

7           So far as we know, in the Southern District of New  
8 York, which I believe probably tries more suits of this kind  
9 than any other Federal District, ~~no~~ stockholder's derivative  
10 suit has ever been tried by a jury.

11           As the authorities cited in our brief indicated ---  
12 I hesitate to use the term, but the overwhelming weight of  
13 authority; indeed, unanimous weight of authority with the  
14 exception of De Pinto and the District Court here, has been,  
15 in Mr. Haudek's words, that the derivative is a creature of  
16 equity, and therefore conferred no jury right which the Seventh  
17 Amendment could preserve.

18           Now, as I understand my friend's argument, it is that  
19 history must be reread or rewritten because of what, I submit,  
20 is a misreading of this Court's Opinions in Beacon and Dairy.  
21 The misleading begins with the premise that a derivative suit  
22 is, in essence, a combination of two claims: an equitable claim  
23 against the directors of the corporation for unlawful refusal  
24 to assert a corporate claim and secondly, the claim -- what is  
25 called the underlying claim on behalf of the corporation.

1           Beginning with that premise, Petitioner analyzes  
2 Beacon in the terms that where legal and equitable issues are  
3 joined within the same lawsuit, the Court may not, by first  
4 trying the equitable issue, frustrate the adversary's right to  
5 a jury trial.

6           That reasoning, I submit, is wholly inapplicable  
7 here.

8           Q     Do you think the premise is wrong?

9           A     The premise --

10          Q     The premise -- what you referred to as the  
11 premise, that there are, in effect, two lawsuits.

12          A     Yes, sir. In the stockholder's derivative  
13 suit, Your Honor, I submit there are not two lawsuits. Because,  
14 what my friend calls the first claim; the claim predicated upon  
15 the refusal of the corporation's officers and directors to  
16 assert the corporate claim, I say is inseparable and indivisible  
17 from the claim asserted on behalf of the corporation.

18           Unlike the situation, for example, in Beacon, where  
19 the claim was that the defendants had threatened anti-trust  
20 litigation against the Plaintiffs; had threatened to sue cus-  
21 tomers, and where the plaintiff brought an action, not only for  
22 a suit for injunction, -- against such threats, but also  
23 brought a legal claim for a determination under the Declaratory  
24 Judgment Act of whether the plaintiffs' conduct violated the  
25 anti-trust laws. Unlike that situation, where it was the

1 Plaintiff's option to state those claims separately or to-  
2 gether. In a derivative suit they cannot be separated out.  
3 It is an essential predicate of any derivative suit --

4 Q What is the object of a derivative suit?

5 A The object of the derivative suit, Mr. Justice  
6 Black, is to assert a claim ordinarily against those who con-  
7 trol the corporation, which the corporate entity has, itself,  
8 refused to assert.

9 Q Would that have anything to do here with a  
10 governing law when you try the case for damages?

11 A Governing law in the sense of whether it's  
12 state or Federal?

13 Q No; the law that governs the trial for damages.  
14 Is that controlled at all by the law -- by the principles that  
15 give a right to recover -- make the corporation bring the suit?

16 A I think not, Your Honor, if I understand your  
17 question. Our position is that once the claim is acknowledged  
18 to be derivative in nature -- that is that the plaintiff pur-  
19 ports to assert a claim which is not his own, but a claim of  
20 another -- a corporation in which he claims to own stock --  
21 that that fact and that fact alone makes the action one which  
22 is cognizable historically in equity and only in equity and  
23 regardless of the nature of the claim asserted on behalf of  
24 the corporation, the Seventh Amendment preserved no right which  
25 existed before.



1 I point also, Mr. Justice Black, to Old Equity Rule  
2 27. In the 1880's this Court, after Hawes against Oakland,  
3 promulgated a rule to limit what it considered to be abuses in  
4 stockholder's derivative suits. That rule appeared in the  
5 Equity Rules since 1881 and it's perfectly clear from that  
6 rule that stockholder's derivative suits could only be brought  
7 on the equity side of the Federal District Courts.

8 That rule was lifted almost bodily into the Federal  
9 Rules in 1938 as Rule 23. So, this Court, itself, recognized,  
10 prior to 1938, that the stockholder's derivative suit was a  
11 creature of equity; could only be brought on the equitable side  
12 of the court. And what makes it that way, may it please the  
13 Court, is that it was unknown to the common law that a man  
14 could bring a claim on behalf of another; that the whole area  
15 of court litigation was analogized in the first instance when  
16 the law of trusts --

17 Q What is the basic right of recovery in a deri-  
18 vative suit? What is it the man's after that files a derivative  
19 suit?

20 A Well, in this case, or the case of the  
21 complaint, the man is after money.

22 Q Yes; but what is the basic claim he has; what  
23 does he have to prove to establish his right to go along with a  
24 derivative suit?

25 A He has to prove in this case, Your Honor, two

1 things: first he has to prove a wrongful refusal --

2 Q By corporation to sue?

3 A By corporation to sue and then he must prove,  
4 in his words, "gross breach of fiduciary duty" on the part of  
5 those who control the corporation, with the effect that they  
6 profited unlawfully and should disgorge their profits to the  
7 corporation. That is what he must do.

8 Q And are either one of those issues relevant in  
9 the main action that he wants to get to trial for damages?

10 A I think none of them is relevant -- only one is  
11 relevant to the issue of whether he is entitled to a trial by  
12 jury.

13 Q I'm not talking about a jury; I'm talking about  
14 whether he's entitled to damages.

15 A Well, if he fails to prove unlawful refusal by  
16 the corporation to bring the suit, the suit terminates at that  
17 point. He must surmount that hurdle in order to stay in court.  
18 No matter whether or not --

19 Q -- and if he has proven that, he hasn't proven  
20 anything in connection with the ultimate suit he wants to file  
21 for damages, has he?

22 A Theoretically that's so.

23 Q Isn't it true practically?

24 A No, sir.

25 Q Why not?

1           A        It's not true practically, Your Honor, because  
2 of Rule 23, which as I said before, fits verbatim Old Equity  
3 Rule 27. That rule requires that a plaintiff either allege  
4 that he has made demand upon the corporation and that it has  
5 refused to accede to that demand, or it must allege an excuse  
6 for its failure to do so.

7           If Your Honor will turn to the Complaint in this  
8 case, which is in the Appendix, he will find that in order to  
9 comply with that provision of the rule, the plaintiff alleges on  
10 Page 27 of the Complaint, that the demand to bring suit here  
11 would be futile because the directors are the wrongdoers;  
12 because the corporation is in hostile hands and so on.

13           I can say from my experience that I have never seen a  
14 complaint in a derivative case which does not contain such an  
15 allegation in order to comply with Rule 23. As a practical  
16 matter, that allegation which gets them into court on a deriva-  
17 tive basis in the first place, is ordinarily the crucial issue  
18 in the case on the merits, as between the corporation and the  
19 individuals.

20           So, I say, as a practical matter, the very issue of  
21 demand is basic to the lawsuit itself.

22           Q        Suppose an administrator of an estate or an  
23 estate, refuses to file a suit and someone says he's doing it  
24 by reason of fraud or some legal right to have the suit brought;  
25 what kind of an action would be required against that

1 Administrator to make him file the suit?

2 A In my jurisdiction, Mr. Justice Black, I think  
3 the ordinary action against an administrator of an estate would  
4 be to seek his removal and the appointment of a special ad-  
5 ministrator to bring the suit.

6 Q You mean he couldn't proceed against him to  
7 make him file a suit?

8 A I am not an expert in this -- I doubt it very  
9 much. If I could change the analogy, with Your Honor's  
10 approval, to a trust --

11 Q With that analogy.

12 A Right -- to a trust rather than an administra-  
13 tor, that I suspect that in my jurisdiction there could not be  
14 a derivative suit on behalf of the administrator, but I would  
15 not be positive of that answer. I suspect it could not be  
16 done.

17 Q I ask that question because it seems to me that  
18 here you have a situation where a corporation -- it might be an  
19 administrator; it might be something else -- refuses to file a  
20 suit. The man wants it filed; he thinks he has the right to  
21 recover, say, for fraud or for personal injuries or for a  
22 thousand different things, all of which are triable in a court  
23 of equity. Now, if that administrator

24 Now, if that administrator does refuse to file, do you  
25 mean that -- and somebody does get a way to file it or force

1 him to file it, that all that would be would be an equitable  
2 case?

3 A If, Your Honor --

4 Q IF it was a violation, for instance, of the  
5 anti-trust laws?

6 A If such a suit were maintainable in the Federal  
7 Courts; that is, a suit by a beneficiary of an estate in the  
8 name of and for the benefit of an administrator, against a  
9 wrongdoer, I say that that would be cognizable only on the equity  
10 side of the Court, so to speak, and there would be no right to  
11 trial by jury.

12 Q And it would have to be tried without a jury?

13 A Yes, sir.

14 Q The tail would wag the dog?

15 A I think not because the tail is not that an  
16 alleged beneficiary is bringing the suit, that's the essence of  
17 the claim. A claim takes on a different coloration, has a  
18 completely different posture when it is asserted by the man who  
19 owns it -- by the entity who owns it -- than it does when it's  
20 asserted by one who claims to be, indirectly, one of many  
21 hundreds of beneficiaries. I don't think it's the tail, I think  
22 it colors the whole claim and the nature of the claim and the  
23 manner in which it is tried and the manner in which it is to  
24 be handled, as a matter of judicial administration. I don't  
25 it's the tail.

1 Q Well, it seems entirely separate and distinct  
2 to me. One of the issues here is that a corporation won't  
3 file a suit by reason of fraud or something else. The other  
4 issue is: if the corporation does or it had filed the suit  
5 it can recover damages. It seems to me like they are entirely  
6 separate and distinct.

7 A Your Honor, if they were separate and distinct,  
8 then I submit, as Your Honor pointed out in Beacon, derivative  
9 suits could not have been maintained in the Federal Courts  
10 prior to 1938.

11 Q Well, this was not prior to 1938.

12 A Well, Your Honor, prior to 1938 separate, equal  
13 and equitable claims could not be joined in a single case.

14 Q But they can now; can't they?

15 A They can now, but doesn't it demonstrate the  
16 fact that derivative suits were maintained in Federal Court  
17 before 1938; that the two aspects are not separate, because if  
18 they were separate then there could not have been a derivative  
19 suit in the Federal Court.

20 My point, may it please the Court --

21 Q Has that issue that you were just saying, ever  
22 been dealt with here, that a derivative suit -- in some case  
23 prior to 1938 in this Court said that a derivative suit may  
24 involve a claim for damages and the trial without a jury?

25 A That question was never advertently considered

1 in this Court.

2 Q Just never came up?

3 A No. But, I say it was --

4 Q Fleitman is about the closest thing to it.

5 A I don't know -- I don't -- Fleitman was in a  
6 different context.

7 Q It was a derivative action, wasn't it?

8 A It was a derivative action and Mr. Justice  
9 Holmes had before him the problem of whether there could be  
10 such an animal -- if I may use those terms -- as a derivative  
11 treble damage claim. And he approached that problem by saying  
12 that the right to trial by jury was an essential ingredient of  
13 the scheme of enforcement which Congress had created and that,  
14 essential ingredient could not be satisfied on the equity side  
15 of the Court, ergo, no derivative treble damage claims. It's  
16 the only case which raises that point in this Court.

17 But the point I was trying to make is that the two  
18 aspects could not be deemed separable, because if they had been  
19 separable, there could have been no Equity Rule 27 and there  
20 could have been no derivative jurisdiction in the Federal  
21 Courts at that time.

22 Thank you.

23 MR. CHIEF JUSTICE BURGER: Mr. Haudek, your time has  
24 expired.

25 Thank you, gentlemen, for your submission. The case  
is submitted.