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Right to Jury Trial in Shareholder Derivative Suits

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RIGHT TO JURY TRIAL IN SHAREHOLDER DERIVATIVE SUITS

The right of trial by jury has its origin deeply rooted in Anglo-Norman legal history and tradition, and is manifested in the United States by our federal constitution.[1] This note will examine the applicability of this common law right in a shareholder's derivative suit.

The right to trial by jury in the federal courts has been determined by the use of what has become the "historic test". Under this test the court examined the issue presented and referred to the common law as it existed in 1791 in order to determine whether or not the right existed.[2] If the cause of action were equitable or statutory, the right to trial by jury did not exist unless the legislature had specifically provided for it.[3]

However, more modern issues could not always be firmly placed into the legal framework of the Eighteenth Century. Therefore, the courts have attempted to draw an analogy between the modern action, and some similar action from the past. These courts, however, have often run into problems when they attempted to apply to the Twentieth Century the jurisprudence which developed in Eighteenth Century England.[4] The distinctions were not always based upon a well-planned or reasoned system of law and equity. The two systems were the result of centuries of struggle between the common law courts and the Lord Chancellor, each trying to prevent injustice while at the same time maintaining or in-

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1. U.S. CONST. amend. VII:
> 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.

Fed. R. Civ. P. 38(a):
> The right to trial by jury declared in the Seventh Amendment to the Constitution or as given by statute of the United States shall be preserved to the parties inviolate.

The Seventh Amendment creates no new right to trial by jury. 5 MOORE, FEDERAL PRACTICE ¶ 38.08[6] at 90 (2d ed. 1951).

2. Parson v. Bedford, 28 U.S. (3 Pet.) 433 (1830).

3. *Id.*

4. Under the English system, actions under the common law were entitled to a jury trial, while those under equity jurisdiction were only tried before the Chancellor. 5 MOORE ¶ 38.02[1], at 8-9. This was more than a procedural difference since there were actually two separate court systems deriving their authority and influence from different sources. 2 MOORE ¶ 2.03; James, *Right to a Jury Trial in Civil Actions*, 72 Yale L.J. 655 (1963). The American courts maintained the law and equity distinctions, and actions were fitted into one or the other by analogy to some historical counterpart. Of course this could, and did, lead to a great amount of overlap and confusion as to their respective jurisdictions.

creasing their powers and influence. Many times, the battle for power between Parliament and the Crown was the motivating force behind the various changes and developments in the English legal system.[5] The United States is one of the last surviving beneficiaries of this legacy, for, indeed, even England has largely repudiated the system, and has discarded the jury trial in all but about 2.5% of its civil cases.[6]

The federal courts have tried to eliminate some of the resulting waste and overlap found in the dual system by merging the separate procedures so that legal and equitable issues can be tried together in one "civil action."[7] The general procedure now adopted is to look to the basic nature of the issue.[8] If the issue is basically legal in nature, then the jury right attaches with any equitable issues being tried by the court.[9] If the basic nature of the issue is equitable, the court will decide all the issues,[10] even the incidental legal ones. However, where the case contains both separate legal and equitable issues where one cannot be considered incidental to the other, the problem of trial sequence arises, because a prior determination of facts in the equitable portion of the proceedings may estop further adjudication of any legal issues in a subsequent jury trial.[11] Thus the right to trial by jury could be circum-

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5. For an excellent historical background discussion concerning the right to trial by jury *see* James, *Right to a Jury Trial in Civil Actions*, 72 Yale L.J. 655 (1963). Also see 5 MOORE ¶ 38.02[1] [2].

6. 15 DePaul L. Rev. 403 (1966); JUDICIAL STATISTICS, ENGLAND AND WALES, 1969: *Civil Judicial Statistics* 13 (1970).

7. Fed. R. Civ. P. 1:
> These rules govern the procedure in the United States district courts in all suits of a civil nature whether cognizable as cases at law or in equity or in admiralty, with the exceptions stated in Rule 81. They shall be construed to secure the just, speedy, and inexpensive determination of every action.

Fed. R. Civ. P. 2:
> There shall be one form of action to be known as "civil action."

Fed. R. Civ. P. 18(a):
> A party asserting a claim to relief as an original claim, counterclaim, cross-claim, or third-party claim, may join either as independent or as alternate claims either legal or equitable or maritime, as he has against an opposing party.

Fed. R. Civ. P. 42(a):
> When actions involving a common question of law or fact are pending before the court, it may order a joint hearing or trial of any or all of the matters in issue in the actions; it may order all the actions consolidated; and it may make such orders concerning proceedings therein as may tend to avoid unnecessary costs or delays.

8. 5 MOORE ¶ 38.16 (2d ed.).

9. Dickinson v. General Acc. Fire & Assur. Corp., 147 F.2d 396 (9th Cir. 1945); Prudential Ins. Co. v. Saxe, 134 F.2d 16 (D.C. Cir. 1943).

10. Ring v. Spina, 166 F.2d 546 (2d Cir.), cert. denied, 335 U.S. 813 (1948); Beaunit Mills Inc. v. Eday Fabric Sales Corp., 124 F.2d 563 (2d Cir. 1942); Reliable Mach. Works, Inc. v. Unger, 144 F. Supp. 726 (S.D.N.Y. 1956). *See also* Morris, *Jury Trial under the Federal Fusion of Law and Equity*, 20 Texas L. Rev. 427 (1942).

11. Hopkins v. Lee, 19 U.S. (6 Wheat.) 109 (1821). Partmar Corp. v. Paramount Pictures Theatres Corp., 347 U.S. 89 (1954). *See also, Developments in the Law—Res Judicata*, 65 Harvard L. Rev. 289 (1960).

vented by joining a legal issue with an equitable issue, if the equitable issue were tried first.[12]

In order to handle this problem the federal courts have used various procedures.[13] Traditionally, the courts would decide the equitable issues first. Then any remaining legal issues would be tried before a jury,[14] unless the legal issues were deemed incidental, in which case the court would also settle these legal issues under the "clean up" doctrine.[15] As mentioned before, this procedure presents the problem of estoppel due to the prior determination of the facts by the court.[16]

A second solution would be to try the legal issues first,[17] thus preserving the right to trial by jury. However, this introduces an element of inflexibility into the system because there may be cases where some equitable action should be taken before a jury decision is made on the legal issues.

A third solution would be to give the courts discretionary power to set the order of trial, basing their decision on the facts of the particular case.[18] This would leave the determination of the right to a jury trial to the wisdom of the court, a situation which may not be very satisfactory to those desiring consistency and certainty in the law. It is interesting to note that while we rely on the wisdom of the courts to tell us when our Constitutional rights have been violated, we do not allow them to use that wisdom in a discretionary manner.

The Supreme Court has considered this problem and has established a procedure which provides that a separate law/equity determination will be made for each issue presented, and that legal issues will be tried first. In *Beacon Theaters, Inc. v. Westover*,[19] the plaintiff sought both an in-

12. However, joinder of claims should not effect a waiver of a jury trial. Leimer v. Woods, 196 F.2d 828 (8th Cir. 1952); Ring v. Spina, *supra* note 10.

13. See Comment, 35 N.Y.U.L. Rev. 289 (1960).

14. American Life Ins. Co. v. Stewart, 300 U.S. 203 (1937); Liberty Oil Co. v. Condon National Bank, 260 U.S. 235 (1922); Mather v. Ford Motor Co., 40 F. Supp. 589 (E.D. Mich. 1941).

15. An action "once properly in a court of equity for any purpose will ordinarily be retained for all purposes, even though the court is thereby called upon to determine legal rights that otherwise would not be within the range of its authority." McGowan v. Parish, 237 U.S. 285, 296 (1915).

16. The Supreme Court has consistently demonstrated the importance of this problem in determining if there is a right to trial by jury. Simler v. Conner, 372 U.S. 221 (1963); Dairy Queen, Inc. v. Wood, 369 U.S. 469 (1962); Scott v. Neely, 140 U.S. 106 (1891); Parsons v. Bedford, 28 U.S. (3 Pet.) 433 (1830).

17. Bruckman v. Hollzer, 152 F.2d 730 (9th Cir. 1946).

18. 5 MOORE, ¶ 39.12, at 729.

Fed. R. Civ. P. 42(b):

> The court, in furtherance of convenience or to avoid prejudice . . . may order a separate trial of any claim, crossclaim, or third-party claim, or of any separate issue or of any number of claims, crossclaims, counterclaims, third-party claims, or issues. . . .

19. 359 U.S. 500 (1959).

junction to prevent the defendant from bringng an anti-trust action, and a declaratory judgment. The defendant answered and counterclaimed for treble damages under the anti-trust laws and demanded a jury trial on the factual issues. The trial court held that the issues were primarily equitable and ordered the case to be tried before the court. This ruling was upheld on the initial appeal where the Circuit Court of Appeals for the 9th Circuit stated that the right of trial by jury is determined by looking at the complaint as a whole, and that the complaint was for injunctive relief which was historically equitable. The Supreme Court reversed, holding that the anti-trust issues were cognizable in law, the parties had a right to a jury trial on these legal issues and that the legal issues must be tried first. The Court said,

> [T]hat only under the most imperative circumstances, circumstances which in view of the flexible procedures of the Federal Rules we cannot now anticipate, can the right to a jury trial of legal issues be lost through prior determination of equitable claims.[20]

The Court extended this doctrine in *Dairy Queen, Inc. v. Wood*,[21] where the plaintiff sought an injunction and an accounting in equity for breach of a contract under which defendant had the right to use plaintiff's registered tradename. The Court held that the action was basically for damages for breach of contract and that "the constitutional right to trial by jury cannot be made to depend upon the choice of words in the pleading."[22] The Court went on to say that the right to a jury trial on the legal issues could not be lost even where the legal issues could properly be characterized as incidental to equitable issues.[23]

The rationale used by the Court in both of these decisions was based upon the premise that in both suits there were combinations of separable legal and equitable issues. Under prior practice equity would have

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20. *Id.* at 510-11. The effect of the *Beacon Theaters* decision has been to limit the use of discretion to remove the legal issue from a jury trial. The Fifth Circuit realized this when in a case similar to *Beacon* it held:

> 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 out-weighed 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 right it creates controls. This is the teaching of *Beacon Theaters*, as we construe it.

Thermo-stitch, Inc. v. Chemi-Cord Processing Corp., 294 F.2d 486, 491 (5th Cir. 1961).

21. 369 U.S. 469 (1962).

22. *Id.* at 477-78.

23. It would seem that equity will suffer from this doctrine. Beacon Theaters, Inc. v. Westover, *supra* note 19, at 509:

> Thus, the justification for equity's deciding legal issues once it obtains jurisdiction . . . must be re-evaluated in the light of the liberal joinder provisions of the Federal Rules which allow legal and equitable causes to be brought and resolved in one civil action.

taken initial jurisdiction of both cases and, by trying the equitable issues first, would have estopped any subsequent jury determinations of the legal issues.

Beacon and *Dairy Queen* have removed the problem of loss of the right to a jury determination through estoppel by requiring that the legal issues be tried by a jury and the equitable issues subsequently determined by the court.[24] But it must be remembered that the development of the jury right in *Beacon* and *Dairy Queen* applied only to historically separable legal and equitable issues that joined together under the merged system of procedure. They say nothing about a cause of action that is unitary in nature and found historically cognizable only in equity.

Thus, the procedure for the judicial determination of the right to a jury trial is as follows. First, the parties file their complaints, answers, counterclaims and crossclaims. Then the court examines each separate issue, together with the relief sought, and makes a determination of any right to a jury trial based on the relation of the issue and the remedy to the common law as it had progressed up to 1791. Once this is done, the court will order a jury trial for the legal issues first, then a court trial for the equitable issues. Equity jurisdiction becomes subserviant to the law, so that the cherished right to trial by jury is preserved—and in some cases "preserved" where it had never existed before.

Ross v. Bernhard,[25] is a recent United States Supreme Court decision which carries this approach to the extreme. In this case, the Court was presented with a derivative suit, a creation of equity, and allowed a jury trial on the legal issues presented by the corporation's cause of action, theorizing that had the corporation itself brought suit, it would have enjoyed the right to a jury trial on any legal issues involved. In broad terms, the Court treated the derivative suit as a possible combination of both legal and equitable issues. Because the shareholders have an equitable right to sue in the name of the corporation if the corporation fails to act, the shareholders' right to sue is the equitable issue, and the corporation's right is the second issue which entitles the parties to a jury trial if the corporate right proves to be legal in nature.[26] Thus, applying the doctrine laid down in *Beacon* and *Dairy Queen*, the Court

24. Now a prior determination of the legal issues may estop further equitable determinations. Thus the problem of estoppel is not removed, it is merely reversed.
25. 396 U.S. 531 (1970).
26. At law the corporation is regarded as a unit; and at law, therefore, individual shareholders may not sue although damage to the corporation necessarily has reduced the value of the interest of each shareholder. The complaint of a shareholder is

took a single equitable cause of action, split it, and treated the two parts as separable legal and equitable issues with the right to trial by jury carefully "preserved."

Historically, a shareholder's derivative suit was a creation of the equity courts,[27] because the common law did not provide an adequate remedy for the distressed shareholder. Early English courts allowed the shareholder of a corporation to sue the corporation for breach of its fiduciary duty to the owners. This was the "trust theory" that was later followed by the American courts in the early Nineteenth Century.[28] The corporation was considered as the trustee for the shareholder beneficiaries, and it was, therefore, held to be liable to them either for mismanagement of the business or for the breach of a fiduciary duty. However, where the corporation itself had a legal cause of action against a third party and either failed or refused to act, the shareholders were powerless in any effort to force the corporation to act.

The derivative suit evolved in equity, starting with the trust theory, and later expanding into cases involving shareholders and third parties. While equity allowed the shareholders to sue third parties derivatively in order to enforce their rights, the theory was beginning to change from that of trustee-beneficiary action to that of a dual action, one for the shareholder and one for the corporation.[29] Although the corporation's action could be founded in either law or equity, the equity court retained jurisdiction. The Supreme Court, in *Cohen v. Beneficial Industrial Loan Corp.*[30] put it this way:

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maintainable in equity, where it has been recognized almost since the beginnings of the business corporation. 2 HORNSTEIN, CORPORATION LAW AND PRACTICE sec. 711 at 191 (1959). LATTIN, CORPORATIONS ch. 2 § 11 (1970); STEVENS, CORPORATIONS § 10 (2d ed. 1949). STEVENS also follows the dual analysis of derivative actions in sec. 170.

27. Koster v. Lumbermens Mut. Cas. Co., 330 U.S. 518 (1947); Prunty, *The Shareholders' Derivative Suit: Notes on its Derivation,* 32 N.Y.U.L. Rev. 980 (1957); Glenn, *The Stockholder's Suit—Corporate and Individual Grievances,* 33 Yale L.J. 580 (1924).

28. Robinson v. Smith, 3 Paige Ch. R. 222 (N.Y. 1832), is the American case considered the first shareholder's derivative suit. This case was based on dictum by Chancellor Kent in Attorney-General v. Utica Ins. Co., 2 Johns Ch. R. 371 (N.Y. 1817), where he said:

> The persons who, from time to time, exercise the corporate powers may, in their character of trustees, be accountable to this Court for a fraudulent breach of trust; and to this plain and ordinary head of equity, the jurisdiction of the Court over corporations ought to be confined. at 389.

Robinson applied this when it said:

> The directors are the trustees or managing partners, and the stockholders are the *cestui que trusts,* and have a joint interest in all the property and effects of the corporation. And no injury to the stockholders may sustain by a fraudulent breach of trust can, upon the general principles of equity, be suffered to pass without a remedy. at 232.

See also Taylor v. The Miami Exporting Co., 5 Ohio 162 (1831); and 4 POMEROY, EQUITY JURISPRUDENCE § 1095 (1941).

29. Koster v. Lumbermans Mut. Cas. Co., *supra* note 27 at 522-523; Ashwander v. TVA, 297 U.S. 288 (1936). See also 4 POMEROY, *supra* note 28, at 278.

30. 337 U.S. 541, 548 (1949).

> Equity came to the relief of the stockholder, who had no standing to bring a civil action at law against faithless directors and managers. Equity, however, allowed him to step into the corporation's shoes and to seek in its right the restitution he could not demand on his own.[31]

Today, the ability of the shareholders to enforce the corporate right, when management has failed to take action, is the essence of the shareholder's derivative suit. The right to sue or act on behalf of the corporation does not belong directly to the shareholders,[32] but is derivative or secondary.[33] The primary legal right belongs to the corporation, but the equitable right belongs to the beneficial owners of the corporation, the shareholders.

Before a shareholder can bring this type of action, he must show that he has requested the corporation to take its own action, that the corporation has refused, and that he has exhausted all corporate procedures in his attempt to enforce the corporate right. It must also be shown that the damage is to the corporation, not to the individual shareholder, and that the relief sought will go directly to the corporation and not to the shareholders.[34]

Since the derivative suit was a child of equity, the Seventh Amendment's guaranty of a jury trial had not been applied to these actions.[35] *Liken v. Shaffer*, adequately expressed this point when it said:

> A stockholder's derivative suit is an invention of the courts of

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31. *See* also Koster v. Lumbermans, *supra* at note 27; Meyer v. Fleming, 327 U.S. 161, 167 (1946); Hawes v. Oakland, 104 U.S. 450 (1881); Dodge v. Woolsey, 59 U.S. (18 How.) 331, 341-44 (1855). For further information about the equitable nature of the derivative suit see 3B MOORE ¶ 23.1.15[1].

32. Forbes v. Whitlock, 3 Ed. Ch. 446 (N.Y. 1841), was the first case where a stockholder sued a third party for a breach of contract entered into with the corporation. The court would not use the trust theory in this situation, stating that shareholders "have not such an interest now as entitles them to . . . prosecute on their individual account," and fearing that such a right "would be attended with endless difficulty and embarrassment." at 447-48. But the court went on to say that shareholders have a direct right "when the directors, officers or managers, having the control of the corporation and its affairs, are guilty of misconduct, that amount to a breach of duty as trustees."

33. Dodge v. Woolsey, 59 U.S. (18 How.) 331 (1855).

34. Ross v. Bernhard, *supra* note 25, Fed. R. Civ. P. 23.1.

35. United Copper Co. v. Amal. Copper Co., 244 U.S. 261, 264 (1917). Text writers have said the following:

LATTIN, ch. 8, § 3.

> A derivative action is an invention of courts of equity and may be brought only in equity whether the corporate cause of action be in law or not. As far as corporate rights and defenses available against it are in issue, these is- matter of jury trial, for the case being in equity there is no right to jury trial.

13 FLETCHER CYC. CORP. (Perm. Ed., 1970), § 5931.

> An action by individual stockholders making the corporation a party defendant is equitable in nature, and plaintiffs are not entitled to a jury trial as a matter of right.

Pomeroy, *supra* note 28 and MOORE, § 38.38(4), both find that the derivative suit is an equitable action and therefore find there is no right to a trial by jury.

> equity and is recognizable only in equity and cannot be maintained at law . . . . Even if the claim, if sued directly by the corporation, would be an action at law, yet, if enforced by means of a stockholder's derivative suit, it is prosecuted by an action in equity.[36]

Until *DePinto v. Provident Security Life Insurance Co.*,[37] this area of the law seemed well settled. In *DePinto* the Court of Appeals for the 9th Circuit held there was a right to a trial by jury on any of the legal issues between the parties. No federal or state court had ever made such a ruling before. In *DePinto*, the shareholders accused the directors of fraud, negligence, and breach of fiduciary duty in purchasing worthless shares of another corporation. The shareholders filed a timely demand for a jury trial, but when they later tried to withdraw this motion, the defendant objected contending it had the right of trial by jury. The trial court reserved judgment on the motion and impaneled an advisory jury. After the jury returned its verdict for $20,000, the court entered its own verdict for $314,794.19, ruling that the derivative suit was an equitable cause of action where there was no right to a jury trial. The Court of Appeals reversed and remanded for a new trial, holding that a right to trial by jury exists in shareholder derivative suits.

The court admitted that the shareholder's derivative suit was founded in equity, but it used the conceptual approach of the dual nature of the action to transform it into an action at law. The shareholders can come into court because of their equitable right to protect their beneficial interest in the corporation. Once there, the court will look at the nature of the individual issues that are presented in the corporation's stead. Then, applying the rulings of *Beacon* and *Dairy Queen*, the court said that any of the legal issues presented, whether primary or incidental would be entitled to be tried by a jury.

No court had followed this reasoning until *Ross v. Bernhard*.[38] There the plaintiff accused the directors of gross abuse of trust, gross misconduct, wilful misfeasance, bad faith, and gross negligence, and sought an accounting. While the district court allowed the plaintiff's demand for a jury trial on the factual issues, the circuit court on an interlocutory appeal reversed, and held that there is no right to a trial by jury in a shareholder's derivative suit. The Supreme Court reversed, affirming the district court by applying the reasoning of *DePinto*. The Court held:

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36. 64 F. Supp. 432, 441 (N.D. Iowa 1946).
37. 323 F.2d 826 (9th Cir. 1963) (Cert. denied, 376 U.S. 950 (1964).
38. *Supra* note 25.

> [T]he right to jury trial attaches to those issues in derivative actions as to which the corporation, if it had been suing in its own right, would have been entitled to a jury.[39]

The Court said that the Seventh Amendment right is applicable to any individual issue in a derivative suit which is legal in nature. It reached this decision by using the conceptual approach of the dual nature of the shareholder's derivative suit to split the action into its supposedly separable legal and equitable elements. The derivative suit, even though created and heretofore administered by the equity courts, was no longer a single unitary action. It is now to be considered two separable actions; one in equity, to allow the shareholder in court, and one for the corporate right which could be either legal or equitable. Once the court has ruled on the propriety of the shareholder's right to sue, the court then examines all of the claims existing between the corporation and third parties just as if the corporation itself had brought the action. Any legal issue will be tried by a jury, before any equitable issue is determined by the court, in accordance with the holdings of *Beacon* and *Dairy Queen.*

As the minority in *Ross* said:

> Somehow the Amendment and the Rules magically interact to do what each separately was intended not to do, namely, to enlarge the right to a jury trial in civil actions brought in the courts of the United States.[40]

The majority claimed the merged system merely removes a procedural obstacle that before merger had prevented a jury trial.

The end result may or may not appeal to the reader, but it does seem to be based on an insecure foundation. Had the derivative suit been a combination of two separable causes of action, one legal and one equitable, there would be no problem. The case would fit squarely within the guidelines set down in *Beacon* and *Dairy Queen.* However, the fact of the matter is that the derivative suit is viewed historically as a single action, created by the equity court because of an inadequate remedy at law. Procedural obstacles did not keep the suit out of the law courts—such suits simply were not recognized. The idea that issues of fact must be decided by a chancellor is nothing new in equity, it is a practical reality.

The *Ross* case goes further in granting the right to a jury trial than did *Beacon Theaters* or *Dairy Queen.* In these cases both historically legal and equitable relief was sought. The issues involved would have

39. *Id.* at 532-33.
40. *Id.* at 543.

been tried at law if only the legal relief were sought or in equity if only the equitable relief had been requested. The combination of the two forms of relief in one action caused the problem because historically each would have been treated differently, and the Court was concerned lest the joinder of an equitable claim with a legal one impede the right to a jury trial on that issue.

In *Ross*, on the other hand, there is no question but that historically the whole case would have been tried in equity. Nevertheless, the Court divided the case into two issues, the shareholder's right to sue and the corporation's cause of action, and finding the corporation's cause of action to be legal determined that the right to a jury trial applied to it. In *Beacon* and *Dairy Queen* there was a need to separate the issues because the actions involved a combination of historically separable suits, while in *Ross* there was a historically unitary equitable action. Yet the Court used the same issue approach although the need which led to its adoption in *Beacon* and *Dairy Queen* was not present.[41]

As the dissent correctly states, the difficulty with the issue approach is that many issues could be historically equitable or legal, depending on the action brought.[42] It is this disregard of the nature of the action and the adoption of an issue approach in all cases which leads the dissent to conclude the Court has not "preserved" but extended the right to a jury trial, and to express fears that in other historically unitary legal actions, such as actions solely for an injunction (involving a cause of action which would be tried by a jury if damages had been sought), the Court would now require a jury trial on the underlying issue and a court determination restricted solely to the question of whether the issuance of the equitable remedy was appropriate. It is, however, submitted that on this latter point the fears of the dissenters are probably unwarranted and the impact of the decision will not extend as far as feared by the dissent. The Opinion of the Court, in a footnote, indicated the remedy sought and pre-merger custom are two of three factors to be considered in determining if an issue is legal or equitable.[43] It seems that the case is properly restricted to situations where, like a derivative action, a legal remedy is sought in the context of an action which for historical reasons was cognizable only in equity.

The state courts have consistently followed the traditional equitable approach to the derivative suit; and, when the question has been raised,

41. The Court had also previously used an issue approach in declaratory judgment actions, where the action was historically neither legal nor equitable. *Beacon Theaters*, *supra* note 19; Simler v. Conner, *supra* note 16.
42. 396 U.S. at 549-50.
43. *Id.* at 538; note 10.

they have denied the claimant the right to trial by jury.[44] Many states, including Illinois have not considered the question presented in *Ross v. Bernhard*, but in practice they have allowed the derivative suit to be heard only as one historically cognizable in equity and not at law.

In Illinois, the historical background of the derivative suit closely parallels the development within the Federal system. The Illinois courts originally viewed the corporation as a trustee of the shareholder's beneficial interests, owing a fiduciary duty to the shareholders.[45] For a breach of this duty, the shareholder had a cause of action against the corporation in equity. Eventually the Illinois courts allowed the shareholders to enforce corporate rights against third parties. Again, shareholders were required to show that they had made a just demand for action, that the demand had been refused, and that all other corporate remedies had been exhausted.[46]

It is important to remember that the shareholder's derivative suit was a creation of equity, and not the common law. In *McIlvaine v. City National Bank & Trust Co. of Chicago*, the court said:

> Normally a cause of action accruing to a corporation is to be enforced by the corporation itself, whether by an antitrust law or a suit in equity. Stockholders cannot ordinarily maintain a suit to enforce any right of the corporation. There is no common law right in the stockholders or creditors to sue derivatively in the name of a corporation. The privilege of maintaining derivative suits has been accorded to stockholders and creditors, whenever the corporation, either actually or virtually, refused to institute or prosecute a cause of action. Then in order to prevent a failure of justice equity will permit a suit to be brought and maintained by a stockholder or stockholders substituting or subrogating them for the benefit of the corporation to the corporation's right of action.[47]

The Illinois Constitution provides that, "The right of trial by jury as

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44. Goetz v. Manufacturers' & Traders' Trust Co., 154 Misc. 733, 277 N.Y. Supp. 802 (Sup. Ct. 1935); Metcalf v. Shamel, 166 Cal. 2d 789, 333 P.2d 857 (1959); Morton v. Morton Realty Co., 41 Idaho 729, 241 P. 1014 (1925); Neff v. Barber, 162 N.W. 667 (1917); Steinway v. Griffith Consol. Theaters, 273 P.2d 872 (Okla. 1954).

45. Farwell v. The Great Western Telegraph Co., 161 Ill. 522, 44 N.E. 891 (1896).

46. City of Chicago v. Cameron, 120 Ill. 447 (1887); Bruschke v. Der Nord Chicago Schuetzer Verein, 145 Ill. 433 (1893); Schmidt v. Crowell-Collier Pub. Co., 349 Ill. App. 229, 110 N.E.2d 464 (1953).

47. 314 Ill. App. 496, 512; 42 N.E.2d 93, 102 (1942). It should be noted that in *McIlvaine*, the court said that "there is no common law right in stockholders or creditors to sue derivatively in the name of the corporation." In facing the question of creditors suing shareholders derivatively through the corporation, the Illinois Supreme Court said that there was no right to a jury trial because the action was found only in equity. Parmalee v. Price, 208 Ill. 544, 70 N.E. 725 (1904); Golden v. Cervenka, 278 Ill. 409, 116 N.E. 273 (1917). Since this is the other side of the same "derivative" coin, it may be a good indication of how the Illinois courts would handle the question of the right to a jury trial for a shareholder's derivative suit today.

heretofore enjoyed, shall remain inviolate."[48] The approach taken to determine whether this right exists is determined by an examination of the common law as it existed at the time the Illinois Constitution was adopted.[49] In applying this right, the Illinois Supreme Court has limited it to traditionally recognized common law causes of action or to actions where it has been specifically authorized by the Legislature.[50]

Illinois has eliminated the procedural distinctions between law and equity,[51] and legal and equitable issues can be tried together in one action.[52] So in a situation where both legal and equitable issues have been joined, and the court has determined that there is a right to a jury trial on the legal issues, these issues must be separated from the equitable ones as the chancellor can no longer maintain jurisdiction over them.[53] The Illinois court has the discretion to determine whether or not the legal and equitable issues are separable[54] and in what order they will be tried.[55] In determining which issues are legal and which are equitable, the Illinois courts have held that where a declaration of rights alone

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48. Ill. CONST. Art. I, sec. 13 (1970).

49. People v. Kelly, 347 Ill. 221, 179 N.E. 898 (1931); People v. Niesman, 356 Ill. 322, 190 N.E. 668 (1934); People v. Bruner, 343 Ill. 146, 175 N.E. 400 (1931); Stephens v. Kasten, 383 Ill. 127, 48 N.E.2d 383 (1943).

50. Weininger v. Metropolitan Life Insurance Co., 359 Ill. 584, 195 N.E. 545 (1935); Fisher v. Burgiel, 382 Ill. 42, 46 N.E.2d 380 (1943); Lazarus v. Village of Northbrook, 31 Ill. 2d 146, 199 N.E.2d 797 (1964). Houston v. Brackett, 38 Ill. App. 2d 463, 187 N.E.2d 545 (1963); Flaherty v. Murphy, 291 Ill. 595, 126 N.E. 553 (1920). The Illinois Supreme Court has said that the jury trial is the favored mode of adjudication. Dept. of Public Works & Buildings v. Melling, 78 Ill. App. 2d 37, 222 N.E.2d 515 (1966). This feeling was adequately stated in Ney v. Yellow Cab, 2 Ill. 2d 74, 84, 117 N.E.2d 74, 80 (1954) where the Supreme Court said:

> The right of trial by jury is recognized in the Magna Carta, our Declaration of Independence, and both our State and Federal Constitutions. It is a fundamental right in our democratic judicial system. Questions which are composed of such qualities sufficient to cause reasonable men to arrive at different results should never be determined as matters of law. The debatable quality of issues such as negligence and proximate cause, the fact that fair-minded men might reach different conclusions, emphasize the appropriateness and necessity of leaving such questions to a fact finding body. The jury is the tribunal under our legal system to decide that type of issue. To withdraw such questions from the jury is to usurp its functions.

51. Ill. Civ. Pr. Act, Sec. 1.

> The provisions of this Act apply to all civil proceedings, both at law and in equity. . . . As to all matters not regulated by statute or rule of court, the practice at common law and in equity prevails.

52. Ill. Civ. Pr. Act Sec. 44:

> Joinder of causes of action and use of counter claims—Transfer from one docket to another. (1) Subject to rules any plaintiff or plaintiffs may join any cause of action, whether legal or equitable or both, against any defendant or defendants. . . .

53. Rozema v. Quinn, 51 Ill. App. 2d 479, 201 N.E.2d 649 (1964). The equity court may grant a jury trial, but it will be advisory only. Highland Park v. Calder, 269 Ill. App. 255 (1932).

54. Ill. Sup. Ct. Rules 135 and 232.

55. Usually the courts follow the old Federal procedures of trying the equity issues first, then the legal issues. Williams v. Northern Trust Co., 316 Ill. App. 148, 44 N.E 2d 333 (1942); Ill. Civ. P. Act, Sec. 44.

is sought, the jury right is determined by an examination of the disputed issues and the characteristics of the facts which would indicate the appropriateness of legal or equitable relief. However, where relief is sought, the nature of the relief is determinative.[56]

There is no case in Illinois comparable to *Beacon* or *Dairy Queen* holding that the legal issues are to be tried first to prevent the possible problem of estoppel because of a prior determination of common equitable facts. Thus Illinois lacks the first step in any attempt to follow the *Ross* analysis. It would seem that the court, if presented with a controversy which included both legal and equitable issues, would determine any jury right by an examination of the individual remedies sought along with the appropriate historical background. If the issues can be separated, the court will do so upon a proper jury demand.

In the shareholder's derivative suit, the court would not look at the basic nature of the issue, but rather to the nature of the relief that the shareholders are entitled to, the derivative suit, historically a unitary action founded only in equity. Therefore, under present practice in Illinois, the courts should deny a request for a jury trial on any factual issues in the derivative suit.

WARREN J. MARWEDEL

56. Lazarus v. Village of Northbrook, *supra* note 50, Beck v. Will County, 34 Ill. 2d 588, 218 N.E.2d 98 (1966).