

## **CLASS ACTION LAW SUIT: A NEW SPECTRUM OF CORPORATE LAW**

**“The idea is like anything in our democracy - the more people you have speaking as one voice, the louder that voice becomes.”<sup>1</sup>**

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### **ABSTRACT**

The government-Nestle legal battle is the first instance of a class action suit filed in the country by the Department of Consumer Affairs, Ministry of Consumer Affairs, Food & Public Distribution, citing the Consumer Protection Act, 1986. Business Standard reaches out to legal experts to understand the legal intricacies of a class action lawsuit.

The conception of Class Action Suits is one of the many improvement introduced in the Companies Act, 2013 vide Section 245. The concept of *Class Action* is not new but in Indian context it has found recognition and enforceability now only by means of Companies Act, 2013. The class action suit first time came to the highlight in the context of securities market was when the Satyam scam broke out in year of 2009. Subsequently, the Indian investors in India couldn't take any legal remedy against the company while their counterparts in USA filed class action suit claiming compensations from the company. This mechanism evolved to overcome the well-known 'Collective Action' problem, where suits by smaller stakeholders are not cost effective, and so may never get filed. As such, this is applicable not just in corporate law, but across the board.

The injunctive reliefs could be overlapping but we have got a completely different concept for availing compensation, damage or any other appropriate action for the fraudulent activity of the company, its directors, even auditors and advisers. The statutory provisions have made it wider and appropriate till date as far as the compensation is concerned. The remedies available under the two are different. Sections 241-244, which also seek to redress cases of oppression and management have a greater array of remedies.

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## **INTRODUCTION**

Legal recognition and enforceability of Class Action Suit is given in 2013 Act but is not new and known for a long time. In USA and UK it developed in the middle of 17<sup>th</sup> century as a bill of peace. It was allowed in English courts when there were number of applicants and the joining of applicants will cause delay of trial and was practically not possible, the members in the group possess a joint interest, any decision regarding it would affect all of them and when it is seen that all the members can be represented by one, a bill of peace may be filed.

Collective lawsuits/Class Actions originated in the United States in 1938 and are still predominantly a U.S. phenomenon. It describes a “Sui Generis “area of Litigation. In the United States federal courts, class actions are governed by Federal Rules of Civil Procedure Rule 23 and 28 U.S.C.A. § 1332(d). In federal Civil Procedure law, which has also been accepted by approximately 35 states in U.S (through adoption of state civil procedure rules similar to the federal rules), the class action must have certain definite characteristics. In several European countries with civil laws different from the English common law principle (which is used by US courts), changes have in recent years been made that allow consumer organizations to bring claims on behalf of large groups of consumers. Class Actions Suits are allowed in European Countries i.e. Austria, Canada, Germany, France, Netherlands, Spain.<sup>2</sup>

The bill of peace, later the class action, provided a convenient and efficient way for resolving legal disputes affecting a number of parties with similar claims. Common issues that could have similar outcomes did not have to be tried piecemeal in separate actions, thus saving the courts and the litigants' time and money.<sup>3</sup> The basic motive of incorporating in 2013 Act is to check the increasing number of corporate cases related to fraud instituted in courts. In India the concept of class action suit was first dealt with in the satyam scam case where a scam related to securities was discovered in 2009 which had a huge impact on global headlines.

The foreign investors in other countries were able to take their claim by filing a class action suit but due to lack of adequate provisions in India at that time, the investors couldn't take their money back. The shareholders filed a petition in Supreme Court for claiming 5000 crores but was of no avail and petition was being dismissed.

Now with the above foresaid reasons the concept of class action suit is being incorporated under section 245 of Companies Act, 2013. This section enables the members and depositors or any class of them to file an application against a company in National Company Law Tribunal. Suit under Section 245 may be filed by members or depositors or any class of them before the National Company Law Tribunal, if they believe that the management or conduct of the affairs of the company prejudices the interest of the company, its members or depositors.<sup>4</sup> Therefore we can define Class Action Suit as a suit which can be filed by a group of members against a group of members i.e. Company.

A group of people who have common interest to be sue or be sued. The incorporation of this section has brought us many advantages which will help Indian Corporate Industry and a Public at large. The effect can be seen in a recent case of Nestle versus Central Government of India where a class action suit was filed by the government against the Nestle Company for stopping the production of its product Maggi and asking for imposing a ban on it as allegations were made that this product contained a high amount of lead which is harmful for human body.

Thus, it would be right to state that by incorporating the said provision, the legislature aims to encourage the investors and boost their confidence in the capital market and thus initiate healthy investments and healthy growth of the economy.<sup>5</sup> The concept of Class Action suit was first being recommended by J.J Irani Committee Report in 2005.

### **DEFINITION OF CLASS ACTION SUIT**

According to the Rule 23 of the Federal Rule of Civil procedures, there are three types of class action suits. The first one is filed where different lawsuits might affect other members of the class or the defendant. Secondly where a class action is being filed when a class of people seeks an injunction or some type of relief and in the third type of class action suit where there is a question of law or a fact which is common to the entire class. Under this type, individual members of the class may "opt out" of the litigation if they do not want to be bound by the results of the suit.<sup>6</sup>

In India prior to the enactment of 2013 Act, class action suits were being filed as representative's suit under Section 91, Order 1 Rule 8 Civil Procedure Code 1908 and in the form of Public Interest Litigations. It was also being provided under Consumer Protection Act 1986. "The government can take action under Section 12 of the Consumer Protection Act, 1986, either in its

individual capacity, or on behalf of the complaining consumers.”<sup>7</sup> The government in this case appears to have done so on behalf of consumers, however any such suit has to be presented along with cogent evidence, thorough preparation, assisted and accurate quantification of damages, with product liability cases based on testing.<sup>8</sup> But different provisions have different procedures of filing suit. In Satyam scam Case, class action was being filed under Consumer Protection Act only. After the enactment of Companies Act, 2013, it has been defined under section 245 which explains that any members or depositors or any class of them or the case may be<sup>9</sup> may file an application to the tribunal i.e. National Company Law Tribunal in case where they are of the opinion that the management or conduct of the affairs of the company are being conducted in such a way that is prejudicial to the interests of the company or its members or depositors,<sup>10</sup> and relief or reliefs could be sought which may include, restraining the company from committing an act which is ultra vires or beyond the scope of the articles or memorandum of the company,<sup>11</sup> restraining the company from committing breach of any of provision of the company’s memorandum or articles,<sup>12</sup> declaring a resolution to alter the memorandum or articles of the company as void if the resolution was passed by suppression of material facts or obtained by mis-statement to the members or depositors,<sup>13</sup> restraining the company and its directors from acting on such resolution,<sup>14</sup> restraining the company from doing an act which is contrary to the provisions of the Act or any other law for the time being in force,<sup>15</sup> restraining the company from taking action contrary to any resolution passed by the members,<sup>16</sup> claiming damages or compensation or demand any other suitable action from or against the company or its directors, the auditor including audit firm of the company, or any expert or advisor or consultant or any other person, for any incorrect or misleading statement made to the company or for any fraudulent, unlawful or wrongful act or conduct or any likely act or conduct on their part<sup>17</sup> and lastly seeking any other remedy as the Tribunal may deem fit.<sup>18</sup> As per Section 245(3), the requisite number of members for bringing in the suit, in case of company having a share capital, shall be not less than one hundred members of the company or not less than such percentage of the total number of its members as may be prescribed and whichever is less.<sup>19</sup> Secondly, in the case of a company not having a share capital, the requisite number of members shall not be less than one-fifth of the total number of its members.<sup>20</sup> Also, the requisite number of depositors under sub-section (1) of Section 245, shall not be less than one hundred depositors or not less than such percentage of the total number of depositors as may be prescribed, whichever is less, or any

depositor or depositors to whom the company owes such percentage of total deposits of the company as may be prescribed.<sup>21</sup> It must be noted that, under Section 245, any order passed by the Tribunal is binding on the company and all its members, depositors and auditors including the audit firm or expert or consultant or advisor or any such person associated with the company.<sup>22</sup> If a company fails to comply with an order passed by the Tribunal under Section 245, is liable to be punished with fine ranging from five lakh rupees to twenty-five lakh rupees and every officer of the company who is in default shall be punishable with imprisonment for a term which may extend to three years and with fine ranging from twenty-five thousand rupees to one lakh rupees.<sup>23</sup> However, the provision of Class Action Suit doesn't apply to a banking company as is defined under Section 245(9) of the Act.

From the study of above section we can conclude that the legislature had an intention to safeguard the interest of creditors and investors and this section implies it in strict sense. This section focuses on to reduce the court burdens, minimize the corporate fraud cases, to protect the investors from the bad intentions of the company.

### **CRITICAL ANALYSIS OF SECTION 245 OF COMPANIES ACT, 2013**

One recent example of this is the filing of a suit by four investors under Civil Procedure Code, against Financial Technologies (India) Limited (FTIL) and National Spot Exchange Limited (NSEL) and forty other related entities to abstain them from selling their assets. This suit has been filed by four investors of which one, Modern India, has invested rupees 30 crores in NSEL.<sup>24</sup>

Section 245 of the Companies Act, 2013 places several restrictions on shareholders. The company under the current law still holds immense power and control over the shareholders, for instance, the company can prescribe the minimum number of shareholders required to apply to the NCLT. Also, derivative action does not completely ensure corporate governance and good practice in the company. The tribunal thoroughly scrutinizes the application made by shareholders and depositors, making the application more about the shareholders than the company. There are still several hindrances that restrict shareholders from filing a lawsuit against the company's management.<sup>25</sup>

Therefore this section relating to prevention of oppression and mismanagement permits shareholders and depositors of a company to take up any matter of mismanagement or fraudulent

practice with the tribunal. Shareholders and depositors under this section can not only restrain the company’s management from continuing the unlawful act but can also claim damages and compensation for any damage done to them .Both civil and criminal liabilities are imposed on the directors, managers, and management of the company for fraudulent activities..

**DIFFERENCE BETWEEN CLASS ACTION SUIT AND SUIT FOR OPPRESSION AND MISMANAGEMENT**

An application can be filed by any member of the company under section 241 of Companies Act 2013 when oppression and mismanagement is done in the company whereas an application under section 245 can be filed by any person that is any member, group of members, depositor or depositors or any class of them when an company does an act which is prejudicial from the interests of the company. Both sections have different meaning and difference relevance but often people confuse between them. Therefore there are some minute differences - Firstly, oppression and mismanagement is being filed by any member of the company against a company and its depositors only whereas a class action suit can be also filed against a third party, not only by its members but also by the creditors, investors and anyone. Secondly, oppression and mismanagement suit could be filed against the company and its statutory appointees only,<sup>26</sup> thirdly, petitions under section 397/398 of the Act can be filed for past mismanagement and to prevent recurrence.<sup>27</sup>

Earlier in the Companies Act 1956, the oppression and mismanagement was being defined in Section 397 and 398 and no concept of class action was being incorporated but when the amendment took place and a new act was being enacted the provisions of Oppression and Mismanagement was being shifted to section 241 as well as the concept of class action suit was being incorporated under section 245 of this Act. This was being required as A depositor, upon being aggrieved by the actions of a body corporate could file a class action suit but not a suit under Section 397/398 of the old Act and under section 241/242 of the new Act.

It can be clearly explained by the help of tabular form<sup>28</sup> -

	PREVENTION OF	CLASS ACTION SUITS U/S
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POINTS	OPPRESSION AND MISMANAGEMENT U/S 241 TO 244	245
Who can file application?	Members of the Company	Members as well as deposit holders of the company
Against whom application can be filed?	Company and its statutory appointees	Company, any of its directors, Auditor, including audit firm, Expert or advisor or consultant or any other person.
Matters for which application can be filed	Any current or past activity or to prevent recurrence	Any current, past or future activity, including to desist from one or more particular action that have not been taken yet.
Beneficiaries	It is the derivative Claim wherein it is for the benefit of all the shareholders, the company and in public interest	The plaintiffs are the beneficiaries

### **ADVANTAGES AND DISADVANTAGES OF CLASS ACTION SUIT**

There are many advantages of class action suits as it will lead to reduce the number of suits who have a common interest, will work as a benefit to large number of people, it will act as a public reform in the country, it reduces legal costs and improves efficiency in the legal process, stakeholders are being provided with a better platform other than oppression and mismanagement to fight with the company, benefit is given to the deposit holders who were not having any right to file against a company if injustice is done to them, it reduces the trial time, avoids the repetition of same witnesses and evidences, non- government organizations and cooperative societies have found a way to help people and raise their voice against a company and the most important factor

that the companies will be more vigilant now, they will be focused on their work and will not do any act which will hampering the interests of stakeholders and other people.

Despite of these benefits there are some lacunae in class action suits leading to its failure such as it is only provided to deposit holders and members, other stakeholders such as creditors, bankers, debenture holders and even regulatory authorities are not given, there is also a delay in our legal system which leads us to delay in class action suits. Another major factor is that there is no prohibitive cost of filing suits, lawyers don't put up their full efficiency as no incentives and reward is given to them which is completely different in USA as US laws permit contingency fees for lawyers that is a success fee paid to the lawyer arguing the class action for the plaintiff. The fee will only be paid if the order is in favour of the plaintiff and is paid from the compensation and damages that is awarded.

Another major setback is that it can be used as a major misuse by the minority shareholders for their infructuous interest by hampering the functions and regulations of the company. This suit is also to be filed in National Company Law Tribunal which is already overburdened with many cases hence no speedy action is taken. According to my opinion the class action suits should be dealt by Securities and Exchange Board of India, as the Securities Class Action already vest in it.

## **CONCLUSION**

These are the words said by Attorney Christopher Gilreth<sup>29</sup> and it is really true when applied. If there are more people who raise a voice against something, then their voice is being given importance and when there is an objection raised by lesser people, they are being neglected. With the same meaning, the concept of class action suit is being incorporated in India in Companies Act, 2013.

In our country, this concept of class action has always failed, but is very important to promulgate it at the minimum level where the stakeholders are aware about their rights. It is to be ensured that the benefits of class action are given to shareholders and the tribunal takes an effective and immediate actions. It is a benefit for investors, who risks their interest in the company, it provides them a medium to fight as one unit against a massive company and its management. Deposit holders who were not having any mode to fight with the company are also given an opportunity to file a class action suit against any wrongful action done by the company. With the help of this the



accountability of the company and its management towards its stakeholders and the minority is also being increased.

However, it has been observed in various class action suits (particularly in the US) that victims receive no compensation or benefits for their association. Sometimes, it is felt that the compensation awarded may have been greater if the case was pursued by an individual rather than a group. Also, a majority of people are not really aware of the concept in its entirety and the nature and amount of compensation that they are entitled to receive.<sup>30</sup> The success of the class action suit in the corporate industry is still uncertain and the reason behind is the exclusion of a major class of stakeholders comprising of creditors, bankers and debenture holders. Even the regulatory authorities and banking companies have been kept out of its ambit. There have been many criticisms regarding these defects but no action is being taken by our government and courts to amend it.

Till now class action suits have no effect and no strength in our country, it has to be measured by giving the full effect upon the constitution of National Company Law Tribunal. The best part of class action suits is that if it fails it has no effect in the similar cases going forward as each and every case depends upon its merit which is further based upon legal evidences and legal issues. But the said provision is of great importance for the stakeholders, as it provides them with more powers and has given a value to depositors who were not having any value till now.

Keeping all the factors in mind, we can say that by introducing this provision legislature had taken a step towards the better future of corporate world and a good corporate governance.

## REFERENCES

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<sup>4</sup> Archit Rajpal and Urwashi Srivastava, "Class Action Suit – A new trajectory in Indian Corporate Industry", <http://www.ijesls.com/Archit%20Rajpal%20&%20Urvashi%20Srivastava%20-Full%20Paper-.pdf>, April 20, 2016, 03:17 PM.

<sup>5</sup> *ibid.*

<sup>6</sup> Phillips Petroleum Co. v. Shutts

<sup>7</sup> Consumer Protection Act 1986, Section 12 (1)(c)

<sup>8</sup> Sudipto Dey, "Class action lawsuit explained", [http://www.business-standard.com/article/opinion/class-action-lawsuit-explained-115081600603\\_1.html](http://www.business-standard.com/article/opinion/class-action-lawsuit-explained-115081600603_1.html), April 20, 2016, 03:57PM

<sup>9</sup> Companies Act 2013, Section 245 (1).

<sup>10</sup> *ibid*, Section 245 (2).

<sup>11</sup> *id*, Section 245 (1) (a).

<sup>12</sup> *id*, Section 245 (1)(b)

<sup>13</sup> *id*, Section 245 (1) (c).

<sup>14</sup> *id*, Section 245 (1) (d).

<sup>15</sup> *id*, Section 245 (1) (e).

<sup>16</sup> *id*, Section 245 (1) (f).

<sup>17</sup> *id*, Section 245 (1) (g).

<sup>18</sup> *id*, Section 245 (1) (h).

<sup>19</sup> *id*, Section 245 (3)(1)(a)

<sup>20</sup> *id*, Section 245 (3)(1)(b)

<sup>21</sup> *id*, Section 245(3)(ii)

<sup>22</sup> *id*, Section 245(6).

<sup>23</sup> *id*, Section 245(7).

<sup>24</sup> *Supra* note at 3

<sup>25</sup> Tanvi Kini, "The significance of Derivative Action in India", <http://journal.lawmantra.co.in/wp-content/uploads/2015/05/5.pdf>, April 16, 2016, 11:03PM

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