The question, however, of how public problems might possibly be fitted into the category of stockholders' monetary interests for the purpose of bringing a derivative suit is suggested by the instant case and by the leading case of *Dodge v. Ford Motor Company*. There a program of expansion and price reduction for purposes of giving employment to more people, producing more cars, and bringing them within the reach of more people was held to be contrary to the financial advantage of the stockholders, and the company was forced to declare a dividend instead of implementing its program. If, however, stockholders can state a cause of action against directors for pursuing an imprudent and costly anti-labor policy, a cause of action might equally be made out where a corporation pursues a racially discriminatory and costly employment policy, or where it seeks to enforce restrictive covenants at the expense of community good will with consequent loss of revenues, or where it might, for example, require a political or religious test for employment, with the same result. In such instances the stockholders' monetary losses might be considerably more remote than in the case of directors selling goods to their corporation at a large personal profit, but they would be nonetheless real, and perhaps no more remote than in the *Ford* case. Although in the type of cases mentioned the defense under the "business judgment rule" might still prove insurmountable, the decision of the Court of Appeals in the instant case would seem to be encouragement enough for actions of this nature to be attempted. Should experience show that, although such suits were being brought in good faith, their chief value was harassment, and the number of recoveries was negligible, the flood of litigation might very well result in stricter construction of pleadings by the courts or in new legislation restricting the bringing of stockholder suits.

A final factor tending to govern the effect of such possible litigation is the incipient "economic planning" element that is present whenever courts interfere with the business conduct of enterprises. As yet, not even the most enthusiastic votaries of a planned economy have suggested that the courts are the appropriate agency for effectuating it. In view, however, of the extent of economic planning that already necessarily exists in our tightly interwoven social fabric, the courts may become more concerned with adjusting the established rights of individuals where corporate planning is not in the interests of the shareholders.

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**EXTENSION OF FIDUCIARY DUTIES IN SETTLEMENT OF DERIVATIVE SUITS: A FOOTNOTE TO YOUNG V. HIGBEE**

In 1944, the Supreme Court, in *Young v. Higbee Co.*, imposed a fiduciary duty upon two preferred shareholders who had contested a reorganization under the Bankruptcy Act and who had dropped the suit after a private settlement while an appeal was pending from an adverse decision. It was held that

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1 324 U.S. 204 (1945).
the shareholders, who had sold their preferred stock to the junior creditors for over five times its market value in exchange for dismissing their appeal, must account to the other preferred shareholders for the difference between what they had received and the fair value of their stock. This decision was viewed as a possible method of checking the abuses of shareholders' derivative suits,\(^2\) in which the plaintiff's status as a fiduciary for the corporation and other shareholders is well established.\(^3\) It was thought that "strike" suits, instituted in the hope of effecting profitable private settlements, would be discouraged if the strikers were made to disgorge the fruits of their settlements.\(^4\) Moreover, meritorious class claims which, in the past, have been jeopardized through what was, in effect, bribery, might be better protected if the temptation were dissipated by the probability that if the shareholder yielded he would only have to disgorge.

In the district court, to which the case was remanded by the Supreme Court, the stockholder-fiduciaries, however, were allowed to deduct the par value of their stock and a sum for expenses and attorneys' fees from the amount they were to pay to the other preferred shareholders. Upon appeal, the circuit court reduced the deduction to the depressed market value of the stock at the time of the settlement. Nothing was allowed for expenses and attorneys' fees.\(^5\)

In allowing the shareholder-fiduciaries only the market value of their preferred stock at the time of the settlement, instead of using some other basis of valuation, the circuit court strictly applied the "principle that doubts are to be resolved against fiduciaries so as to exclude profits from conduct inconsistent with the interest of their cestui que trust."\(^6\) Limiting the allowance to the low market value, therefore, was meant to penalize those who had breached a fiduciary duty. The threat of such low valuation, if they are ultimately compelled to disgorge, acts as a deterrent to shareholders who would settle corporate


\(^3\)"The stockholder's suit is thus a derivative action, for the plaintiff-stockholder is attempting to enforce a cause of action belonging wholly to another party and does not stand to gain individually by a favorable judgment; he has merely 'derived' the right to sue by virtue of being a stockholder and any recovery accrues to the corporation." McLaughlin, Capacity of Plaintiff-Stockholder to Terminate a Stockholder's Suit, 46 Yale L.J. 421, 423 (1937).


\(^5\)Interest also had to be paid on the sum disgorged. Young v. Potts, 161 F. 2d 597 (C.C.A. 6th, 1947).

\(^6\)Ibid., at 599.

\(^7\)In one sense the rule applied in the instant case is not a penalty, since it would leave the shareholder in the same position as he could have been had he made a bona fide sale of his shares at the time of settlement. It is unlikely, however, that the shareholder would have selected that particular time to sell his shares if it were not for the incentive offered by the settlement.
claims privately. The deterrent effect, however, is limited to those cases in which the "sale of stock" technique is used to effect the private settlement.

The denial of an allowance for expenses and attorneys' fees is also a deterrent and its effect is independent of the form of the settlement. A tangible loss is thus imposed upon all those who settle derivative suits privately and are later forced to account. If attorneys' fees were allowed without court supervision, settlements could conceivably be disguised in that form. If when the settlement is challenged the court were to allow a reasonable amount for attorneys' fees, the shareholder would risk little in the attempted private settlement. By the complete denial of an allowance for attorneys' fees, such shareholders are deprived of the enviable position of having everything to gain and practically nothing to lose.

The effectiveness of the Supreme Court's sanction as clarified by the circuit court depends, of course, upon other shareholders being apprised of private settlements of corporate claims so that derivative suits to account to the corporation may be brought. In the federal courts, Rule 23 of the Federal Rules of Civil Procedure would seem to provide for adequate notice to other stockholders in case of a discontinuance induced by a private settlement. The provisions for court approval and notice, however, have sometimes been construed so as not to extend to private settlements. If such a construction persists, even if the dismissal is without prejudice by the time other shareholders learn of a settlement through their own initiative, the statute of limitations on the original cause of action may well have run. Moreover, in many states no notice at all is required when a shareholder dismisses a derivative action. It is under such circumstances that an action by the other shareholders to account for the gains from a private

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8 It must be conceded that if methods of settlement are used other than a formal contract for the sale of stock or for attorneys' fees, proving the exact amount of the settlement may still be extraordinarily difficult.

9 It may be argued that, since the corporation would have received nothing if not for the initiative of the shareholder who is compelled to disgorge, he should at least recoup expenses and fees.

10 (a) "Representation. If persons constituting a class are so numerous as to make it impracticable to bring them all before the court, such of them, one or more, as will fairly insure the adequate representation of all may, on behalf of all, sue or be sued, when the character of the right sought to be enforced or for against the class is (1) joint, or common, or secondary in the sense that the owner of a primary right refuses to enforce that right and a member of the class thereby becomes entitled to enforce it. . . . (c) Dismissal or Compromise. A class action shall not be dismissed or compromised without the approval of the court. If the right sought to be enforced is one defined in paragraph (1) of subdivision (a) of this rule notice of the proposed dismissal or compromise shall be given to all members of the class in such manner as the court directs. . . ." Federal Rules of Civil Procedure, Rule 23, 48 Stat. 1064 (1934), 28 U.S.C.A. § 723c (1944).

settlement assumes importance as the sole remaining remedy. However, in the absence of a liberal construction of Rule 23, the probability that other shareholders will not hear of private settlements can only be partially offset by making the penalty more severe if they should find out. Although the results in the instant case were the most practical possible at that late stage in the litigation, it would seem that the more urgent need is not for increasing the severity of the penalty if the settlement should come to light, but rather for increasing the probability that it will come to light by extending mandatory notice provisions.

GIFT FOR "BENEFICIAL" MUNICIPAL PURPOSES AS CHARITABLE TRUST

The testatrix, a Colorado resident, left real and personal property situated in Arizona to "trustees for any purpose deemed by them beneficial to the Town of Paonia, Colorado, or the Paonia Schools." A proceeding was brought to determine heirship in connection with the ancillary probate of the will in Arizona. It was held that the trust was unenforceable as a valid charitable trust because there was no restriction limiting use of the trust funds to a charitable purpose, and the plan of execution was not sufficiently clear. In re Hayward's Estate.

Trusts for the benefit of a particular community, and trusts for the benefit

12 Restitution to the corporation or other shareholders of the money from the private settlement raises an interesting collateral question. If the statute of limitations has not run, are the other shareholders nevertheless barred by this action from bringing another derivative suit on the original cause of action? If not, shall the fruits of the settlement be set off against a later judgment in favor of the corporation?

13 The decision of the Supreme Court in the instant case might support the contention that shareholders and their attorneys in derivative actions should also be considered fiduciaries when they act in good faith, and thus should be entitled to fees measured against the total class recovery if they are successful. Such an extension of the fiduciary concept would encourage legitimate derivative suits by those who might otherwise be deterred by the risk of the personal loss of attorneys' fees and costs in the events of failure. It should also be noted that the decision in the instant case does not create any additional penalty for a shareholder who dismisses a derivative suit for a valid reason. He is only deterred from making a private settlement at the expense of the other shareholders.


3 Peirce v. Attorney General, 234 Mass. 389, 125 N.E. 609 (1920) (to trustees "... to be paid ... in the discretion of said trustees to the use and benefit of the Town of Middleborough, in such manner as said trustees or their successors shall determine"); Rotch v. Emerson, 105 Mass. 431 (1870) (agricultural and other philanthropic purposes at trustees' discretion); Corporation of Wrexham v. Tamplin, 28 L.T.N.S. 761 (1873) (for the use and benefit of a town); Nixon v. Brown, 46 Nev. 439, 214 Pac. 524 (1923) (gift of a theater for the use of the inhabitants of a town). There appears to be little doubt that a direct devise to a city even without specifying its use is a valid gift to charity. Dickinson v. City of Anna, 310 Ill. 222, 141 N.E. 754 (1923); Estate of Boyles, 4 T.C. 1092 (1942); In re Smith, [1932] 1 Ch. 153 ("unto my country England—"); Mayor of Faversham v. Ryder, 18 Beav. 318 (1854) (for the benefit and ornament of a town); Rest., Trusts § 373 comm. (c) (1935). For a pertinent categorization of valid charitable purposes, see statement of Lord Macnaghten in Commissioners for Special Purposes of Income Tax v. Pemsel, [1891] A.C. 531, at 583.