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THE SETTLEMENT AND DISMISSAL OF STOCKHOLDERS' ACTIONS—PART I

by

William E. Haudek*

SINCE the adoption of Federal Rule 23 (c) in 1938, federal practice has permitted the dismissal or compromise of class suits, including stockholders' derivative and representative actions, only with the approval of the court. The Rule made provision for notice of the proposed dismissal or compromise to the members of the interested class; an amendment of the Rule in 1966 has tightened the notice requirement. A majority of the states have followed the federal model more or less faithfully, and a substantial wealth of federal and state decisions, mostly in the field of stockholders' actions, has undertaken to give detailed meaning to the general language of the Rule. Although the abuses at which the Rule was directed seem to have been largely eliminated, new problems have arisen and quite a few of them stubbornly defy satisfactory solution.

This paper will review some of the experiences gathered and some of the difficulties encountered during the last thirty years in connection with the compromise and dismissal of stockholders' actions. The first part of this Article discusses the history and purposes of Federal Rule 23 (c), the types of stockholders' suits and proceedings to which it applies, and the dismissal of such suits. The second installment, scheduled for publication in the May 1969 issue of the Journal, will deal with the settlement of stockholders' actions, including the permissible and desirable terms of the

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1 Fed. R. Civ. P. 23(c).

2 Id. 23(e), as amended; id. 23.1.


I. Forms of Stockholders' Actions

Pursuant to a familiar distinction, stockholders' class suits are either "derivative" or "representative." In a derivative suit, the complaining stockholder asserts a cause of action belonging to his corporation; he is permitted, subject to rather stringent conditions, to enforce the corporate claim where the directors cannot or will not do so. The recovery in such a suit normally belongs to the corporation. In a representative action, on the other hand, the stockholder advances a claim of his own and, at the same time, asserts the related rights of other shareholders. This type of action is marked by the great variety of rights that may be alleged, of the relief that may be sought, and of the scope of the class the plaintiff may represent. Suits to dissolve a corporation, to enjoin the dilution of outstanding shares, to declare the relative voting rights of classes of stock, or to recover damages for shareholders defrauded by false financial statements may serve as random examples of stockholders' representative actions. Any tangible recovery goes to the plaintiff and the class members he represents. The dividing line between derivative and representative stockholder suits is not always sharply drawn. Nevertheless, the distinction, as will be seen, may be relevant to several incidents of the settlement of stockholders' class suits.

II. The Federal Rule: Its History and Purpose

History. The evils which Federal Rule 23 (c) was designed to cure have often been recited. From the early days of the class suit, it had been widely accepted doctrine that a representative or derivative plaintiff owed no duties to his class or corporation. He was the dominus litis; since he

12 Thus the authorities differ whether an action to compel the declaration of dividends is representative or derivative. Compare Doherty v. Mutual Warehouse Co., 241 F.2d 609, 612 (5th Cir. 1957), with Elliman v. Elliman, 306 N.Y. 415, 119 N.E.2d 331 (1953).
13 See authorities cited note 4 supra; McLaughlin, Capacity of Plaintiff-Stockholder To Terminate a Stockholder's Suit, 46 Yale L.J. 421 (1936); Moore & Cohn, Federal Class Actions, 32 Ill. L. Rev. 307, 321-25 (1937); Note, Recurrent Problems in Action on Behalf of a Class, 34 Colum. L. Rev. 118, 123-27 (1934); Note, Protection of Non-Participating Stockholders in Representative Suits, 44 Yale L.J. 134 (1935).
bore all the expenses of the action, he could dismiss or compromise it at pleasure and on any terms he saw fit. That right continued until intervention by another class member or entry of a decree in favor of the class. Thus, the class plaintiff could drop his suit in return for the payment to him of a "private settlement" in an amount vastly exceeding his individual interest. Other class members had no right to share in the proceeds of the private settlement and had no standing to object to the dismissal of the suit. Once the action was abandoned, they could not intervene and revive it. There apparently was only one restriction to the class plaintiff's freedom from control: A compromise by the plaintiff of the corporate or class rights could be enjoined or rescinded for fraud or bad faith. To forestall that possibility, the voluntary submission of corporate settlements for judicial approval came into increasing use in the 1930's.

The prevailing state of the law plainly invited abuse. Most stockholders' suits involve corporate or class claims of considerable magnitude. The temptation for the defendants to buy off the plaintiff by a relatively modest private settlement was therefore great. Many stockholders' actions of doubtful merit were brought simply to secure private settlements for themselves and their lawyer. Private settlements also were employed to...

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19 A more rigorous view of the derivative stockholder-plaintiff's duties—treating him like a trustee or guardian ad litem and exercising judicial supervision over all derivative settlements and dismissals—was accepted in California and found occasional expression elsewhere. Whitten v. Dabney, 171 Cal. 621, 154 P. 312 (1915); Spellacy v. Superior Court, 23 Cal. App. 2d 142, 72 P.2d 262 (1937); Lewin v. New York Emblem, Inc., 183 Misc. 181, 169 N.Y.S.2d 744 (Sup. Ct. 1947); Goodwin v. Castleton, 19 Wash. 2d 748, 144 P.2d 725 (1944), Annot., 150 A.L.R. 859 (1944); see Hallett v. Moore, 282 Mass. 380, 185 N.E. 474 (1935); Auburn Button Works v. Perryman Elec. Co., 107 N.J. Eq. 554, 55 A. 1 (Ch. 1931); State ex rel. Milwaukee v. Ludwig, 106 Wis. 226, 82 N.W. 118 (1900).


24 Rogers v. Hill, 34 F. Supp. 358, 367 (S.D.N.Y. 1940); Gerith Realty Corp. v. Normandie Nat'l Sec. Corp., 154 Misc. 211, 20 N.Y.S. 655 (Sup. Ct. 1933), aff'd, 211 App. Div. 717, 269 N.Y.S. 1007 (1934), aff'd, 266 N.Y. 525, 191 N.E. 183 (1934). In both cases, early derivative actions had been voluntarily submitted for judicial approval. In both, the judgments of approval were held to bind the class as res judicata.

25 In addition to the authorities cited note 12 supra, see Wood, Survey and Report Regarding Stockholders' Derivative Suits (1944); Note, Extortionate Corporate Litigation: The Strike Suit, 34 Colum. L. Rev. 1308 (1934).
stifle meritorious suits brought initially in good faith. In derivative suits, the corporation, frequently controlled by the alleged wrongdoers or their allies, could not be expected to resist the sacrifice of claims which it had been unwilling to assert by direct action. Even without a private settlement, complaining stockholders often dropped their suits simply to avoid further expense and trouble. By the time the class suit was dismissed, the statute of limitations or laches often barred other stockholders from bringing actions of their own; advantages already gained in the litigation were lost. The termination of the action without notice to the class also served to conceal whatever wrongs had been done, so that uninformed class members were unable to safeguard their rights. The stockholder's suit was in danger of becoming a tool for defeating the class rights it was intended to protect.

Such, in broad outline, was the law before Rule 23 (c) forbade the dismissal or compromise of a class action without the approval of the court. Under the Rule as originally phrased, notice to the class members of a proposed dismissal or compromise was mandatory only in derivative and other "true" class actions; 30 in other types of class suits notice was to be given only if the court required it. In either case the manner of notice was left to the court's direction. The 1966 amendment of the Federal Rules has segregated representative and derivative actions for separate treatment in Rules 23 and 23.1, respectively; but the substance of old Rule 23 (c) has been preserved, except that class notice of a proposed dismissal or compromise is now mandatory in all types of class suits. 31

The rather bland and general language of the Rule furnishes only limited guidance for its application. The lack of standards for the approval or rejection of a proposed dismissal or compromise is most notable; if the Rule is designed to suppress private settlements, it certainly does not say so. A host of other questions, it will be seen, is left equally without answer. Resort to the underlying purposes of the Rule is, therefore, essential.

Purpose. The draftsmen of the Federal Rules, so articulate on other occasions, accompanied Rule 23 (c) only with this terse explanatory statement: "See McLaughlin, Capacity of Plaintiff-Stockholder to Terminate a Stockholder's Suit, 46 Yale L.J. 421 (1937)." McLaughlin's seminal paper is, therefore, a cardinal source for the interpretation of the Rule and has often been so cited. His strictures of the private settlement 32 have been held to indicate that it was the principal mischief to be eradicated by the
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When a private settlement is not involved, McLaughlin thought that a shareholder-plaintiff, unwilling to invest further in an expensive and burdensome action, should be permitted to drop it unless there would be prejudice to the corporate cause of action by res judicata, limitations, or surrender of a litigative advantage.

The plaintiff's loss of heart, no less than his greed, has thus been held to be a target of the Rule. Indeed, an indirect effect of the Rule may be that the stockholder-plaintiff is now widely treated as a fiduciary owing duties to his class or corporation similar to those of a guardian ad litem or next friend.

Nor was McLaughlin satisfied with curbing only the stockholder-plaintiff's freedom of action: "[I]n a stockholder's derivative suit, we have an unusual difficulty; the good faith of all parties before the court is uncertain." The judicial supervision required by the Rule should, therefore, extend as well to the defendants (the corporation and the alleged wrongdoers).

Despite the great weight of McLaughlin's views, they should not necessarily be accepted as an authoritative gloss on the Rule; substantial differences between his position and the express provisions of the Rule must not be overlooked. McLaughlin saw profound policy differences between representative and derivative stockholders' actions and proposed court approval only for the compromise or dismissal of derivative suits.

The Rule embraces both types of actions. McLaughlin did not envisage notice to the class; the Rule requires it. McLaughlin proposed procedural changes to be achieved without the help of a statute or rule of court. The adoption of Rule 23 (c) made a fresh start; it brushed aside old precedents and opened the path for a new growth of the law. In this regard, the objective should be a just balance between the interests of the litigants and the interests of the class. The operation of the Rule should not, therefore, be rigidly confined to the eradication of past evils; "a principle, to be vital, must be capable of wider application than the mischief which gave it birth."
III. Stockholders’ Class Actions Governed by the Rule

Class Suits and Individual Suits. A suit brought by a stockholder as such need not always be a class suit. An individual stockholder’s action is not governed by the Rule; it may be dismissed or compromised without court approval. Thus an action to compel the registration of the plaintiff’s stock can hardly be anything but an individual suit. In many cases, the stockholder has a choice of suing individually or for a class—as in damage actions for prospectus fraud or in suits to annul proxies improperly procured. Some stockholders’ actions can be maintained only as class suits; derivative actions to redress a wrong to the corporation are the outstanding example. The dismissal or compromise of any stockholder’s class suit requires court approval unless all interested parties consent; in that case the need for class protection disappears and Rule 23(c) is inapplicable.88

The individual or class nature of a stockholder’s action is not necessarily determined by the allegations of the complaint. If the action is brought as a representative class suit, the court must decide whether it can be maintained as such;89 this decision, which should be made early in the case, determines whether the Rule is applicable. When the class suit determination must await the outcome of a hearing on facts,90 the action should not, in the interim, be dismissed or compromised without court approval; such approval will ordinarily be postponed until the class nature of the suit and the scope of the class are settled.91 If, on the other hand, the complaint purports to set forth a claim for individual relief, the action should be treated as an individual suit, even though the facts as pleaded support only a derivative or representative action.92 In such a case the individual complaint may be legally insufficient and subject to dismissal, but the plaintiff should not be cast in a representative role he does not choose to adopt. An amendment of the complaint may, of course, in appropriate circumstances, convert an individual action into a class suit.

Stockholder Intervention in Corporate Action. A corporation, like any other litigant, can ordinarily dismiss or settle its actions without court approval.93

88 Bruckshaw v. Appanoose County Tel. Co., 252 Iowa 1037, 109 N.W.2d 615 (1961) (the two intervening stockholders had acquired all the outstanding stock and had settled with the other parties; dismissal of the action held not to require court approval).
89 Fed. R. Civ. P. 23(c)(1), as amended. The provision deals only with representative class suits and has no counterpart applicable to stockholders’ derivative actions. If an action brought as a derivative suit does not comply with new Rule 23.1, it is subject to dismissal; until its dismissal, however, the action cannot be voluntarily dropped or settled without court approval and class notice.
92 Wolf v. Barkes, 348 F.2d 994, 997 (2d Cir.), cert. denied, 382 U.S. 941 (1967); Post v. Buck’s Stove & Range Co., 200 F. 918, 920-21 (8th Cir. 1912); Cutter v. Arlington Casket Co., 255 Mass. 52, 151 N.E. 167 (1926). A settlement approved by a board controlled by the defendants is subject to the same judicial scrutiny as any other transaction among self-dealing fiduciaries. See Wolf v. Barkes, supra at 996.
Sometimes, however, stockholders are permitted to intervene in a corporate action because conflicting interests of the directors may render them inadequate representatives of the corporation. Such an intervention ends the corporation's unrestricted freedom to dismiss or settle. Since the directors' loyalty is suspect, the intervening stockholders are the true champions of the corporate claim; the case is thus essentially not different from an action brought initially as a stockholder's derivative suit, and the grounds for judicial supervision are no less persuasive.

Takeover of Stockholder's Action by Corporation. In the reverse situation, the corporation may seek to take over a stockholder's derivative action brought for its benefit. This is not a rare occurrence, but it can present some delicate questions. The "beneficiary corporation" is an indispensable party defendant in the derivative action. Nothing prevents it from adopting the complaining stockholder's claim and asserting it as a cross-claim against the "real" defendants. If the corporation and the stockholder-plaintiff join forces, the action continues as a class suit, so that a dismissal or settlement must receive court approval. Often, however, the corporation seeks to oust the original plaintiff and to take sole control of the litigation. Its right to do so, and the effect of a takeover, are still unsettled.

An early California case held that a corporate takeover "in good faith" automatically displaces the plaintiff and reduces him to a "supernumerary party" without standing in the action; the case becomes a suit by the corporation, having come under the control of the defendant, decided not to seek Supreme Court review of adverse en banc decision of equally divided court of appeals; stockholders' motion to intervene in order to seek such review, denied as untimely).


Mecartney v. Guardian Trust Co., 280 F. 64 (8th Cir. 1922); United States Lines, Inc. v. United States Lines Co., 96 F.2d 148 (2d Cir. 1938); Golconda Petroleum Corp. v. Petrol Corp., 46 F. Supp. 23 (S.D. Cal. 1942) (in the latter two cases, the plaintiff corporation, having come under the control of the defendants, sought to dismiss the action; dismissal was denied and a stockholder permitted to intervene and carry on); National Power & Paper Co. v. Rosman, 122 Minn. 355, 142 N.W. 818 (1913) (on similar facts, the dismissal of the corporation's action was vacated and the petitioning stockholders were substituted as parties plaintiff); Park & Tilford v. Schulte, 160 F.2d 984, 988-89 (2d Cir.), cert. denied, 332 U.S. 761 (1947) (stockholder permitted to intervene in corporation's action "to guard against even the appearance of any concerted action" between the corporation and the defendants); Molybdenum Corp. of America v. International Mining Corp., 32 F.R.D. 415 (S.D.N.Y. 1961) (stockholder permitted to intervene in corporation's action where control of plaintiff's board of directors was in serious dispute), and cases cited therein, id. at 419. Contra, General Inv. Corp. v. Warriner, 219 App. Div. 408, 19 N.Y.S.2d 566 (1940) (stockholders cannot intervene in corporation's action). See also Alleghany Corp. v. Kirby, 144 F.2d 171 (2d Cir. 1965), cert. dismissed sub nom. Holt v. Alleghany Corp., 334 U.S. 28 (1946) (corporation, having come under the control of the defendant, decided not to seek Supreme Court review of adverse en banc decision of equally divided court of appeals; stockholders' motion to intervene in order to seek such review, denied as untimely).

poration itself, free of judicial supervision. Such a broad rule, however, appears dangerous. "Good faith" can rarely be disproved; a board of directors arguably implicated in the wrongs complained of should not be permitted to supplant the plaintiff. The same has been held to be true if the board of directors, after initial rejection of the claim, experiences a change of mind. In neither case is the board's reliability as protagonist of the claim sufficiently assured to justify the ouster of the plaintiff and the termination of the class suit safeguards.

In Lazar v. Merchants’ National Properties, Inc., a New York court proposed a different approach: Despite initial rejection of the claim, the corporation should be permitted to supplant the plaintiff if the board's independence and intent to prosecute the action in good faith are established at a hearing on notice to all stockholders. This procedure hardly commends itself. The board's original hostility renders its good faith suspect. The class notice and hearing would be expensive and would unnecessarily divert much time and effort from the main controversy. The protection which Rule 23 (c) affords to the class should not be so lightly dissipated; the Rule was adopted for the very reason that in stockholders' actions the good faith of all parties before the court is uncertain. It seems vastly preferable to retain the original plaintiff as a co-party, so that the action continues as a class suit. The board, to be sure, will then be unable to settle or dismiss the case without court approval, but if the board truly proceeds in good faith it has no reason to shun judicial scrutiny of its actions. Additionally, cooperation between the corporation and the stockholder-plaintiff is likely to be helpful to the corporation's cause.

The corporation may seek to dissociate itself from the derivative action by bringing a separate suit for the same cause in a different court. This device should not be permitted to eliminate the derivative suit and thus to strip the stockholders of their class protection. In one case of that character, in which the corporation was found to have a new and independent board, the federal court stayed the derivative suit until determination of the corporation's state court action. This point is less significant where a new and ostensibly independent board is elected after commencement of the action. See Tenney v. Rosenthal, 6 N.Y.2d 204, 160 N.E.2d 463, 466, 189 N.Y.S.2d 158, 162 (1959). But even the new board's independence may present a fact issue.

50 This point is less significant where a new and ostensibly independent board is elected after commencement of the action. See Tenney v. Rosenthal, 6 N.Y.2d 204, 160 N.E.2d 463, 466, 189 N.Y.S.2d 158, 162 (1959). But even the new board's independence may present a fact issue.
51 McLaughlin, supra note 12, at 435.
52 Margolis v. Zale Corp., N.Y.L.J., March 27, 1968, at 17, col. 2 (Sup. Ct., Index No. 16218/1965, appeal pending), held that, upon class notice and hearing, an independent board installed after commencement of the action and acting in the best interest of the corporation may take over the suit in order to dismiss it. This would seem contrary to Lazar v. Merchants’ Nat’l Properties, Inc., 22 App. Div. 2d 253, 254 N.Y.S.2d 712 (1964), which authorizes a corporate takeover if an independent board intends to prosecute the action in good faith. Under old Fed. R. Civ. P. 23(b), now Fed. R. Civ. P. 23.1, a stockholder’s derivative suit cannot be maintained unless the plaintiff first exhausts his intra-corporate remedies with the board of directors and, if necessary, with the stockholders. Once he has cleared these hurdles, the action should no longer be subject to dismissal at the hands of the corporation. See Outing v. Plum, 212 Iowa 1169, 235 N.W. 519 (1931).
class rights enjoyed at least some protection; a subsequent settlement be-
tween the corporation and the defendants was held to require the approval
of the federal court upon notice to the stockholders. Even with this
limited safeguard, class rights could be jeopardized if the corporation
should prosecute its suit with less than wholehearted zeal. In order to bal-
ance the need for managerial freedom against the need of the stockholders
for protection from managerial abuse, a separate suit by the corporation
should not be permitted to supersede the derivative action unless the board’s
independence and good faith are clearly established and the forum chosen
by the board offers substantial jurisdictional or other advantages over the
forum of the derivative suit. Short of such a reasonable basis, however,
the corporation’s desire to escape the derivative suit and to oust the stock-
holder-plaintiff as a joint litigant may well appear sufficiently suspicious
to justify an order restraining the corporation from proceeding outside the
framework of the derivative action. Where that should not be feasible or
desirable, the stockholder-plaintiff should at least be permitted to intervene
in the corporation’s action.

Actions Similar to Stockholders’ Derivative Suits. An individual director
may, under New York law, bring a derivative suit on behalf of his corpora-
tion if the board refuses to authorize a corporate action. The necessity of
court approval for the dismissal or settlement of such a suit has not yet
been judicially determined, but the similarity of stockholders’ and direc-
tors’ derivative actions is so close that the court approval rule should apply
to both.

A security holder’s action for the recovery of “insiders’ short-swing
profits” pursuant to section 16(b) of the Securities Exchange Act of
1934 is technically not a stockholder’s action because it may be brought
by the holder of any kind of security. Although other parts of Federal
Rule 23 do not apply to this action, it is now settled that a section 16 (b)
suit cannot be dismissed or compromised without court approval and notice
to the class. It might be suggested that the class entitled to notice in-
cludes all security holders of the corporation; but the interest of the

51 The knotty question whether 28 U.S.C. § 2283 (1964) would prevent a federal court from
enjoining a state court suit by the corporation is beyond the scope of this paper. See generally 1A
J. Moore, Federal Practice §§ 0.208–213 (2d ed. 1965). The court in which the corporation
brings its suit, can, of course, stay it pending the determination of the derivative action; but the
defendants will not move for the stay if they expect easier treatment by the corporation than by the
stockholder-plaintiff.
Corp. Law § 720(b) (McKinney 1963). According to J. G. Hornstein, Corporation Law &
Practice § 421, at 524 (1919), there is considerable uncertainty whether this right exists without
statutory basis.
Moss, 393 F.2d 865, 871 (3d Cir. 1968).
holders of promissory notes, bearer bonds or other debt securities appears too remote to require notification, except perhaps by publication. 58

Settlements in bankruptcy proceedings require judicial approval under section 27 of the Bankruptcy Act. 59 If the settlement disposes of conflicting class claims, Rule 23 (c) has been held to be likewise applicable. 60 Without express reference to the Rule, its procedures were employed in the settlement of a receivership suit brought by the Securities and Exchange Commission under the Investment Company Act and the Securities Exchange Act. 61

IV. DISMISSAL

Rule 23 refers separately to the dismissal and the compromise of class suits. Since they involve somewhat different questions, the present discussion deals with dismissals which are not connected with a compromise; the subject of settlements will be treated in the second installment of this Article.

Voluntariness. Only a voluntary dismissal requires class notice and court approval under Rule 23. 62 Since the Rule is designed to protect the class against surrender of class rights by a greedy or fainthearted plaintiff, 63 its purpose does not reach a dismissal that is honestly contested. Class notice is, therefore, normally not necessary if the action is dismissed after hearing or trial 64 or upon grounds such as legal insufficiency of the complaint, 65 lack of personal jurisdiction, 66 or mootness. 66 Like most distinctions, that between voluntary and involuntary dismissals has its practical problems.

The dismissal of a class action for lack of prosecution 67 is, on its face,

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58 Upon settlement of § 16(b) suits, actual notice to the Securities and Exchange Commission and notice by publication to all security holders, including the stockholders, are customary practice. See Blau v. Allen, 171 F. Supp. 669, 670 (S.D.N.Y. 1959); Potash v. Divak, 71 F. Supp. 737, 739-40 (S.D.N.Y. 1947) (requiring also actual notice to the directors). 5


64 Pelelas v. Caterpillar Traction Co., 113 F.2d 629 (7th Cir.), cert. denied, 311 U.S. 700 (1940).


66 National Hairdressers' & Cosmetologists' Ass'n v. Philad Co., 4 F.R.D. 106 (D. Del. 1944); Smith v. Industrial Sec. Corp., 49 F. Supp. 919 (D. Conn. 1943). But see Blau v. Reidy, CCH Fed. Sec. L. Rep. § 92,192 (S.D.N.Y. 1969) (dismissal of a stockholder's derivative action on the ground that payment in full requires notice to the shareholders where the claim was unliquidated and its amount had been computed by the attorney for the plaintiff).

involuntary. One line of cases dispenses, therefore, with notice to the class. The inaction of the plaintiff may, however, be the practical equivalent of a voluntary dismissal. If he accepts a private settlement, or simply gets tired of litigating, a formal discontinuance would invite class notice and scrutiny of his conduct; to avoid these consequences he might simply do nothing and wait for the quiet interment of the dormant action. Since the plaintiff's choice of tactics should not be permitted to determine the class rights, another group of authorities refuses to dismiss a class suit for want of prosecution until the class members are notified of the threatened dismissal and of their right to seek intervention.

The conflict among the decisions suggests the wisdom of avoiding broad generalizations. For the purposes of Rule 23 (c), the potential of mischief is, indeed, the same whether a class suit is dismissed upon the request of the plaintiff or because of his deliberate inaction. Frequently, however, the neglect to prosecute is careless rather than willful; the analogy to a voluntary dismissal is then inapposite. An extreme case of that sort was Partridge v. St. Louis Joint Stock Land Bank. After nine years of skirmishing, the prolonged avoidance of trial by the plaintiffs finally resulted, over their opposition, in a dismissal which was held to be involuntary and hence not to require a class notice. The decision is in accordance with the purpose of Rule 23 (c) since there was no ground to suspect a private settlement or a deliberate abandonment of the action. In other cases, to be sure, the facts will not be so clear-cut and may permit conflicting inferences. It would, therefore, seem preferable to leave the requirement of class notice of a proposed dismissal for lack of prosecution to the discretion of the court. In aid of its discretion, the court might call for proof by affidavit that no improper inducement was offered or given to the plaintiff or his counsel for permitting the action to fail. Under local district court rules, inactive class suits, like other dormant actions, are frequently dismissed more or less automatically upon the court's own motion without notice to the class. The practice is dictated by the

67 Partridge v. St. Louis Joint Stock Land Bank, 130 F.2d 281 (8th Cir. 1942) (creditors' action); see Saylor v. Lindley, 391 F.2d 965 (2d Cir. 1968) (prior stockholder's derivative action had been dismissed, without class notice, for lack of prosecution and failure to give security for litigation expenses); Harman v. Grabowetsky, 21 App. Div. 2d 862, 251 N.Y.S.2d 88 (1964) (director's derivative action); neither of these two cases discussed the requirement of class notice.

68 Webster Eisenlohr v. Kalodner, 143 F.2d 316 (3d Cir.), cert. denied, 321 U.S. 867 (1944) (plaintiffs had sold their shares to the defendants at a premium; action not to be dismissed until notice to other stockholders of their right to intervene); Malcolm v. Cities Serv. Co., 2 F.R.D. 401, 407 (D. Del. 1942); 5 J. Moore, Federal Practice § 41.11(2), at 1164 n.3 (2d ed. 1968). See also notes 73 and 78 infra.

69 110 F.2d 281 (8th Cir. 1942).

70 N.Y. Civ. Prac. Law & R. 1003 (McKinney 1965) makes equal provision for the compromise of a class suit, its dismissal by consent, by default or for neglect to prosecute. In all these cases the New York rule prescribes court approval, but leaves class notice to the discretion of the court.

71 The use of affidavits of this sort is suggested by analogy to Del. Ch. Ct. R. 23, as amended in 1962 and 1968, which permits the court, in its discretion, to dispense with the class notice if the dismissal is without prejudice to the class and "if there is a showing that no compensation in any form has passed directly or indirectly from any of the defendants to the plaintiff or plaintiff's attorney and that no promise to give any such compensation has been made."

necessity of clearing the courts' dockets of deadwood; but the lack of notice may tend to facilitate the abuses which Rule 23 (c) was designed to eliminate. For this reason, at least one case has held that Rule 23 (c) supersedes the local rule. The case has not, however, been followed, perhaps because of the practical difficulties which would attend an insistence on notice. The court will not pay for the expenses of the notice, and no effective machinery to enforce payment by the plaintiff seems available. Since dormant class suits cannot remain indefinitely on the docket, the prevailing practice may be expected to continue despite its potential impact on the effectiveness of Rule 23 (c).

A dismissal for a default of the class plaintiff or for his failure to comply with the Rules or with a court order should be treated like a neglect to prosecute. The court, in the exercise of discretion, should require class notice if the circumstances suggest that the dismissal serves as a cloak for a private settlement or for a voluntary abandonment of the suit.

If the plaintiff in a stockholder's derivative action sells his shares, he loses his standing and is subject to a dismissal on the merits. Since the dismissal rests on the voluntary act of the plaintiff, it should not be allowed without notice to the class; but here again enforcement may be difficult. Unless the defendants were the purchasers, it would be unfair to burden them with the expense of the notice, and no procedure to compel payment by the plaintiff seems to be available.

Lack of opposition by the plaintiff to other types of dismissal—as on a defense motion for summary judgment—will rarely call for notice to the class. Unless the plaintiff's prior neglect of the action renders his class
representation suspect, his failure to resist the dismissal may be taken as a
good faith acknowledgment that there is no basis for opposition. The dis-
missal is then essentially "involuntary." The result is different if the plain-
tiff has stipulated in advance to offer no resistance; the class must then be
notified of the proposed dismissal, no matter how hopeless any opposition
may be. Class notice may also be in order if the plaintiff's surrender
manifestly ignores a promising ground for opposing the dismissal.

In rare circumstances a dismissal voluntary in form may, nevertheless,
be approved without class notice. For instance, federal diversity jurisdi-
cction is destroyed if one of several defendants is a citizen of the same
state as the plaintiff, but the plaintiff can save the action by procuring
its dismissal as to the non-diverse defendant. Although the dismissal is at
the request of the plaintiff, it is involuntary since the alternative is the
dismissal of the entire case.

Forms of Dismissal. The voluntary dismissal of an action is generally gov-
erned by Federal Rule of Civil Procedure 41 (a). Under Rule 41 (a) (1),
a non-class plaintiff can dismiss his suit without court order by filing a
unilateral notice of dismissal or a stipulation of dismissal signed by all ap-
pearing parties. The notice, however, must be filed before the adverse
party serves an answer or a motion for summary judgment; otherwise,
under Rule 41 (a) (2), voluntary dismissal requires an order of the court
upon such terms and conditions as the court deems proper.

In class suits, Rule 41 (a) (1) is expressly made "[s]ubject to the pro-
visions of Rule 23 (c)." The intent of this language is not altogether
clear. Since Rule 23 (c) and its successors prescribe court approval of the
voluntary dismissal of a class suit in all cases, it might be suggested that
the 41 (a) (1) procedure, which dispenses with a court order, is wholly
inapplicable to class suits; but this conclusion is neither necessary nor de-
sirable. There is at least one distinct advantage available to the plaintiff
through the utilization of Rule 41 (a) (1) in the voluntary dismissal of a
class suit. By filing a timely notice of dismissal or a stipulation of dismissal
under Rule 41 (a) (1), the class plaintiff bars any objections by the defend-
ants. The court's approval of the dismissal of the class suit is still necessary
under Rule 23 (c), but in granting or withholding it, the court will con-

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80 Brendle v. Smith, 7 F.R.D. 119 (S.D.N.Y. 1946); see Certain-Teed Prods. Corp. v. Topping, 171 F.2d 241 (2d Cir. 1948).
84 Horn v. Lockhart, 84 U.S. (17 Wall.) 570, 579 (1873); Oppenheim v. Sterling, 368 F.2d 316, 318 (10th Cir. 1966); Kerr v. Compagnie de Ultramar, 250 F.2d 860 (2d Cir. 1958).
85 Cohn v. Columbia Pictures Corp., 9 F.R.D. 204 (S.D.N.Y. 1949); Contra, Robertson v. Limestone Mfg. Co., 20 F.R.D. 365, 374 (W.D.S.C. 1957). In the reverse situation, a class plaintiff unsuccessfully sought to dismiss one of several defendants in order to destroy diversity of citi-
sider only the interests of the class, not those of the defendants. An application to dismiss after joinder of issue would entitle both the defendants, Rule 42(a)(2), and the class, Rule 23(c), to the court's consideration. An amendment of the complaint that drops some or all of the class claims has the same effect as a voluntary dismissal and should, therefore, require court approval and class notice. In this connection, it should make no difference whether the plaintiff amends the complaint by stipulation, by leave of court, or “as a matter of course” before a responsive pleading is served.

A subtle method to avoid class notice has recently met with judicial encouragement. In several stockholders' representative cases, the parties jointly asked the court to determine that the requisites of a class suit were not satisfied. In the absence of opposition, the court made the requested finding and permitted in one case the action to proceed as an individual suit, authorized in another the private settlement of the suit, and approved the dismissal of the action in a third, in each instance without notifying the class. This, it would seem, is dubious practice. The criteria of a proper representative action are not mechanical; the sufficiency of the size of the class, the adequacy of the protection of the class interests by the plaintiff, the preponderance of common over individual questions, and the superiority of the class suit over other procedural devices may all give rise to legitimate and substantial differences of opinion. To reach

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87 In Cross v. Oneida Paper Prods. Co., 117 F. Supp. 919, 921 (D.N.J. 1954), a class plaintiff's unilateral notice of dismissal, filed before answer pursuant to FED. R. CIV. P. 41(a)(1), was vacated upon motion of the defendants for lack of court approval and class notice. It does not appear why the court did not, at that stage, direct notice to the class and a hearing; perhaps the plaintiff was unwilling to undertake the expense of the class notice. The defendants were, of course, free to call the court's attention to the lack of a class notice. Accord, Ensher v. Ensher, Alexander & Barroom, 187 Cal. App. 2d 407, 410, 9 Cal. Rptr. 732, 734 (1960).

88 In Delahanty v. Newark Morning Ledger Co., 26 F. Supp. 327 (D.N.J. 1939), the plaintiffs in a stockholders' derivative action moved during trial for a dismissal without prejudice. Following notice to the class, the court held that the defendants were entitled to dispel the clouds hung over them by the action and directed a dismissal with prejudice or the resumption and conclusion of the trial.

In Mashek v. Silberstein, 20 F.R.D. 481 (S.D.N.Y. 1957), a stockholders' derivative suit, the court permitted one of the plaintiffs to dismiss the action as to him on condition that he submit to his deposition by the defendants. Although the court referred to FED. R. CIV. P. 23(c), it did not require notice to the class.

89 Ensher v. Ensher, Alexander & Barroom, 187 Cal. App. 2d 407, 9 Cal. Rptr. 732 (1960). The opposite result, but without reference to FED. R. CIV. P. 23, was reached in Kohler v. Humphrey, 174 F.2d 946 (5th Cir. 1949). After the complaint had been sustained as a stockholder's derivative action, the plaintiff amended it so as to assert an individual instead of a derivative claim. Because of this change, another stockholder's application to intervene in the suit as in a derivative action was denied.

90 FED. R. CIV. P. 11(a).


95 FED. R. CIV. P. 23(a)(1), as amended.

96 Id. 23(a)(4), as amended.

97 Id. 23(b)(3), as amended.

98 Id.

99 Compare, e.g., Eisen v. Carlisle & Jacquelin, 391 F.2d 555 (2d Cir. 1968), with the lower court's opinion in the same case, Eisen v. Carlisle & Jacquelin, 41 F.R.D. 147 (S.D.N.Y. 1966);
a sound decision, the court needs an adversary presentation of the conflicting viewpoints. A class plaintiff anxious to accept a private settlement or otherwise to shed his representative duties cannot perform the adversary role. In these circumstances, the class should have an opportunity to be heard before the court determines the class or nonclass character of the action. Interlocutory consent orders which do not provide for the dismissal or settlement of the class suit are not governed by Rule 23 and need not be on notice to the class. Similarly, events occurring outside the framework of the lawsuit afford no basis for the application of Rule 23. Thus a private settlement by the stockholder-plaintiff or the sale of his shares will not, by themselves, trigger judicial action, even though they come to the court's attention. The Rule does not vest the court with inquisitorial powers. Occurrences such as those indicated must be actually invoked as grounds for dismissal before the court has occasion to grant or withhold its approval or to direct notice to the class.

Partial Dismissal. The authorities do not agree on the particular rule of law governing the dismissal of an action as to less than all the plaintiffs or defendants. For the purposes of Rule 23 (c), this technical controversy would seem unimportant. Whether Federal Rule 41 (a) (voluntary dismissal), Rule 21 (dropping of parties), Rule 15 (a) (amendment of pleadings) or the general powers of the court be deemed most nearly in point, the incidents of the partial dismissal of a class suit should be determined in light of the purposes of Rule 23 (c).

The dismissal of a class suit as to ‘part of the defendants’ lends itself to the same abuses as the dismissal of all. The partial dismissal may be the result of a private settlement; it may afford the haven of the statute of limitations.


The plaintiffs in Berger v. Parolator Prods., Inc., 41 F.R.D. 342 (S.D.N.Y. 1966), openly argued for a non-class suit determination in order to be able to accept a private settlement offered by the defendants.

In the Jacobs and Polakoff cases, the courts disqualified the actions as class suits because the plaintiffs, no longer willing to represent the class, could not adequately protect the class interests. Upon reasoning like this, a class plaintiff might always secure a dismissal without class notice by the simple device of stating that he no longer wants to represent the class. The proper response to such a statement would be a notice inviting the class to take over.

Cunningham v. English, 269 F.2d 139, 141 (D.C. Cir. 1919). But a union on whose behalf a class suit was brought could not, without class notice, commit itself by a consent order to pay the plaintiffs' counsel fees. Id.


limitations to the dismissed defendants; or it may render the further prosecution of the action unpromising if the remaining defendants are marginal or of doubtful solvency. A dismissal as to less than all of the defendants requires, therefore, court approval upon notice to the class. The class notice may be dispensed with where a party has been inadvertently named as a defendant or where the dismissal of a defendant is necessary to cure a defect in the diversity jurisdiction of the federal court.

The dismissal of a class suit as to part of the plaintiffs presents different considerations. Since, by hypothesis, the remaining plaintiffs continue the litigation, a private settlement with those who withdraw would make no sense and need not be suspected; nor does their withdrawal raise the specter of the statute of limitations. The remaining plaintiffs may possibly be less competent, aggressive or tenacious than their ex-colleagues, but if they should prove inefficient or try to bow out, there will still be time to notify the class. Normally, therefore, a dismissal as to less than all of the class plaintiffs does not involve the mischiefs of a total dismissal and Rule 23(c) is inapplicable. Court approval and class notice are necessary, however, if the candidates for withdrawal have alleged claims which the other plaintiffs do not or cannot assert (for instance, because they had not been stockholders at the time the derivative claims alleged by their withdrawing colleagues accrued).

Relevance of Prior Interventions. The adoption of Rule 23(c) did not at once succeed in eliminating the effects of the earlier law it was designed to supersede. Under the influence of that law, a 1941 decision of the First Circuit, May v. Midwest Refining Co., assumed that the Rule permits the settlement or dismissal of a stockholder's derivative action without court approval or class notice if the rights of other class members are not affected, i.e., if no other class members have intervened in the action and if no settlement of the corporate claim is involved. Although the court's language was probably mere dictum, it has been often cited and occa-

111 See 121 F.2d 431, 439-40 (1st Cir.), cert. denied, 314 U.S. 668 (1941).
sionally followed. By now, however, rigorous distinctions and severe criticism seem to have destroyed its vitality as a precedent. The requirement of court approval and class notice under the Rule is absolute and does not depend on the intervention of other stockholders. A compromise of a derivative action not designed to satisfy the corporate claim is a private settlement; as such, it is a primary target of the Rule.

Judicial Approval. In contrast to its explicit insistence on class notice and judicial approval, Rule 23 omits any standards for the guidance of the court in granting or withholding its approval. While the authorities have developed criteria for the approval of class suit settlements, they are singularly reticent in dealing with class suit dismissals.

One principle should be clear: a dismissal should ordinarily not be approved when class members, in response to a class notice, seek to intervene and continue the action. Indeed, since the original plaintiff cannot be forced to carry on, the class notice would, as a rule, be pointless unless it is designed to give the class members an opportunity to intervene. Grounds to deny the intervention will, therefore, be rare. The plaintiff certainly cannot oppose it since he withdraws from the case. Nor should the defendants be entitled to object to the substitution of a willing for an unwilling class champion. The merits and prospects of the litigation would seem irrelevant. The request to intervene will, as a rule, be "timely" since it is occasioned by the proposed dismissal.

The intervenor must,


\[115\] Questions concerning the content and other incidents of the class notice are treated in the second part of this Article in connection with the discussion of class suit settlements.

\[116\] In Brendle v. Smith, 7 F.R.D. 119 (S.D.N.Y. 1946), the court required class notice of a defense motion for summary judgment based on res judicata because the plaintiff had stipulated not to oppose the motion (see note 80 supra). The notice directed the class to show cause why summary judgment should not be granted.

\[117\] If the stockholder-plaintiff has sold his shares to the defendants, other class members have an absolute right to intervene. Webster Eisenlohr v. Kalodner, 141 F.2d 316, 320 (3d Cir. 1944), cert. denied, 325 U.S. 867 (1945) (dictum); Malcolm v. Cities Serv. Co., 2 F.R.D. 405, 407 (D. Del. 1942) (dictum).

\[118\] In Brown v. Bullock, 35 Misc. 2d 370, 230 N.Y.S.2d 660 (Sup. Ct. 1962), aff'd, 17 App. Div. 2d 424, 231 N.Y.S.2d 817 (1962), motion to dismiss appeal denied, 13 N.Y.2d 667, 191 N.E.2d 161 (1963), class members were denied intervention because of their failure to demonstrate the likelihood of success of the action. Likelihood of success is not, however, a factor relevant to the right of intervention under Fed. R. Civ. P. 24 or corresponding state laws.

In Pittston v. Reeves, 263 F.2d 328 (7th Cir. 1959), the district court had authorized the voluntary dismissal of a stockholder's derivative action without notice to the class. Upon appeal by an intervening class member, the court of appeals vacated the order of dismissal, directed that the class be notified, and left to the district court the determination whether the class members "will or will not be prejudiced by the dismissal." This somewhat cryptic statement may refer to a settlement among the original parties briefly mentioned in the opinion, but the facts are set forth too scantily to throw light on the quoted phrase.

of course, be qualified to represent the class. The court may impose reasonable conditions upon the intervenor; thus if the action has been pending a long time and has been amply prepared for trial, the court might curtail further pretrial proceedings and require an early trial.

Even if no class member intervenes, the dismissal of the class suit still requires court approval under the Rule. The court remains, therefore, under a continuing responsibility to consider the interests of the class. Above all, the dismissal must not be a cloak for a private settlement. At times, a proposed class suit dismissal is accompanied by an arrangement under which the defendants are to pay the fee of the plaintiff's lawyer. Although this practice was tolerated for a while, it is now clear that the payment constitutes a private settlement, and that a dismissal contemplating such a payment must be disapproved. The lawyer for the class plaintiff is under the same duty as the plaintiff himself to protect the interests of the class; if his compensation could be tied in with the dismissal of the action, his self-interest would not parallel the interests of the class and his reliability as a class protector would be perverted.

Apart from the prevention of private settlements, the court can do little to protect a class whose members are unwilling or perhaps unable to intervene and thereby to forestall a dismissal. Even though the institution of a new suit may be barred by the statute of limitations, the court cannot force the plaintiff to proceed with the pending action. The imposition of "terms and conditions" pursuant to Federal Rule 41(a)(2) may require the plaintiff, for instance, to pay the defendants' costs and expenses as a condition of the dismissal, but that is a matter between the parties and does not concern the class. A more serious question arises from the court's power, under Federal Rule 41(a) and (b), to choose between a dismissal "without prejudice" and one "upon the merits." The exercise of that power in stockholders' class suits is closely tied to the

\[\text{In a stockholder's representative suit, the intervenor must satisfy the court that his claim is typical of the class claims and that he will fairly and adequately protect the class interests. Fed. R. Civ. P. 23(a)(3), (4), as amended. In a stockholder's derivative action, the burden of demonstrating the intervenor's inadequacy rests on his adversaries. Fed. R. Civ. P. 23.1.}\]

\[\text{In a majority of stockholders' class suits, the fees of plaintiffs' counsel are contingent upon the success of the action; Smolowe v. Delendo Corp., 136 F.2d 231, 241 (2d Cir. 1943); Eisen v. Carlisle & Jacquelin, 370 F.2d 119 (2d Cir. 1966), cert. denied, 386 U.S. 1035 (1967).}\]

\[\text{Fistel v. Christman, 133 F. Supp. 300 (S.D.N.Y. 1955), refusing to follow two contrary unreported decisions.}\]

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\[\text{Dabney v. Levy, 191 F.2d 201 (2d Cir.), cert. denied, 342 U.S. 887 (1951); Certain-Teed Prods. Corp. v. Topping, 171 F.2d 241, 243 (2d Cir. 1948). These cases deal with dismissals yielding no benefit to the class or corporation. Fee arrangements in connection with proper corporate or class settlements involve different principles.}\]

\[\text{5"Fistel v. Christman, 133 F. Supp. 300 (S.D.N.Y. 1955), refusing to follow two contrary unreported decisions.}\]

\[\text{In a majority of stockholders' class suits, the fees of plaintiffs' counsel are contingent upon the success of the action and are payable out of the recovery. See Marine Midland Trust Co. v. Forty Wall St. Corp., 11 App. Div. 2d 118, 121, 213 N.Y.S.2d 689, 692 (1961), aff'd, 11 N.Y.2d 679, 180 N.E.2d 909, 227 N.Y.S.2d 775 (1962); Hornstein, The Counsel Fee in Stockholders' Derivative Suits, 39 COLUM. L. REV. 784, 805 n.133 (1939).}\]


\[\text{2B W. BARRON & A. HOLZOFF, FEDERAL PRACTICE & PROCEDURE § 914 (C. Wright rev. ed. 1961); J. MOORE, FEDERAL PRACTICE §§ 41.06 (2d ed. 1968).}\]
broader problem of whether a voluntary dismissal with prejudice can preclude the rights of the corporation or class. The problem calls for separate discussion.

The Effect of a Voluntary Dismissal upon the Rights of the Class. Under Federal Rule 41 (a), a voluntary dismissal—whether by unilateral notice, stipulation or court order—is "without prejudice" unless otherwise provided in the notice, stipulation or order. If the court or the parties "otherwise" provide, the dismissal is "upon the merits." Likewise, a unilateral notice of dismissal "operates as an adjudication upon the merits" when filed by a plaintiff who has once before dismissed an action based on the same claim.

If a stockholder's class suit is dismissed without prejudice, other class members are free, of course, to bring a new action on the same claim. Clearly, also, a voluntary dismissal "upon the merits" or "with prejudice" will bar a similar action by the same plaintiff. Does such a dismissal also preclude other class members—or, in the case of a derivative action, the corporation—from bringing or continuing a suit on the same cause? There is a dearth of authorities,18 and the question does not lend itself to an easy answer.

It has frequently been held by high authority that a judgment on the merits in a true class suit binds the class.19 The holdings assume, however, that the class was adequately represented by the plaintiff.180 Adequate representation is required by constitutional due process,181 and the Federal Rules make the requirement explicit.182 A class plaintiff who voluntarily seeks to dismiss his action is an inadequate class representative.183 He disavows his representative role and duties. If he consents to a dismissal with prejudice to the class, he assumes a position hostile to the class rights. A class litigant with interests antagonistic to those of the class is the prototype of an inadequate representative.184 It would seem to follow that the

18 In Kaufman v. Annuity Realty Co., 301 Mo. 638, 256 S.W. 792 (1923), the plaintiffs in a stockholders' derivative action had secured the appointment of a receiver; upon appeal by the defendants, the parties filed a stipulation setting aside the decision and dismissing the action. A second similar suit by other stockholders, who claimed that the dismissal of the first action had been fraudulent, was dismissed on the ground of res judicata; the judgment, it was held, could not be attacked collaterally for fraud. The decision, rendered long before the adoption of the Federal Rules, hardly is a precedent for class suits under the Rules or their state counterparts. Even at the time it was rendered it was probably an anomaly.


187 Id.

188 Fed. R. Civ. P. 23(a) (4), as amended; id. 23.1.


voluntary dismissal of a class suit, even though declared to be on the merits, cannot, without infringing constitutional fairness, bar the rights of other class members. This conclusion would not be weakened by a judicial determination made at an earlier stage of the case that the plaintiff can fairly represent the class interests. Such a determination may be changed as the action proceeds; it is, therefore, only tentative and must yield to the manifest repudiation by the plaintiff of his class duties.

Is the conclusion different when the class has received advance notice but has failed to avail itself of a genuine opportunity to intervene in the action? To put it differently: Does the notice of a proposed voluntary dismissal put the class members under a duty to intervene, on pain of being bound by a dismissal with prejudice? The answer should probably be in the negative. The class members should not be forced to take over an action initiated, prosecuted, and finally abandoned by a plaintiff who has revealed himself to be disqualified to represent them. They have, in these circumstances, a legitimate interest to litigate in a forum of their choice, to adopt their own strategy, and to be free of any setbacks suffered by the unrepresentative plaintiff. The defendants, to be sure, may claim an interest not to be exposed to multiple actions, but that interest is generally accorded only limited recognition and should not outweigh the right of the class to be unaffected by the acts of a disqualified representative. Thus, on the views here advanced, it makes no difference to the class whether the voluntary dismissal of a class suit is labeled “without prejudice” or “on the merits.” The class is not bound in either case.

As previously mentioned, a dismissal for lack of prosecution, for disobedience to the Rules or to a court order, or for a default of the plaintiff may be sufficiently similar to a voluntary dismissal to call for notice to the court to determine whether the suit may be maintained as a class action. An affirmative determination necessarily includes a finding that the plaintiff will fairly and adequately protect the class interests.

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126 Under Fed. R. Civ. P. 23(e)(1), as amended, the court must determine whether the suit may be maintained as a class action. An affirmative determination necessarily includes a finding that the plaintiff will fairly and adequately protect the class interests.


128 The adequacy of the class representation by the plaintiff is open to collateral attack by other class members against whom the class suit judgment is invoked as res judicata; Hansberry v. Lee, 311 U.S. 32 (1940). For a procedure designed to restrict the possibility of such a collateral attack, see Philadelphia Elec. Co. v. Anaconda Am. Brass Co., 43 F.R.D. 472, 459, 462 (E.D. Pa. 1968).

class in the discretion of the court. Rule 41 (b) provides that a dismissal on one of these grounds "operates as an adjudication upon the merits" unless the court in its order of dismissal otherwise specifies. Does such a dismissal bind the class? Dictum in Saylor v. Lindsley suggests that it does; since the defendants have been put to the inconvenience of preparing their case, the dismissal should relieve them of the burden of defending another similar action. This reasoning may be valid if the second action is brought by the same plaintiff, but it does not meet the question of whether the plaintiff's neglect in prosecuting the suit does not disqualify him as an adequate representative of the class.

The effect of a class plaintiff's neglect or carelessness upon his representative standing has been scarcely explored. Normally, it may be assumed, his lack of care and his oversights in trying or litigating the case on the merits will not prevent an adverse judgment from binding the class. Otherwise the class could reap the fruits of his victory but could easily repudiate the consequences of his defeat, a result neither just nor consonant with the purpose of Rule 23. These considerations, however, carry little weight if a dismissal for lack of prosecution or for similar reasons prevents an actual determination of the merits. In the absence of a contest on the merits, the class does not enjoy the potential of success and should not bear the burden of failure. While we permit the neglect or default of counsel to be held against his client, this is tolerable because the client has selected his counsel. The class plaintiff, by contrast, is a self-appointed representative. To visit his inaction or default upon the class would seem too harsh to satisfy elementary procedural fairness.

Even apart from the restrictions imposed by due process, it is doubtful whether the Rules themselves permit a dismissal for lack of prosecution with prejudice to the class. To say, as does Rule 41 (b), that a dismissal for want of prosecution or similar reasons "operates as an adjudication upon the merits" throws no light on the class effect of the dismissal; for there are dismissals on the merits that do not bind the class. In particular, a dismissal on grounds personal to the class plaintiff—such as his individual laches—is an "adjudication upon the merits," but cannot affect

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140 Text accompanying notes 66-81 supra.
144 Under Fed. R. Civ. P. 23 (d) (2), as amended, the class may be afforded an opportunity to object to the representative standing of the plaintiff; but, as a rule, most of the class members will lack the information necessary to form an intelligent judgment on the subject. Fed. R. Civ. P. 23 (d) (2), moreover, does not apply to derivative actions.
145 There are many other grounds for a dismissal "on the merits" which concern only the class plaintiff individually rather than the class. Thus a stockholder's derivative action may be dismissed "on the merits" because the plaintiff did not exhaust his intra-corporate remedies or because he participated in the wrongful transactions or ratified them. Such a dismissal cannot bar the claim
other class members. The quoted language of Rule 41 (b) is thus inconclusive so far as the class rights are concerned. At common law, a dismissal not actually resting on the merits could not operate with prejudice, even though it was so labeled.\textsuperscript{146} It is arguable that this principle still shields the class from the adverse effects of a dismissal for lack of prosecution or on other grounds not actually going to the merits.

Even a dismissal actually based on the merits may not bind the class if it was rendered without opposition by the plaintiff and without notice to the class. In \textit{Winkelman v. General Motors Corp.},\textsuperscript{147} a New York state court had granted an unopposed defense motion for summary judgment in a stockholder's derivative action. In a companion suit brought by other stockholders in the federal court, the state court judgment was denied res judicata effect. Federal Rule 23 (c) was held to reflect a public policy; the federal court must not be deprived of the right to pass on the merits by what was, in effect, a consent judgment entered without notice to all stockholders. The decision is remarkable not only for its expansive view of the Rule, but also for applying Federal Rule standards to a state judgment rendered under altogether different procedural principles.\textsuperscript{148}

\textbf{Dismissal of Appeal.} While Rule 23 (c) curbs the voluntary dismissal of stockholders' class suits, its wording would not appear to restrain the voluntary dismissal of an appeal taken by the stockholder-plaintiff from an adverse final judgment. The Rule, in terms, governs only the dismissal of "actions" and applies only to proceedings in the district courts. Rule 42 of the new Federal Rules of Appellate Procedure permits the voluntary dismissal of an appeal, by stipulation or on motion, but makes no particular provision for class suit appeals. Any judicial supervision of the dismissal of class suit appeals would, therefore, have to rest on the inherent powers of the courts.

The extent to which such supervision is desirable may be open to debate. Unquestionably, an appeal from an adverse class judgment lends itself to abuses similar to those which Rule 23 (c) was designed to curb; the stockholder-plaintiff may sell out the rights of his class by dismissing his appeal for private pay. Two of the leading cases outlawing the private settlement arose precisely in this fashion. In \textit{Young v. Higbee Co.},\textsuperscript{149} the


\textsuperscript{148} In the latter aspect, the case is comparable to \textit{Ashley v. Keith Oil Corp.}, 73 F. Supp. 37, 51, 54 (D. Mass. 1947), where a stockholder's derivative suit in the Massachusetts state court had been settled with court approval but without notice to the other stockholders, which Massachusetts law did not require. In a subsequent similar action brought by other shareholders in the federal court, the lack of class notice was held to deprive the state judgment of res judicata effect against shareholders who had not known of the earlier proceeding.

\textsuperscript{149} \textit{Fed. R. CIV. P.} 1.

\textsuperscript{150} 324 U.S. 204 (1941).
appellant-stockholders sold their appeal but were held liable for the proceeds. In *Whitten v. Dabney,* the appellate court denied a defense motion to dismiss the appeal because the dismissal was based on a private settlement among the parties.

Nevertheless, it may not be wise to prescribe class notice and court approval at the appeal stage. To begin with, an unsuccessful stockholder-plaintiff need not take an appeal at all. There is no great difference between the failure to take an appeal and the withdrawal of an appeal already taken. More important, the time to appeal is short and notice of appeal is therefore often filed before the prospects of success are fully evaluated. Many a class plaintiff might be deterred from filing a timely appeal if the price of withdrawing it were notice to the class with its substantial expense. Perhaps, also, the grounds for protecting the class rights are less urgent after the trial court has found them to be without merit. Finally, the appellate court may be ill equipped to supervise the class notice and to conduct a hearing on the proposed dismissal, and a remand for that purpose to the trial court would be rather burdensome.

Admittedly, none of these grounds is conclusive, but a compromise solution might be suggested. Before permitting the voluntary dismissal of a class suit appeal by the plaintiff, the court should receive proof by affidavit that neither the plaintiff nor his lawyer has received anything of value for dropping the appeal. Such a requirement would forestall the most serious abuses, would impose no undue burden on the appellate courts, and would preserve the class plaintiff's freedom to prosecute or abandon his appeal according to his best judgment of the merits.

The second part of this Article, dealing with the settlement of stockholders' suits, is scheduled for publication in the May issue of the Journal.

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171 Cal. 621, 154 P. 312 (1915).

138 The use of comparable affidavits, although in a somewhat different context, is prescribed by Del. Ch. Ct. R. 23(e), as amended in 1968. See note 71 supra.