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TRANSFER OF INTEREST AFTER PENDENCY – A COMPARATIVE ANALYSIS OF THE SOLUTIONS ADOPTED BY THE AMERICAN AND GERMAN CIVIL PROCEDURE SYSTEMS

MADELEINE TOLANI

I. INTRODUCTION

This paper deals with the problem of the transfer of interest in the context of litigation, which occurs with reasonable frequency in commercial law. The transfer of interest after pendency arises when a litigant assigns his rights or obligations to a third party while the action is pending. This is illustrated by the following short example: A – the owner of some jewelry – brings a suit against B, claiming the restitution of the jewelry, which he lent to B. During the lawsuit, B sells the jewelry to C and tells him about the pending lawsuit, and that A had sold the jewelry to him. However, transfer of interest is not only employed when an individual litigant transfers an asset; it is also relevant in a corporate context when a business organization merges or dissolves *pendente lite*. As a result, another legal entity is created and, thus, becomes the successor.¹

In this example, the question arises how different legal systems treat the problem of transfer of interest. The answers vary and give cause for

1. *Luxliner v. Luxliner*, 13 F.3d 69, 71 (1993); *Froning's Inc. v. Johnston Feed Service, Inc.*, 568 F.2d 108, 110; *DeVilliers v. Atlas Corp.*, 360 F.2d. 292, 297.

shedding more light on the respective rules in a civil law country like Germany, whose procedures are characterized as “inquisitorial,” and a common law country, like the U.S., whose procedure is described as “adversarial.” The procedural rules concerning the transfer of interest play a considerable role in modern civil procedure and interestingly have not been subject to any comparative analysis so far. This article will analyze the different concepts of transfer of interest. It will focus on the various criteria for substitution and its effects. Furthermore, it will discuss the central objectives of the rules and differences in the legal cultures.

II. DIFFERENT MODELS FOR TRANSFER OF INTEREST

Procedural laws offer a number of possible solutions for the problem of transfer of interest after pendency. One example is the prohibition of transfer during the pendency of the action. This was the preferred solution under Roman law, aiming at the protection of the opposing party. Some European countries developed their own legal solutions based on this rule, which vary somewhat. France and the Netherlands, for instance, did not adopt the Roman rule, while some parts of Germany did and kept the prohibition until 1879, when the German Code of Civil Procedure came into force.² The development of trade and the subsequent need to have a flexible system in the modern economy may have been the reasons for this evolution.³ However, this explanation is considered to be too simple, because trade was already increasing in Germany between the sixteen and eighteen hundreds.⁴

In the current German system and in the U.S., the transfer is now allowed,⁵ which means that the asset remains marketable despite the pendency of the litigation. This solution seems reasonable, because it would be unfair for the owner to lose the right to sell his asset solely because he is in litigation and has to defend his right, which often happens involuntarily.

In the above-mentioned example, B could sell the asset and give it to C even though the litigation is pending against B. The logical consequence

2. Kohler, *Funktionales Recht – Zum Wandel im Rechtsdenken*, dargestellt an einem zivilprozessualen Beispiel, in: *AcP* 192 (1992), at 255, 258 (Ger.).

3. Mandrioli, *Direitto Processuale Civile*, 3, Torino, 2007 at 406. (It.).

4. *See supra* note 2. Another interesting fact is the existence of the prohibition of transfer as a consequence of the pendency of a proceeding in some cantons in Switzerland. However, without any sanction, the transfer is not void. O. Vogel, *Grundriß des Zivilprozessrechts*, 5th edition (1997), chapter 5 mn 107 at 151, i.V.m. chapter 8 mn 54 at 214. (Ger.).

5. The transfer after pendency is also allowed in Italy under Article 111 of the Italian Code of Civil Procedure (ICCP) and in Japan under Article 50 of the Code of Civil Procedure.

would be that B is substituted and the real holder of the asset, C, takes over B's position. Another option is that the successor would have the right to intervene. Finally, another possibility is the continuance of the trial between the original parties, A and B. Under this last solution, the procedural situation would not be affected by the transfer.

However, there are different rules governing transfer of interest, which can be found in § 265 of the German Code of Civil Procedure (ZPO) and Federal Rule of Civil Procedure (F.R.C.P.) 25 (c) in the U.S.

III. FAIRNESS AND EFFICIENCY AS CRITERA OF THE ANALYSIS

The primary purpose of institutions of civil justice in modern political economies is the fair, accurate, and efficient vindication of private rights and interests.⁶ Thus, the above-mentioned rules of civil procedure concerning the transfer of interest will be analyzed according to the following criteria of fairness and efficiency.

A. FAIRNESS

A procedural mechanism can be considered fair if it takes care of the interests of the different parties. The principle of fairness contains the following different aspects: (1) fair notice and fair warning; (2) a hearing before an impartial judge; (3) rationality of the proceeding; and (4) fair play.⁷ Fairness is a fundamental feature of a proceeding in a State embodying the rule of law (constitutional State) and is derived from the constitutions of both Germany and the U.S.

In Germany, the Supreme Federal Constitutional Court (Bundesverfassungsgericht) has been vigilant in applying constitutional norms to civil litigation. The Court interprets the general clauses of the Constitution (Grundgesetz), Article 2, which guarantees citizens the maximum scope of personal freedom consistent with an ordered society, and Article 3, which guarantees that all persons are equal before the law (Alle Menschen sind vor dem Gesetz gleich),⁸ as requiring a "fair proceeding" in both criminal and civil litigation.

6. For comparison, see Peter L. Murray & Rolf Stürner, *German Civil Justice* 575 (2004).

7. Simona Grossi, *A Comparative Analysis Between Italian Civil Proceedings and American Civil Proceedings Before Federal Courts*, 20 *Ind. Int'l & Comp. L. Rev.* 213 (2010).

8. See *supra* note 6, at 5; This has been interpreted to require that the parties have equal chances (Waffengleichheit) in civil litigation. Musielak, ZPO, 9th edition (2012) introduction, mn 29-30. (Ger.).

Fair play is also embodied in the Due Process and the Equal Protection Clauses of the U.S. Constitution. These clauses guarantee the fairness of a proceeding. The Fifth and the Fourteenth Amendments prohibit governmental actions that would deprive “any person of life, liberty or property without due process.” One part of the Due Process Clause restricts the legislature, while the other part has a procedural aspect that guarantees a certain process if a person is deprived of life, liberty or property. In *Hardy v. Johns-Manville Sales Corp.*, the Court held that the right to a full and fair opportunity to litigate is a right protected by the Due Process Clause.⁹

B. EFFICIENCY

Another term of comparison is efficiency. Efficiency is defined as the least time and cost consuming.¹⁰ “A lengthy and expensive device will not be efficient and the legal system should try, as much as it can, to adopt efficient solutions.”¹¹ However, efficiency cannot be isolated from the principle of fairness; there is a correlation between fairness and efficiency because a device that is very time and cost consuming cannot be evaluated as being fair.¹² Thus, the reasonable duration of a trial is an element of a fair proceeding.

IV. ANALYSIS OF THE RESPECTIVE RULES

A. THE GERMAN RULES

The German rule § 265 ZPO (Code of Civil Procedure) provides the following concerning a transfer of a moveable property or right:

(1) Pendency shall not exclude the right of either party to transfer the property subject to the litigation or to assign the claim asserted. (2) Such transfer or assignment shall have no effect on the proceeding. The successor shall not be entitled, without the consent of the opponent, to enter the proceeding as the position of his or her predecessor as the party or to intervene. In the event that the successor joins the proceeding § 69 shall not be applicable. (3) In the event that the plaintiff made the transfer or assignment, then to the extent that, pursuant to § 325, the judgment would not be effective against the successor, the

9. *Hardy v. Johns-Manville Sales Corp.*, 681 F.2d 334, 338 (1982).

10. *See supra* note 7.

11. *Id.*

12. *Id.*, “Efficiency and fairness are interrelated concepts.”

objection may be raised by him or her that he or she is no longer entitled to assert the claim.¹³

This basic principle means that after a transfer of interest occurs, the same proceeding is continued among the original parties. Three requirements must be fulfilled in order to continue the trial between the original parties: (1) the transfer is about a property under litigation or about a claim asserted; (2) the legal succession occurs after pendency; (3) the transferee does not qualify as a good faith transferee without notice under § 325 and would be bound by the judgment rendered between the original parties.

If the court has no knowledge of the transfer, the judgment will be rendered against or in favor of the transferor based on the substantive law before the transfer.¹⁴ Thus, in the example above, the trial would be continued between A and B even if A is no longer the owner of the asset under the substantive law.

If the same proceeding is continued between the original parties, a claim by the successor will be precluded as a consequence of the pendency of the suit with the same subject matter, § 261 III number 1 ZPO.¹⁵ The position of the transferor is not limited. He can also accept the claim, renounce, or even settle.¹⁶

The situation is problematic when the court has knowledge of the transfer. The question arises if the decision should be based on the situation before the transfer, or if the court should consider the transfer somehow. One way to read § 265 ZPO (“... shall have no effect on the proceeding”) would be that the transfer should not affect the court’s decision at all; it should be irrelevant (“Irrelevanztheorie”). Another interpretation could be that § 265 ZPO (“... shall have no effect on the proceeding”) only concerns the formal positions of the parties in the proceeding, which should remain the same. That would mean that the transfer is relevant for the decision, because under substantive law, the proceeding is about someone else’s asset, namely the transferee’s (“Relevanztheorie”). The divergence of the party in the proceeding and

13. N. Stephan Kinsella & Paul E. Cormeaux, *Digest of Commercial Laws of the World*, Binder 7 (Oceana ed. 2000).

14. However, it will usually also be applicable to the transferee under § 325 ZPO and enforceable under § 727 ZPO. This will be discussed later in this article under sections III. 1. c) cc) and III. 1. d).

15. Becker-Eberhard, in: *Münchener Kommentar Zivilprozessordnung: ZPO*, 4th ed. (2013) § 265 mn 69. (Ger.).

16. Foerste, in: *Musielak Kommentar ZPO*, 9th ed. (2012) § 265 mn. 9. (Ger.).

the owner of a right under substantive law can be practiced with the special mechanism “Prozessstandschaft,” which means that someone that is not the owner of a right is a party at trial.¹⁷ One practical consequence of the “theory of relevance” is the following: if the plaintiff transfers the subject of the litigation to a third person, the defendant can only raise such defenses that he has against the successor. Furthermore, the plaintiff has to change his claim because the defendant has to pay or give the asset to the transferee.¹⁸ This theory is prevailing and accepted by the courts¹⁹ in situations of the transfer by the plaintiff, but if the transfer occurs on the side of the defendant, the transfer will be irrelevant. The plaintiff cannot change the complaint and ask for the decision to be rendered against the successor who had never participated in the proceeding. The court will not consider the transfer in its decision.²⁰

1. Criteria for the substitution under § 265 II ZPO

Under § 265 II ZPO, the transferor can be substituted when the opposing party consents. Furthermore, although the law does not state it expressly, the transferor is also required to consent. This requirement is based on the unwritten German principle that nobody should be deprived of the position he has in a proceeding without his own participation.²¹ Due to this principle, the consent of the opposing party and of the transferor cannot be substituted by a court order based on possible advantages of the procedure. Therefore, the power to substitute lies in the hands of the parties.

If the transferor refuses to consent, the successor can intervene in the form of a principal intervention (“Hauptintervention” § 64 ZPO), § 265 II sentence 2 ZPO. If the opposing party refuses to consent, the successor cannot participate at the proceeding as a party and also cannot intervene. He can only support the position of the transferor in the form of the

17. “Prozessstandschaft” can be based on law (“gesetzliche Prozessstandschaft”), like in the transfer of interest, or can be based on a contract (“gewillkürte Prozessstandschaft”), for which special requirements exist.

18. Bürgerliches Gesetzbuch [BGH] [NJW] 2004, 2152 (2154) (Ger.); Bürgerliches Gesetzbuch [BGH] NJW 1986, 3206 (3207); Becker-Eberhard, in: Münchener Kommentar ZPO, 4th ed. (2013) mn 83; Foerste, in: Musielak Kommentar ZPO, 9th ed. (2012) mn. 10 (Ger.); Grunsky, Die Veräußerung der streitbefangenen Sache (1968) at 101 ff. (Ger.).

19. Since RGZ 56, 301 (Ger.); Bürgerliches Gesetzbuch [BGHZ] 26, 31 (37) (Ger.); NJW-RR 1986, 1182. (Ger.).

20. But the decision can be enforced against the transferee after the title is modified under § 727 ZPO.

21. Becker-Eberhard, in: Münchener Kommentar ZPO, 4th ed. (2012) § 265 mn. 5. (Ger.).

auxiliary intervention (“Streitgehilfe”) pursuant to § 67 ZPO.²² Some scholars criticize this restriction as a violation of the constitutional right to be heard, Article 103 GG.²³ Even if an auxiliary intervention should not be seen as a sufficient tool for the transferee, it would go too far to qualify it as a violation of the right to be heard.²⁴ In this context, the right of the transferee to be heard has to be balanced with the protection of the opposing party. If the opposing party refuses to consent, the transferee’s right to be heard is overruled.²⁵

Overall, the criteria for a substitution – consent of the parties – are very clear and foreseeable. Thus, the German concept can be characterized as fair.

2. The Rationale Behind § 265 ZPO

The rationale behind the German Rule is to avoid a duplicative trial about the same subject matter. This can be done either by the transferee taking over the proceeding or by continuing the proceeding with the original parties. The Germans have adopted the latter.

There are two main advantages to the German concept. The first one is an advantage for the opposing party, because he does not need to adjust to a new person. The Federal Supreme Court (“Bundesgerichtshof”) emphasizes that the opposing party should not be deprived of the achievements, for instance the result of evidentiary proceedings that have been reached so far during the proceeding.²⁶ The second advantage is that continuing the proceeding between the same parties avoids delays and interruptions that a substitution of parties causes.²⁷

The first aspect of the protection of the opposing party seems to be fair. The second aspect of avoiding delays means the proceeding is less time consuming than the substitution. Therefore, the proceeding is economical and complies with the basic German principle of civil procedure favoring concentration of proceedings (“Konzentrationsmaxime”). Thus, the

22. Auxiliary intervention means, that someone intervenes to support the position of a party whose victory or defeat will legally affect the interest of the intervener. Compare for intervention in general: Murray & Stürner, *German Civil Justice* at 206 ff (2004). (Ger.).

23. Pawlowski, *Probleme des rechtlichen Gehörs bei der Veräußerung einer Streitsache. - Zur Auslegung der §§ 265, 325 ZPO*, in: *JZ* 1975 at 681 ff. (682). (Ger.).

24. Becker-Eberhard, in: *Münchener Kommentar ZPO*, 4th ed. (2013) mn 70. (Ger.).

25. Schwartz, *Gewährung und Gewährleistung des rechtlichen Gehörs durch einzelne Vorschriften der Zivilprozessordnung* at 78 (1977). (Ger.).

26. *Bürgerliches Gesetzbuch [BGH]*, NJW 1998, 156 following (158). (Ger.).

27. Becker-Eberhard, in: *Münchener Kommentar ZPO*, 4th ed. (2013) mn 3. (Ger.).

Federal Supreme Court concludes that the proceeding should be shielded by § 265 II ZPO from changes under substantive law.²⁸

3. The Binding Effect of the Judgment and its Limitations

This next section discusses the binding effect of the judgment and its limitations, as it is important to the comprehensiveness of this paper.

(a) The Rationale of the Inter-partes-doctrine

The general rule is that the judgment entered, adverse or favorable, is only applicable inter partes. Rule § 325 I ZPO defines the subjective scope of the res judicata effect of a judgment (and has to be read jointly with § 265 ZPO).

The inter-partes-doctrine is based on two fundamental principles: Firstly, the principle that the litigation is under the control of the parties (dispositive principle, Dispositionsmaxime). This principle finds support in Article 2 of the Constitution, which guarantees citizens the maximum scope of personal freedom consistent with an ordered society.²⁹ It is a fundamental principle that the control of the initiation, termination, and scope of a civil law suit lies in the hands of the parties.³⁰ Secondly, the doctrine is based on the principle of party control of facts and the means of proof (Verhandlungsmaxime).³¹ Only the parties may participate in the litigation, whereas non-parties do not have influence and thus, usually cannot be bound by a judgment.³²

(b) The Extension of the Res Judicata to Nonparties

A judgment in successor in interest cases is an exception to the inter-partes-principle. The judgment can have effect upon the successor in interest with respect to the subject matter of the claims actually asserted and decided.³³ This is the necessary consequence under § 325 I ZPO, which defines the subjective scopes of the res judicata as the following:

- (1) The final judgment shall be effective for and against the parties and the persons who became legal successors of the

28. BGH WM 1992, 1451, 1452. (Ger.).

29. Murray & Stürner, German Civil Justice 575 at 154 (2004).

30. *Id.* at 155.

31. Each party bears the responsibility to describe to the court the factual proof for each contested factual allegation and to identify the source of that proof. Compare Kinsella & Cormeaux, *Digest of Commercial Laws of the World*, Binder 7 at 158.

32. Gottwald, in: Münchener Kommentar ZPO, 4th ed. (2013) § 325 mn. 1. (Ger.).

33. See *supra* note 6, at 357, 359.

parties after the occurrence of pendency of the action or acquired possession of property involved in the litigation in such a manner that one of the parties or his or her legal successor became the indirect possessor. (2) The provisions of the civil law for the benefit of those who derive rights from an unauthorized person shall be applicable analogously.³⁴

Without this binding effect upon the successor, the continuance of the trial against the original party would be unacceptable for the adverse party. The extension of the *res judicata* to a successor *pendente lite* is characterized as a “natural and necessary supplement” to § 265 ZPO.³⁵

(c) Limitation of the Binding Effect to Third Persons

The judgment is not binding on the third person – the successor – if he has good faith. The good faith refers to the pendency of the trial and to the entitlement of the transferor to transfer the asset under substantive law (“double bona fide”), § 325 II ZPO. In the situation of good faith, the transferor is not entitled to continue the litigation. Section 265 (3) provides,

in the event that the plaintiff made the transfer or assignment, then to the extent that, pursuant to § 325, the judgment would not be effective against the successor, the objection may be raised by him or her that he or she is no longer entitled to assert the claim.³⁶

However, such an exception to the basic principle of the continuance of the litigation between the original parties does not exist in the example described in the introduction, because A has good faith concerning the ownership of B, but does not have good faith concerning the pendency of the trial.

4. Enforceability of the Judgment Against the Transferee

Another question is how a judgment rendered between the original parties can be enforced later against the transferee. According to rule § 727 ZPO, a modification of the name in the title is the applicable mechanism if the change of substantive law had not been introduced in

34. See *supra* note 13.

35. Karl August Bettermann, *Die Vollstreckung des Zivilurteils in den Grenzen seiner Rechtskraft* (1948) at 67 (Ger.); Arwed Blomeyer, *Zivilprozessrecht: Erkenntnisverfahren*, 2nd ed. (1985) § 92 III 1 a, at 513. (Ger.).

36. See *supra* note 13.

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the trial. The rule orders, “an enforceable copy may be granted to the legal successor of the creditor named in the judgment as well as against the legal successor of the debtor named in the judgment....”³⁷

5. Application of § 265 ZPO

Section 265 ZPO is applicable for rights and moveable property. The transfer of immobles is governed by a special rule: § 266 ZPO.

One problem is the distinction between the transfer of interest and special rules applicable to the change of a party. The following rules aim at other post filing events: the death of a party (§ 239 ZPO); the event of insolvency proceedings with respect to the assets of one party (§ 240 ZPO); or the situation when one party loses his or her capacity to conduct litigation or when a statutory representative of a party dies (§ 241 ZPO). The distinction between those rules located in the first book, third chapter, and fifth title of the code of civil procedure (Interruptions and Stay of Proceedings) and rule § 265 located in the second book, first chapter, first title (Procedure Until the Judgment), can be summarized as the following: § 265 ZPO is only applicable if the original party is still viable and if the judgment is binding upon the new owner of the asset.³⁸ If there is doubt, the fundamental criteria for the distinction between those special rules and the transfer of interest is the protection of the opposing party. If the opposing party needs to be protected, rule § 265 ZPO will always apply. If it is only necessary to avoid a redundant second trial, the aforementioned special rule will have to be applied.³⁹

An important note in the modern era is that a merger – a fusion of two companies without any liquidation – is not considered a transfer of interest under German law. This is different from the American broad understanding of transfer of interest, where transfer of interest in a corporate context occurs when one corporation becomes another by merger.⁴⁰ Unlike American law, the transferred company under German law is treated like the death of a party and the special rules concerning a

37. Section 727 ZPO: (1) “An enforceable copy may be granted to the legal successor of the creditor named in the judgment as well as against the legal successor of the debtor named in the judgment, and the possessor of the property involved in the dispute, against whom the judgment is effective pursuant to § 325, to the extent that the successor or possessor relations is manifest to the court or is proved by public or notarized form. (2) In the event that the legal succession or the possessory relation is manifest to the court, such shall be shown in the execution order.” Kinsella & Cormeaux, *Digest of Commercial Laws of the World*, Binder 7.

38. Schumann, in: Stein/Jonas, *Kommentar ZPO*, 21st ed. (1996), § 265 mn 19. (Ger.).

39. Becker-Eberhard, in: *Münchener Kommentar ZPO*, 4th ed. (2013) § 265 mn 7. (Ger.).

40. *Luxliner P.L. Export, Co. v. RDI/Luxliner, Inc.*, 13 F.3d 69, 72 (1993); *Froning's, Inc. v. Johnston Feed Service, Inc.*, 568 F.2d 108, 110 (1978).

change of party are applicable.⁴¹ Consequently, the proceeding will be suspended until the acceptance thereof by the successors (§ 239 ZPO).⁴²

B. THE AMERICAN RULES UNDER FEDERAL LAW

One of the consequences of the dual-sovereignty system in the United States is that in every state there are two separate court systems: the federal and the state courts. The U.S. civil procedure system is divided into a federal court system and a state court system. As a consequence of this separation, there are federal and state rules of civil procedure. This article analyzes the transfer of interest under the Federal Rules of Civil Procedure (F.R.C.P.).

F.R.C.P. Rule 25 (c) provides, “In the case of a transfer of interest, the action may be continued by or against the original party, unless the court upon motions directs the person to whom the interest is transferred to be substituted in the action or joined with the original party.” Rule 25 not only governs the transfer of interest, but also the post filing for events like (a) death, (b) incapacity of a party, and (d) the substitution of a public officer that died, resigned or otherwise ceased to hold the office. Thus, Rule 25 with its broad title “Substitution” is more complex systematically than its German counterpart, which has separate rules for the transfer of interest (§ 265 ZPO) and other post filing events (§ 239 ZPO and the following rules).

The continuance between the original parties under Rule 25 (c) is the obvious similarity to the German law. The absence of substitution does not have any consequence; the pending action will be continued. Going back to the example in the introduction, the action would be continued between A and B. Nothing has to be done after an interest has been transferred. This is the most significant feature of Rule 25 (c).⁴³ If the transferor stays in the litigation, without having an interest in the subject matter litigated, he is called a “nominal party.”

The exception from the continuance between the original parties is based on an order from the court, which – not *sua sponte*, but on motion of one party – can order the transferee to be substituted. Therefore, the decision

41. Becker-Eberhard, in: *Münchener Kommentar ZPO*, 4th ed. (2013) § 265 mn 44. (Ger.).

42. In contrast, the sale of a business pursuant to Rule 25 HGB (German Commercial Code) § 265 ZPO is applicable with the consequence that the original owner remains as the party if a trial is pending. Becker-Eberhard, in: *Münchener Kommentar ZPO*, 4th edition (2013) mn 43.

43. *Otis Clapp & Son, Inc. v. Filmore Vitamin Co.*, 754 F.2d 738, 743 (1985).

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regarding substitution is ultimately left to the court, which has the discretion to allow or refuse substitution. The rule is wholly permissive.⁴⁴

1. Objective of Rule 25 (c)

The central objective of Rule 25 (c) is – corresponding to the other portions of Rule 25 – to allow the continued and efficient resolution of an existing action despite post-filing events.⁴⁵ The purpose of the rule is to allow the action to continue unabated when a transfer of interest occurs, rather than requiring the initiation of an entirely new lawsuit.⁴⁶ Case law has held that Rule 25 (c) is a valid procedural rule that is necessary for the efficient functioning of the federal courts.⁴⁷ Like Rule 25 (a), Rule 25 (c) permits the court to continue to hear a case where the action survives, but the original party has transferred interest in the litigation to another. “Rather than require the assignee to initiate a new action, the rule enables the court to continue the action with the assignee joined with or in the place of the original party.”⁴⁸ An initiation of a new action would be a needless repetition of effort and expense, which is prevented by the Rule.⁴⁹ Therefore, the rationale behind the Rule is efficiency and should be kept in mind while finding the criteria for substitution or joinder.

2. Criteria for Substitution: The Court’s Discretion

The discretion that Rule 25 gives the court to order substitution or not, raises the question for the criteria of substitution. Substitution under the Rule is not mandatory. Considering the rationale of the Rule – unabated continuance of the pending trial to avoid starting a new action on the same issue – it would be more logical to allow substitution only rarely.⁵⁰

44. Edward I. Niles, *Federal Civil Procedure*, § 8.440 (2d ed. 1984).

45. Shaun P. Martin, *Substitution*, 73 Tenn. L. Rev. 545 (2006).

46. *ELCA Enterprises, Inc. v. Sisco Equip. Rental & Sales, Inc.*, 53 F.3d 186, 191 (1995); *General Battery Corp. v. Globe-Union, Inc.*, 100 F.R.D. 258, 261 (1982).

47. *General Battery Corp.*, 100 F.R.D. at 262.

48. *Id.* at 262-63.

49. *Id.* (comparing Fed. R. Civ. P. 25(a) and 25(c)).

50. In contrast, commentary literature concerning the Cal. Civ. Proc. Code § 368.5 says that in most cases substitution is “so obviously desirable that it should be ordered as a matter of right if requested by the transferor or the transferee.” Furthermore, in the event of the transfer of interest during the continuation of the litigation, “it follows that a substitution of parties should be made.” Witkin, *California Procedure*, 5th ed., Volume 4 (2008) § 264, 341. Section 368.5 of the California Code of Civil Procedure says the following: “An action or proceeding does not abate by the transfer of interest in the action or proceeding or by any other transfer of an interest. The action or proceeding may be continued in the name of the original party, or the court may allow the person to whom the transfer is made to be substituted in the action or proceeding.” The language “may allow” suggests a discretion, which makes the rule very similar to F.R.C.P. 25(c). Witkin, *California Procedure*, 5th ed. Volume 4 (2008) § 264, 339.

Case law indicates that Rule 25 (c) does not state what factors should guide the court in determining whether to allow the original party to continue, or to order the substitution or joinder of the transferee.⁵¹ Although the criteria are not mentioned expressly in Rule 25 (c), the provision is viewed as an unproblematic rule and thus, has not attracted academic interest so far.⁵²

Likewise, the Rule has not been the subject of a substantial discussion by courts or commentators.⁵³ In *Luxliner P.L. Export, Co. v. RDI/Luxliner, Inc.*, the 3rd Circuit held that “Rule 25 (c) does not specify a method for deciding or a standard to use in determining whether motions can be decided on the papers. This gap in Rule 25 (c) most likely stems from the fact that the rule does not easily lend itself to contested motions practice.”⁵⁴ Therefore, Rule 25 (c) is only applicable where an interest is changing hands during the trial. If the interest were transferred prior to the commencement of the suit, Rule 17 (a) would control.⁵⁵

(a) Criteria According to Which Courts Exercise Their Discretions Under F. R.C.P. 25 (c)

Rule 25 (c) requires a motion for substitution to be made and served with certain formalities. This requirement was expressly stated by the court in *Froning’s Inc. v. Johnston Feed Service, Inc.*, in which one corporation was dissolved and the opponent did not move pursuant to Rule 25 (c). The United States Court of Appeals for the 8th Circuit held that in absence of the motion, it is no error to continue the action in the name of the original parties.⁵⁶ The service of the motion should be made as provided under Rule 25 (a), but there is no limit for making the motion. According to Rule 25 (a), the motion to substitute must be served as provided in Rule 5 or for a nonparty in Rule 4.

The substitution is entirely a question of convenience. This is comparable to Rule 15 (d), concerning the supplement of the complaint. On one hand, the court may find it more convenient to allow the original party to continue the action alone and that the transferee is not participating as a party. On the other hand, the court may order the transferee substituted instead of the original party or the court may order

51. *General Battery Corp.*, 100 F.R.D. at 261.

52. Compare Martin, *Substitution*, 73 Tenn. L. Rev. 545 (2006).

53. *General Battery Corp.*, 100 F.R.D. at 261.

54. *Luxliner P.L. Export, Co.*, 13 F. 3d at 69.

55. *Myrtle E. Hildebrands and Guam Maintenance Inc. v. Far East Trading Company, Inc.*, 509 F.2d 1321, 1323 (1975).

56. *Froning’s, Inc.*, 568 F.2d at 108.

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that the transferee be joined as an additional party to the action.⁵⁷ The motion for substitution will be granted if the court believes the transferee's presence would facilitate the conduct of the litigation.⁵⁸ It can even be granted on the condition that there be no delay to trial.⁵⁹

However, it will be denied if the replacement of the original party by successor would raise new issues, would require new and further discovery, and postpone the pending trial.⁶⁰ These are identical criteria to the criteria of Rule 15 (d).⁶¹ According to the court, there was no abuse of discretion in denying a motion for substitution when the participation would be highly disruptive to the administration of the litigation.⁶²

Another guiding factor in favor of joinder should be the question whether the efforts of the court and the parties up until the present time would be for naught.⁶³ The described considerations seem to meet the previously explained requirement of efficiency.

In the unusual circumstance that the proposed successor's interest would be in conflict with those of the transferor, the transferor should be allowed to prosecute the right in his or her own name. The transferor should not be substituted, but could be joined. This was decided for the special situation where the same insurer who already had paid the compensation to the plaintiff represented the plaintiff and also the defendant.⁶⁴

The obvious limitation of the court's discretion is the refusal of substitution and a refusal of continuance. This complete refusal essentially punishes the party that moved under Rule 25 (c) and is an abuse of the court's discretion.⁶⁵ In *ELCA Enterprises, Inc. v. Sisco Equipment Rental & Sales, Inc.*, the district court denied plaintiff's Rule 25 (c) motion for substitution and also did not allow the plaintiff to continue. However, the court granted the defendant's motion for summary judgment pursuant to Rule 56 (c). In this case, the question of Rule 25 (c) arose because, during litigation, plaintiff ELCA transferred

57. Daniel R. Coquillette, et al., *Moore's Federal Practice*, Vol. 3B, 25.08 (2nd ed. 1955).

58. *Luxliner P.L. Export, Co.*, 13 F. 3d at 69.

59. *Fontana v. United Bonding Insurance Company v. Rockwood Insurance Company*, 468 F.2d 168, 169 (1972).

60. *Otis Clapp & Son, Inc.*, 754 F.2d at 738.

61. *Id.* at 743.

62. *National Indep. Theatre Exhibitors, Inc. v. Buena Vista Distrib. Co.*, 748 F.2d 602 (1984/1985).

63. *General Battery Corp.*, 100 F.R.D. at 263.

64. *Myrtle E. Hildebrands and Guam Maintenance Inc.*, 509 F.2d at 1323.

65. *Elca Enterprises, Inc.*, 53 F.3d at 191.

all of its interest to another company, ELCA Properties. The District Court based its decision on an analysis of the original plaintiff's claims against the defendant and held that a "viable action was a necessary precursor to a substitution of parties,"⁶⁶ which, according to the court's opinion, did not exist in this case. Thus, the District Court determined that Rule 25 (c) only applies if the original plaintiff retains a cause of action against the defendant after the transfer of interest. This would be a question of substantive law.

In a decision of the 8th Circuit Court of Appeals, it was decided that Rule 25 (c) does not substantively determine what actions survive the transfer of an interest; rather, it provides substitution procedures for an action that does survive. The rule expressly permits parties to continue in an action, even if they do not remain the real party in interest, as long as the cause of action itself survives the transfer to the new party.⁶⁷

In that case, the defendant argued granting the substitution would permit ELCA to mount a new case; the court held that "the nature of the action remains the same regardless of the plaintiff's name." The transferee, as the new owner, would seek the same relief and assumes an identical position to the transferor in the lawsuit.⁶⁸ On the other hand, the case *Covington Grain Co., Inc. v. Deal* concerns a different situation: the initial party had a tort claim, whereas the proposed substituted party had contract-related claims. Here, the District Court's refusal to allow substitution was not an abuse of discretion.⁶⁹

Considering both cases, *ELCA Enterprises, Inc. v. Sisco Equipment Rental & Sales, Inc.* and *Covington Grain Co., Inc. v. Deal*, the unwritten restrictive requirement of Rule 25 (c) can be stated as: substitution can only be permitted if the action survived and its nature remains the same. The positions of the transferor and of the transferee have to be identical.⁷⁰ The United States District Court in Delaware also considered that the transferee, who would continue a counterclaim in his position as a defendant, would not be asserting new claims against the opponent. Furthermore, the court considered that the opponent will not be prejudiced in any way by the proposed joinder of the transferee to the

66. *Id.* at 188.

67. *Id.* at 191.

68. *Id.*

69. *Covington Grain Co., Inc. v. Deal*, 638 F.2d 1357, 1361 (1981).

70. *General Battery Corp.*, 100 F.R.D. at 263.

proceeding and that the transferee would occupy the same relative position in the continued action as the transferor.⁷¹

Applying this criteria, abuse of Rule 25 (c) will be avoided. It is in the interest of the opposing party that he is not confronted with another action after the substitution during the litigation. This meets the requirements of fairness with respect to the opposing party, but secures the efficiency of the trial as well, because a change of the nature of the action could make new evidence necessary and thus, would consume more time and costs.

However, fairness shall not only be secured with respect to the adverse party. The question of fairness should especially be considered with respect to the party seeking to be substituted. Under Rule 25 (c), any party can move for substitution. In the situation that the opposing party or the original party wishes that a third person may get involved in the trial, the question arises how it could be fair that this third person becomes a party.

(b) Transfer of Interest According to the State Rules

To understand the position of the American law and to find criteria and a concept for the transfer of interest after pendency, one must consider state court decisions as well as federal. Transfer of interest usually arises by a contract situation, which is state law. Federal courts have "limited" jurisdiction, which means they can only decide certain types of cases ("enumerated powers"). They are concerned with cases arising under federal law. If federal law is not involved, federal courts have jurisdiction pursuant 28 U.S.C. § 1332 (a) under the following circumstances: when the case involves diversity of citizenship (citizens of different states or citizens of a state and citizens or subjects of a foreign state), or if the jurisdictional amount exceeds \$75,000 exclusive of interests and costs (diversity jurisdiction). Since contract law is state law, a federal court in a situation of a transfer of interest can only have jurisdiction under Rule 28 U.S.C. § 1332 (a).

Another reason for considering state cases in this analysis is that Rule 25 (c) is a combination and an adaption of N.Y.C.P.A. (1937) § 83⁷² and

71. *Id.* at 263-64.

72. New York Civil Practice Act, formerly Code Civ. Pro. § 756. Section 756 provided that, in case of any transfer of interest, other than by death, marriage, or other disability of a party, "the action shall be continued in the name of the original party; or the court may allow the person to whom the transfer is made to be substituted in the action."

Cal. Civ. Proc. Code (1937) § 368.5.⁷³ The text of Section 368.5 of the Cal. Civ. Proc. Code, which the mentioned judgment is based on,⁷⁴ is very similar to Rule 25 (c). Section 368.5 of the Cal. Civ. Proc. Code provides, “The action or proceeding may be continued in the name of the original party, or the court may allow the person to whom the transfer is made to be substituted in the action or proceeding.” The language “may allow” suggests the court may use discretion.⁷⁵ The text of N.Y.C.P.A. § 83 is also very similar to F.R.C.P. 25 (c). This rule provides, “Upon any transfer of interest, the action may be continued by or against the original parties unless the court directs the person to whom the interest is transferred to be substituted or joined to the action.”

Due to this obvious similarity, the interpretation and the criteria of Cal. Civ. Proc. Code § 368.5 and N.Y.C.P.A. § 83 cannot differ essentially from F.R.C.P. 25 (c). Also, it should be noted that due process addresses both the Federal (5th Amendment) and the States (14th Amendment), and so the requirements should be identical for each.

In *Higgins v. Kay*, the Supreme Court of California decided that “in any proceeding of judicial character, one whose rights or interests may be affected by action against him therein is entitled to notice and an opportunity to be heard,⁷⁶ and that a failure to accord him that right amounts to lack of due process of law.”⁷⁷ In this case, due to the defendant’s motion for substitution under Code Civ. Proc. § 368.5, the plaintiff was substituted without any notice to the party sought to be substituted. The Supreme Court of California held that the order of substitution without notice of the proposed party was void.⁷⁸ In the decision *Tuffree v. Stearns Ranchos Co.*, it was indicated that the court has discretion to order substitution against the wishes of the transferee.⁷⁹

73. Werner R. Ilsen & Charles E. Clark, Federal Rules of Civil Procedure, Rule 25 Note to Subdivisions (b) and (c) (1944 rev. ed.).

74. The applicable rule now concerning transfer of interest is Cal. Civ. Proc. Code § 368.5: “An action or proceeding does not abate by the transfer of an interest in the action or proceeding or by any other transfer of interest. The action or proceeding may be continued in the name of the original party, or the court may allow the person to whom the transfer is made to be substituted in the action or proceeding.”

75. Witkin, California Procedure, Volume 4 § 264, 339 (5th ed. 2008).

76. This concept is an expression of the due process clause. See *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306 (1950) (emphasis added).

77. *Higgins v. Kay*, 168 Cal. 468, 471-72 (1914).

78. *Id.* 471, 473.

79. *Tuffree v. Stearns Ranchos Co.*, 124 C. 306 (1899); B. E. Witkin, California Procedure, Volume 4, § 262, 339 (5th ed. 2008).

In the case of *White v. Hardy*,⁸⁰ which construed N.Y.C.P.A. § 83, the Supreme Court in New York County stated that where the assignment is absolute, leaving no interest in the transferor, a motion for substitution should be granted. However, when the assignment is not absolute – or where the transferor, notwithstanding the transfer, still has some interest in the cause of action – the motion for substitution should be denied, especially when the transferee opposes the motion.⁸¹

According to C.C.P. § 756, the case was decided where the defendant applied for a substitution, but the original plaintiff and the person sought to be substituted or joined as a plaintiff opposed.⁸² The court held that “it is difficult to see how any one can be compelled, against his will, to become a plaintiff and assume the aggressiveness implied thereby.”⁸³ The court concluded that the discretion of granting the motion should not be exercised in this case.

Based on these state decisions, the following rule is derived therefrom: the right to be heard is constitutional and is a basic aspect of the duty of government to follow a fair process. Thus, the requirement of notice and an opportunity to be heard is an expression of the Due Process Clause.⁸⁴ In the case of transfer of interest during the pendency, a hearing of the proposed party secures fair play, if the adverse party moves for a substitution. In other words, the opposing party is not entitled to obtain substitution without a notice to the transferee, but upon notice, the trial judge could order it.⁸⁵ A notice and a hearing of the party that sought to be substituted would be a less strict requirement in comparison to the German law, which requires an agreement of all parties and thus, secures fairness with respect to all of them. On the other hand, the agreement of all means less flexibility and could prevent substitution in cases where a change of parties would facilitate the proceeding.

3. The Binding Effect of the Judgment and its Limitation

In addition to the question of whether it is fair that the successor get involved in a proceeding of two other parties upon a motion by the adverse party, a second question of fairness is whether a third person can be bound by a judgment rendered between two other persons. One could

80. *White v. Hardy*, 180 Misc. 63, 39 N.Y.S.2d 911 (Sup. Ct. 1943) aff'd, 266 A.D. 660, 41 N.Y.S.2d 210 (App. Div. 1943).

81. *Id.*

82. *Rothbarth v. Herzfeld*, 159 A.D. 732, 144 N.Y.S. 974 (1913).

83. *Id.* at 735.

84. *Fuentes v. Shevin*, 407 U.S. 67 (1972).

85. *Higgins*, 168 C. at 472 (1914); B. E. Witkin, *California Procedure*, Volume 4 § 262, 340 (5th ed. 2008).

ask if it is possible and fair to bind a person who has not made an appearance in court. Interestingly, commentators on the Cal. Civ. Proc. Code § 368.5 recommend that the opposing party should compel substitution of the transferee before the judgment. Otherwise, the transferee may claim that he is not bound by any adverse judgment.⁸⁶ The question arises if and under what circumstances the transferee would be bound.

It is important that the F.R.C.P. do not contain any rules concerning the *res judicata* to parties and third persons. Rule 24, for instance, does not regulate the consequence of an intervention. Another example is F.R.C.P. 13 (a) under which the defendant can raise a counterclaim. The consequence of losing this right by not using the counterclaim is not mentioned in the rule. Therefore, the F.R.C.P. are not designed to solve every single procedural problem in detail; they only provide a framework. The principles of *res judicata* were developed by jurisprudence and are part of case law. “*Res judicata* (is) ... a doctrine judicial in origin.”⁸⁷

(a) The Rationale of the Inter-partes-doctrine

Similar to the German law, the reason for limiting the binding effect to the parties is so that only the parties had an opportunity to litigate.⁸⁸ Other more concrete explanations derive from the right to be heard under the Due Process Clause. “A person cannot be bound by any judgment unless he had reasonable notice of the claim against him and opportunity to be heard in opposition to that claim.”⁸⁹

In American literature, there are two categories of the right to be heard: “instrumental” and “formal” on one hand, and “intrinsic” and “nonformal” on the other hand.⁹⁰ Under the “instrumental”/“formal” aspect, the principle of the right to be heard serves to enforce the substantive law. A person has to be heard in order to present his arguments and to influence the decision.⁹¹ The U.S. Supreme Court held that “when a person has an opportunity to speak up in his own defense, and when the State must listen to what he has to say, substantially unfair and simply mistaken deprivations of property can be prevented.”⁹² Under

86. Cal. Prac. Guide Civ. Pro. Before Trial Ch. 2G(2)(b).

87. *Commissioner v. Sunnen*, 333 U.S. 591, 597 (1933).

88. Restatement (Second) of Judgments § 34 cmt. a (1982).

89. Coquillette, et al., Moore’s Federal Practice at 0.411 (2nd ed. 1955).

90. Ranier Krause, *Urteilswirkungen gegenüber Dritten im US-amerikanischen Zivilprozessrecht* at 58 (1994). (Ger.).

91. *Id.*

92. *Fuentes*, 407 U.S. at 81.

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the “intrinsic”/“nonformal” component of the due process doctrine, the participation gives the party the feeling of dignity. In this context, scholars emphasize the “dignity values.”⁹³

However, on one hand, the aspect of fairness to absent people (Due Process Clause) has to be considered. On the other hand, the advantages of a single adjudication and efficiency have to be considered as well. The judge has to balance both interests, comparable to the situation of class actions under F.R.C.P. 23, where due process considerations require a balance between fairness to absent people – whose claims may be extinguished by the action – and efficiency of a single adjudication.

(b) The Extension of the Res Judicata to Nonparties

Similar to the German law, the judgment rendered in a situation of a transfer of interest is not only binding upon the original parties, it is also effective against the successor, even though he was not substituted or joined and therefore, is not named in the judgment.⁹⁴ At first sight and with regard to the Due Process Clause of the Constitution, the binding effect upon a third person that was not involved in the trial and was not able to defend himself seems problematic. However, the binding effect concerning the third person is necessary for the procedural mechanism. If the judgment would not bind the transferee, it would be useless and unacceptable for the opposing party⁹⁵ to continue the litigation. An interruption would be necessary and a new trial against the third person would need to be initiated.

Based on the legitimate objective of efficiency, Rule 25 (c) wants to avoid this second trial against the third party. The binding effect to the transferee accomplishes the goal of avoiding multiplicity of suits whenever practicable, thereby saving considerable judicial resources. This objective finds expression in other mechanisms of the F.R.C.P. as well. For instance, in the permission for the joinder of several causes of actions arising out of the same transaction under F.R.C.P. 18,⁹⁶ the impleader of a third party defendant under F.R.C.P. 14 (a), the

93. Frank I. Michelman, *The Supreme Court and Litigation Access Fees: The Right to Protect One's Rights*, 6 Duke L.J. 1153, 1173 (1973).

94. Niles, *Federal Civil Procedure*, § 8.440; Coquillette, et al., *Moore's Federal Practice*, Volume 3 B, 25.08 (2nd ed. 1955); *Fronings's Inc.*, 568 F.2d at 110; *Luxliner P.L. Export, Co.*, 13 F.3d at 71.

95. Compare the foundation of the German Rule.

96. *Harris v. Avery*, 5 Kann. 146 (1869).

interpleader under F.R.C.P. 22, or the possibility of counterclaims under F.R.C.P. 13 (a),⁹⁷ accomplishes the goal of judicial efficiency.

Concerning the question of whether the binding effect is fair and thus constitutional, it should be considered that – provided he knew about the pendency of the trial – the successor could have moved for joinder or substitution. This would have offered him the chance of an active participation in the litigation. The court would have been obligated to consider the successor’s position within the decision about the substitution or joinder. In contrast, if the third person is not taking the chance to be part of the trial, he cannot argue that the binding effect upon him would be unfair. By providing the right to make a motion also for the successor, Rule 25 (c) consists of a balance between the doctrines of efficiency and fairness. Thus, concerning a transferee who takes notice of the pending litigation, the rule is settled that the transferee is bound by the judgment.⁹⁸ “In these circumstances it seems reasonable to bind the transferee on notions of both apparent and actual representational authority. If the transferee does not wish to be represented by the transferor, it is a simple matter to seek a substitution of parties.”⁹⁹

(c) Explanation For the Binding Effect on Third Parties

The American concept of the binding effect on third persons is different than the German concept. The basic principle that explains the binding effect on non-parties in American law is “representation.” Res judicata is extended to non-parties “when, in certain limited circumstances, a person, although not a party, has his interest adequately represented by someone with the same interest who is a party.”¹⁰⁰ Representation is equated with participation at trial by the third person that is represented. In the context of class actions under F.R.C.P. 23, absent parties are only bound if they are adequately represented by the representative. This is important to safeguard the due process rights of class members.¹⁰¹ As a consequence, a party who did not “literally” have its day in court is not bound unless it had a “figurative day” in court.¹⁰²

97. *United States v. Heyward-Robinson Co.*, 430 F.2d 1077 (1970).

98. 18A Charles Alan Wright, Arthur R. Miller & Edward H. Cooper, *Federal Practice and Procedure* § 4462, 670 (2002).

99. *Id.* at 670-71.

100. *Martin v. Wilks*, 480 U.S. 755, Fn. 2 (1989).

101. *Hansberry v. Lee*, 311 U.S. 32 (1940).

102. Friedenthal et al., *Civil Procedure* 670 (9th ed. 2008).

(d) Limitation of the Binding Effect to Third Persons

The question arises whether the binding effect is limited where the transferee has no knowledge of the litigation. Generally, it can be stated that U.S. law is reluctant to protect the bona fide interest of the purchaser.¹⁰³ Due diligence is essentially important in any purchase or transaction.

The case, *Golden State Bottling Co. v. NLRB*, involved a transferee with notice. The court held that “persons acquiring an interest in property that is a subject of litigation are bound by, or entitled to the benefit of, a subsequent judgment, despite a lack of knowledge.”¹⁰⁴ Contrary to this broad statement that would even bind the bona fide transferee, one could argue that he needs to be protected. In the circumstance that the transferee does not know about the pendency of a trial concerning the interest, he cannot take the chance to get involved in the trial by seeking substitution or intervening in order to present his position.

Commentators consider the doctrine of fairness and state that the knowledge of the adversary should control. If the opposing party does not learn of the transfer before the judgment, the transferee should be bound. On the other hand, if the adversary knows of the transfer and knows that the transferee does not know of the pendency, it is argued that it seems more fair to deny the binding effect. In this case, the opposing party “could not rely on any apparent authority of the transferor to represent the ignorant transferee, and can protect his own interest in repose by giving notice of the litigation to the transferee.”¹⁰⁵

4. Enforceability of the Judgment Against the Transferee

Another question is how the judgment rendered to the original party can be effective to the transferee that is not mentioned in the title. As mentioned before, commentators on the Cal. Civ. Proc. Code § 368.5 recommend that the opposing party compel substitution. Besides the possibility of a claim by the transferee that he is not bound, the authors mention that the opposing party would run the risk that the judgment may not be enforceable against the transferee.¹⁰⁶

103. Zweigert, *Rechtsvergleichend-Kritisches zum gutgläubigen Mobiliarerwerb*, in: *RabelsZ* 23 1 ff. (1958) (5-10). (Ger.).

104. *Golden State Bottling Co. v. NLRB*, 414 U.S. 168 (1973).

105. *See supra* note 98, at 672-73.

106. Cal. Prac. Guide Civ. Pro. Before Trial Ch. 2G(2)(b).

However, F.R.C.P. 71 extends the enforcement rules to non-parties. This rule is very simple. It states, “When an order grants relief for a nonparty or may be enforced against a nonparty, the procedure for enforcing the order is the same as for a party.” The cases *Westlake North Property Owners Ass’n v. Thousand Oaks* and *Berger v. Heckler* held, “it seems clear that Rule 71 was intended to assure that process be made available to enforce court orders in favor of and against persons who are properly affected by them, even if they are not parties to the action.”¹⁰⁷ Therefore, it has to be distinguished between the enforcement in favor of a non-party on the one hand and enforcement against a non-party on the other hand.

A court order may be enforced by a non-party when that person shares an identity of interest with a prevailing party or is an intended beneficiary of the court order with the right to enforce it.¹⁰⁸ In the case *Peterson v. Highland Music, Inc.*, it was decided that an assignee of a party who prevailed in a dispute concerning the title of property under Rule 71 would be entitled to enforce a judgment in the same manner than the assignor.¹⁰⁹ That means for the situation of the transfer of interest after pendency, a transferee as a non-party may enforce a judgment rendered in his favor.

A court order can be enforced against a person who is not a party if that person’s interests are so closely related to a losing party’s interests that enforcement against that non-party is not unfair.¹¹⁰ In the context of enforcing a judgment against a non-party, the F.R.C.P. are restricted to circumstances where the enforcement does not violate due process or is otherwise lawful.¹¹¹

Considering due process, the requirement that has to be met is that the non-party has notice of the judgments and its contents.¹¹² Furthermore, the enforcement of a judgment against a person who is a successor in interest to a party requires that the court obtain personal jurisdiction over the successor.¹¹³ As previously discussed, the transferee can be bound by the judgment in certain circumstances and thus, the judgment would also be enforceable against him.

107. *Westlake N. Prop. Owners Ass’n v. City of Thousand Oaks*, 915 F.2d 1301, 1304 (9th Cir. 1990); 771 F.2d, 1156, 1165; *Berger v. Heckler*, 771 F.2d 1556 (2d Cir. 1985).

108. *Federal Practice & Procedure – Civil Rules: 2010 Quick Reference Guide*, Vol. 12B, at 1047 (2010).

109. *Peterson v. Highland Music, Inc.*, 140 F.3d 1313 (9th Cir. 1998).

110. *Id.*

111. *See supra* note 108.

112. *Peterson*, 140 F.3d at 1323-24.

113. *LiButti v. US*, 178 F.3d 114 (2nd Cir. 1999).

V. DIFFERENCES OF THE CONCEPTS OF TRANSFER OF INTEREST WITH RESPECT TO DIFFERENT LEGAL CULTURES

More abstract from the previous discussion, this section examines whether differences in the legal cultures have an impact on the particular problem of transfer of interest after pendency under German and American law. Differences in culture have consequences for the legal process. One might ask if the differences in the particular concepts of transfer of interest are expressions of differences in legal cultures. "Cultural differences do explain something of why institutional and procedural differences arise in different legal systems and why transplanting legal institutes from one society to another may be more difficult in one case than in another."¹¹⁴ Of course, the U.S. and Germany share common cultures in many aspects, because they are democracies with free, strong economies. However, there are differences in the historical experiences, in the structure of political and legal institutions, in critical social values,¹¹⁵ and in the view of the constitutional state.

As a result of history, the Americans have a high level of distrust against authority, especially because the judges in the colonies were considered to be tools of the monarch. The American democracy is based on values of individualism and self-sufficiency, which has an impact on the law. One fundamental consequence for the procedure is that there is a heavy reliance on the private initiative of the parties and their lawyers to protect and vindicate legal rights,¹¹⁶ while the American judge is not considered to be powerful. The general rule in common law countries is that the civil litigation is lawyer-dominated, while the judge is considered to play a passive role and acts more like a neutral umpire than a manager.¹¹⁷ This traditional role of the counsels and judges and the "laissez fair proceeding" in the U.S. is a significant feature of American legal culture. In contrast, the European civil justice systems seem to represent a high degree of reliance on state institutions¹¹⁸ and the judge is considered to play an active role in the European systems on the continent, especially

114. Hein Kötz, *Civil Justice Systems in Europe and the United States*, 13 *Duke J. Comp. & Int'l L.* 61, 70 (2003).

115. Oscar G. Chase, *Legal Processes and National Culture*, 5 *Cardozo J. Int'l & Comp. L.* 1, 7 (1997) (regarding the differences between the United States and Germany).

116. Murray & Stürner, *German Civil Justice* at 580 (2004).

117. Richard Freer, *Civil Procedure* at 5 f, (2nd ed. 2009).

118. Murray & Stürner, *German Civil Justice* at 580 (2004).

in taking evidence. This procedure is labeled as “inquisitorial” or “non adversarial.”¹¹⁹

It is an interesting fact that the particular problem of a transfer of interest pendente lite is not treated typically “adversarial” and “inquisitorial” in each system. Under F.R.C.P. 25 (c), the judge has more power than in the civil law country Germany, because he is the one who decides whether to allow the substitution. That means that the applicable rule for the transfer of interest of the “adversarial system” is not adversarial, and the relevant rules of the so-called “inquisitorial” civil procedure are not “inquisitorial” at all.

Another mode demonstrating that the so-called adversarial system bears features of the inquisitorial system is F.R.C.P 54 (c). Under this provision, the judge has the power to grant more than the plaintiff asked for. It is the court’s duty to grant all appropriate relief. Aside from default judgment, the court can award relief beyond what is sought in the complaint.¹²⁰ That would not be permissive in Germany and Italy where, according to § 308 ZPO¹²¹ and article 112 ICCP, the judge is bound to what is demanded. The court cannot grant to the parties a relief different from the one sought. In other words, in Italian and German litigation

119. Geoffrey C. Hazard, Jr. & Michele Taruffo, *American Civil Procedure: An Introduction* 86 (1997): This contrast is based on the difference in the judge’s role in taking evidence, especially in the taking of witness testimony. But labeling the systems in the explained way – adversarial and inquisitorial – is criticized a lot by some authors, who hold the view that in both – in the U.S. and on the European Continent – the civil courts must work with what they are given and must establish the facts for their judgment from the materials which the parties supply and cannot go beyond the parties’ factual contentions.” Hein Kötz, *Civil Justice Systems in Europe and the United States*, 13 *Duke J. Comp. & Int’l L.* 61, 66-7 (2003). Kötz states that the contrasting between the adversarial system and the inquisitorial system “is not only misleading, but also downright wrong.” Also in the Continental civil procedure the judge has no power to introduce independent evidence; he has to base his judgment on the facts that the parties provide (“Da mihi facta, dabo tibi ius”). This principle is called the “formal truth” (“formelle Wahrheit”) in contrast to the “material truth” (“materielle Wahrheit”), which means the “real truth” and applies in criminal matters. “Formal truth is what the court, to the best of its ability, believes to be true having regard to the evidence placed before it by the parties.” *Id.* All in all, the critics say that the contrast between the American and the Continental procedure “has been grossly overdrawn.” John H. Langbein, *The German Advantage in Civil Procedure*, 52 *U. Chi. L. Rev.* 823, 824 (1985). Furthermore, both systems are considered to be adversarial. *Id.*; Hein Kötz, *Civil Justice Systems in Europe and the United States*, 13 *Duke J. Comp. & Int’l L.* at 61, 67; John von Mehren, *The Significance for Procedural Practice and Theory of the Concentrated Trial: Comparative Remarks*, *Europäisches Rechtsdenken in Geschichte und Gegenwart: Festschrift für Helmut Coing* 361 n. 3 (N. Horn ed. 1982). (Ger.).

120. Simona Grossi, *A Comparative Analysis Between Italian Civil Proceedings and American Civil Proceedings Before Federal Courts*, 20 *Ind. Int’l & Comp. L. Rev.* 213 (2010).

121. Section 308 ZPO: “(1) The court shall not be empowered to award by judgment a party anything that shall have not been demanded. Without limiting the generality thereof, the forgoing shall be applicable to trusts, interests and other supplementary claims. (2) The court must decide on the obligations to bear the costs of the action also without a motion.” Kinsella & Cormeaux, *Digest of Commercial Laws of the World*, Binder 7.

there has to be a strict correspondence between what the parties have demanded and what is finally granted by the judge.¹²²

One might say, the different approaches to the situation of the transfer of interest pendente lite – on the one hand discretion of the court and on the other hand consent of the parties – can also be considered an expression of different legal cultures and different ideas of the constitutional state. Discretion means flexibility and adaptability, which is the main feature of common law and especially of the F.R.C.P. As already mentioned, the F.R.C.P. are not designed to solve every single procedural problem in detail; they are only a framework that provides a way to solve a problem. Considering this, F.R.C.P. 25 (c) matches up to the concept of the common law, which can be shaped and changed easily to reflect differing circumstances and needs, while it can also reflect changing social conditions.¹²³ Discretion of the court is the “entrance” for different considerations, whereas the consent of the parties means very clear criteria that do not give any room for further considerations. Specific rules are the feature of civil law countries, which are required due to their specific view of the Constitutional State.

VI. CONCLUSION – MAIN DIFFERENCES AND SIMILARITIES OF THE GERMAN AND AMERICAN CONCEPTS

It can be concluded that the transfer of interest in the context of litigation is treated similarly under the German procedural law and under the American Federal Rules of Civil Procedure. The obvious similarity is that the transfer of an asset is allowed once a trial is pending. This makes sense in modern economic systems. Under the German and the American concepts, the same proceeding is continued among the original parties after the transfer occurs. The rationale of both rules is the same. Firstly, it is efficient to continue the same trial. Secondly, nobody should be deprived of his successes that have been reached during the proceeding, so far. The loss of successes during the litigation would contradict the principle of stability in the allocation of rights.¹²⁴ Continuance is the only way to avoid friction during the proceeding and to avoid unfairness.¹²⁵

122. Concerning Italy: Simona Grossi, *A Comparative Analysis Between Italian Civil Proceedings and American Civil Proceedings Before Federal Courts*, 20 *Ind. Int'l & Comp. L. Rev.* 213 (2010).

123. Jonathan Humbach, *Whose Monet?: An Introduction to the American Legal System* 101 (2007).

124. Rainer Krause, *Urteilswirkungen gegenüber Dritten im US-amerikanischen Zivilprozesrecht* at 73 (1994). (Ger.).

125. *Id.*

Another main similarity is the possibility of the substitution of the transferor. The requirements of such a substitution are different. While the German law requires the consent of the transferor, the transferee, and the opponent, the decision about the substitution under American law lies in the discretion of the court. The German requirement of consent can be assessed very clearly. The American model of discretion is a question of convenience, and different considerations of efficiency and fairness come in to play. Thus, the American rule leads to less predictability and less clarity than the German concept.

Another similarity between the American and the German proceedings is that a judgment is usually only binding between the parties. That is a matter of concern, of course, because only the parties had the opportunity to litigate. However, under the American and German law, the successor is also bound in the situation of a transfer after pendency. That binding effect upon the transferee is a necessary consequence.

The exception to the binding effect is good faith. In the context of the protection of good faith, one of the main differences between the German and the American law should be emphasized. Under the German law, the good faith of the successor would decide the question, if he were bound to the judgment. In the U.S., the knowledge of the adversary should control the extension of the binding effect. Comparing the two concepts, the considerations in the situation of a bona-fide-transferee are more complex in the U.S. Furthermore, the requirements of a limitation on the binding effect to third persons are much stricter than under the German rule. As opposed to the German concept, the good faith on the side of the transferee is not sufficient. Besides the good faith of the transferee, the opposing party needs knowledge of the transfer and of the good faith. Thus, good faith is protected less than it is under German law.

Another obvious similarity of both concepts is that the judgment is enforceable against a third person. This is a necessary consequence similar to the binding effect of the judgment upon the successor.

All in all, the big picture of the transfer of interest of an asset after the trial is pending is the same. The German and the American rules stand in the light of fairness and efficiency. Differences like the requirements of the substitution and the protection of good faith are the mirror of different legal cultures.