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BEYOND STATUTORY THRESHOLDS: THE EVOLVING ROLE OF DERIVATIVE ACTION IN MINORITY SHAREHOLDER PROTECTION

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INTRODUCTION

Corporate governance is based on majority rule, whereby the corporate affairs are conducted as directed by the majority of votes to ensure effective decisions making. The principle of majority originated from the case of *Foss v Harbottle*, where once a decision is passed by the majority of the company's members in accordance with the bylaws, it becomes legally binding on every member.¹ In such settings, where the majority rule is a norm, the voice and interests of minority shareholder are often excluded which can result into oppressive behaviour by the majority such as abuse of corporate powers, siphoning off profits, refusal to grant legitimate rights, or manipulation of the company structure to their benefits. This disequilibrium calls for legal protection to safeguard minority shareholders, against such exploitation and for equitable and proper management of the company.

To meet these challenges, the Companies Act, 2013 provides a statutory framework to safeguard minority interests under sections 241 to 246 as it gives shareholders the right to relief under NCLT by filing and O&M petition if the affairs of the company are being conducted in a prejudicial manner. Apart from these legal remedies, the principle of derivative action also acts as a mechanism in safeguarding the rights of minority. Derivative Actions are suits that are filed by the shareholder on behalf of the company against its officers or directors. It is an action that is brought to either compel the corporation to sue or an action that is brought on behalf of the corporation to redress the harm caused to the corporation.² Although the Indian statutes lack

¹ Ritika Sharma, *Foss v Harbottle case: Rule of Majority*, Tax Guru, 19 March 2024, <https://taxguru.in/company-law/foss-harbottle-case-rule-majority.html>

² Ananya Sinha, *Section 241 of the Companies Act, 2013: a Positive Approach Towards Shareholder Derivative Action Suits in India*, Social Science Research Network, 10 April 2024, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4754345

the codification of derivative actions, the courts have accepted their applicability at times where the majority control leads to inactivity or injustice to the company as well as the shareholders.

This article attempts to critically analyse the legislative regime available under the Companies Act, 2013 for safeguarding minority shareholders, specifically the remedies available under Sections 241 to 246 on the occasion of oppression and mismanagement. The scope and limitation of these provisions are examined while emphasizing the procedural hurdles created by Sections 244 and 245 that frequently bar access to relief. Observing that these statutory provisions can be wanting in some situations, particularly where perpetrators are at the helm and minority shareholders cannot satisfy the specified thresholds, the article goes further to examine the evolution of derivative action as a judicial remedy. In an analysis of Indian jurisprudence, the article identifies how courts have acknowledged and fashioned derivative actions to complete the gaps remaining in the statutory scheme, and ends by proposing formal codification of derivative actions for uniform, equitable, and accessible corporate remedies.

LIMITS OF STATUTORY PROTECTION AND THE RISING RELEVANCE OF DERIVATIVE ACTION IN INDIA

The Companies Act, 2013 brought with it a strong statutory mechanism to safeguard minority shareholder interests, especially in circumstances of oppression and mismanagement. Sections 241 to 246 prescribe mechanisms for relief, vesting the NCLT with powers to act in circumstances where corporate affairs are being conducted in a manner prejudicial to the company's interests, its shareholders, or the public interest. Yet, even though the Act is so extensive, statutory remedies tend to prove inadequate, inaccessible, or procedurally excluded especially where the company is dominated by wrongdoers. It is this that has put derivative action in sharper relief as a needed complement to India's minority protection.

STATUTORY REMEDIES UNDER THE COMPANIES ACT, 2013

Under Section 241, the members of a company may approach the NCLT when the affairs of the company are being conducted in a manner which are prejudicial in manner, which was elaborated in the landmark judgement of *S.P. Jain v. Kalinga Tubes Ltd.*³ where the Supreme Court laid down the principles to determine what concludes to be an oppressive behaviour i.e. that the conduct must be burdensome, harsh and wrongful, involving lack of probity or fair dealing to a member in the matter of his proprietary rights as a shareholder.⁴ Further, the

³ *S.P. Jain v. Kalinga Tubes Ltd*, AIR 1965 SC 1535

⁴ Shaneen Parikh and Namita Shetty, Protection and Redressal of Minority Shareholder Rights, India Corporate Law Blog Cyril Amarchand Mangaldas, 6 March 2023,

Supreme Court clarified in the judgement of *Needle Industries India Ltd. v. Needle Industries Newey (India) Holdings Ltd*⁵ the necessity of mala fide intention. Once such prejudicial activities are detected, the aggrieved can either file for a class action under section 245 which enables action to prevent the company, directors, auditors, or advisers from acting in a manner: ultra vires to the company's constitution; fraudulent or unlawful, or prejudicial to the interests of shareholders or depositors or under section 244 which outlines the right to apply under section 241. Once an application has been made under section 241, the NCLT is empowered under section 242 to aid the minority shareholders by granting relief such as regulating the affairs of the company; termination, setting aside or alteration of agreements; removal of directors; and winding up the company on just and equitable grounds.

BARRIER TO THE STATUTORY REMEDIES

Though there is a strong regulatory machinery under the Companies Act, 2013, to redress grievances of minority shareholders, it too is inadequate in practice to protect minority interests, mainly because of the high threshold requirements under Sections 244 and 245. The procedural hurdles largely deprive aggrieved shareholders of effective relief. Section 244 prescribes the right of a member to move the NCLT under Section 241 in situations of oppression and mismanagement. It provides that only members who hold at least 10% of the issued share capital of the company or not less than one-tenth of the total members can move the Tribunal. Although the level is intended to discourage frivolous or vexatious petitions, it unwittingly excludes legitimate minority complaints. Section 244 does have a proviso that authorizes the Tribunal to dispense with the quantitative requirement, but the discretionary relief is not automatic and in most of the cases necessitates the applicant first to establish that the case is exceptional and prima facie meritorious, creating an additional procedural bar.

Equally, Section 245, which applies to class action suits, also has quantitative and cost-related thresholds. In a case of a share capital company, at least 100 members or such number as may be determined, or members holding at least 10% of the issued share capital are required to join together to start a class action. These thresholds, even if well-motivated, frequently serve as a block to justice, especially when the ill-doing is clear but the complainants are too insignificant in number or lack an adequate interest. This procedural inflexibility complicates it for minority shareholders,

<https://corporate.cyrilamarchandblogs.com/2023/03/protection-and-redressal-of-minority-shareholder-rights/>

⁵ *Needle Industries India Ltd. v. Needle Industries Newey (India) Holdings Ltd*, 1981 3 SCC 333

The question arises when the threshold fails, what happens when a minority shareholder, with a genuine grievance, is unable to meet the threshold under Section 244 and cannot pursue a class action under Section 245?

THE ROLE OF DERIVATIVE ACTION AND ITS JUDICIAL TRENDS

Where a shareholder cannot full-fill the statutory requirement under Section 244 of the Companies Act, 2013, and is also prevented from acting by virtue of the prohibition imposed on the company, ordinarily on account of control exercised by the wrongdoers the only practical and equitable relief available is derivative action. This type of action enables a shareholder to bring proceedings in the company's name in order to remedy an injustice against the company, as opposed to against the shareholder individually. Thus, derivative action addresses an important procedural lacuna generated by the threshold conditions mandated by Sections 244 and 245. In closely held companies, minority shareholders could be numerically unable to bring proceedings under these sections even when faced with serious mismanagement or fiduciary breach by the controllers. Derivative action guarantees that corporate evils are not sheltered from accountability merely because the aggrieved shareholder does not have the mandatory percentage of ownership or support from other members

Although derivative actions are not specifically enacted in the Companies Act, 2013, Indian courts have continuously recognized their legitimacy and necessity, particularly in situations where statutory provisions are inadequate.⁶ The Indian judiciary has been instrumental in determining the contours of derivative action based on common law principles, specifically from English jurisprudence like *Foss v. Harbottle*, which prescribed that the company is the correct plaintiff in cases relating to wrongs inflicted upon it. But Indian courts have transcended the strict majority rule established in *Foss* and developed equitable exceptions in the interest of minority shareholders.

In the case of *Rajmundas Khemka v. Taran Kumar Das & Ors.*, the NCLT confronted the waiver of threshold conditions under Section 244(1). The National Company Law Appellate Tribunal (NCLAT) acknowledged that derivative actions might be permitted where the company is defrauded by controllers, and the shareholder cannot meet the statutory threshold. The Tribunal reiterated that the proviso to Section 244(1) is there to ensure that procedural hurdles do not

⁶ Roopam Dadhich and Sankalp Jain, Contextualising Derivative Action Suits in India, *The Competition and Commercial Law Review*, <https://www.tcclr.com/post/contextualising-derivative-action-suits-in-india> (July 10, 2025)

override substantive justice, and derivative action is a means to that end. Further in the case of *Cyrus Investments Pvt. Ltd. v. Tata Sons Ltd.*, the NCLAT acknowledged the principles of derivative actions in corporate governance failures, highlighting minority shareholders can bring derivative claims where majority shareholders misuse their control.⁷ Although the case concerned larger issues of oppression and mismanagement, the tribunal recognized that the inaction by the company for reasons of internal control dynamics can justify shareholder derivative intervention.

BRIDGING STATUTE AND EQUITY: NEED FOR CODIFICATION AND REFORM

Even though derivative actions have been judicially endorsed in India, the lack of formal legislative recognition introduces uncertainty, procedural indeterminacy, and the possibility of inconsistencies in judicial interpretation.⁸ Derivative actions, even though crucial in serving minority interests when statutory avenues are shut down, in India function only through judicial precedent and equitable doctrine, but not through codified law.⁹

Conversely, jurisdictions such as the United Kingdom have statutorily integrated derivative actions into their legislations. The UK Companies Act, 2006 (Sections 260–263) establishes the basis for bringing derivative proceedings¹⁰, the process to be adopted, and the discretion of the court to grant leave. Likewise, in the United States, Rule 23.1 of the Federal Rules of Civil Procedure prescribes derivative actions, providing procedural certainty and equal access.

The absence of such a codified framework in India leads to a number of challenges:

- Uncertainty over thresholds: In the absence of codified procedural norms, courts use varying criteria for granting derivative suits.
- Judicial discretion: Although courts like the NCLAT have been forward-thinking, over-reliance on discretionary authority can bring about subjectivity and inconsistency
- Limited access and awareness: Lack of legislative clarity deters minority shareholders from seeking derivative remedies, particularly where legal advice or precedent is uncertain.

⁷ Varghese George Thekkel, *Tata v. Mistry: A Case for Greater Protection of Minority Shareholders' Rights*, SCC Times, <https://www.sconline.com/blog/post/2021/05/15/tata-v-mistry-a-case-for-greater-protection-of-minority-shareholders-rights/> (last visit July 10 2025)

⁸ Derivative Action as a Right of the Shareholder, Royzz & Co., (last visit July 10 2025) <https://www.royzz.com/post/derivative-action-as-a-right-of-the-shareholder>

⁹ Pratyush Singh, *Derivative Action – Where does the Jurisdiction Lie*, India CorpLaw, (last visit July 10, 2025) <https://indiacorplaw.in/2023/02/07/derivative-action-where-does-the-jurisdiction-lie/>

¹⁰ Companies Act 2006, § 260

- Overloading of the NCLT with request for threshold waiver: Because derivative action is indirectly channelised by the waiver provision in Section 244, they create technical complexity and delay in already technical proceedings.

Codification of derivative action under Indian company law would fill the gap between equitable justice and statutory relief. A formal legislative process can prescribe eligibility, procedural steps, protection against frivolous claims, and jurisdiction powers of courts thereby bringing predictability and safeguarding legitimate claimants.¹¹

CONCLUSION

The development of minority shareholder protection in India has been a gradual balancing between majority control and minority rights. Whereas the Companies Act, 2013 brought much-needed statutory protections through Sections 241 to 246, the inflexible thresholds under Sections 244 and 245 tend to preclude genuine minority concerns from being addressed.

It is in this context that the remedy of derivative action becomes an important equitable remedy covering procedural loopholes, allowing minority shareholders to protect the interests of the company when the controlling wrongdoers are in control, and ensuring that corporate malfeasance does not go judicially unnoticed just due to technical constraints.¹²

Yet, the banking on judicial interpretation to enforce such actions, where legislative endorsement is lacking, produces uncertainty. A codified regime for derivative actions based on global best practices can balance equity and procedure, facilitating uniform access to justice for shareholders, especially in the Indian corporate sector where power tends to rest with the few¹³. In the future, the inclusion of derivative actions in the statute would represent a milestone in India's corporate law regime, one that empowers minority shareholders, enforces corporate democracy, and keeps accountability and fair play at the core of company law.

¹¹ Anuraj Tiwari, Shareholder Derivative Action Suits in India: Avoiding the Influence of Foss v. Harbottle and Taking Cue from the UK Law, SCC Times (last visit July 10, 2025)

<https://www.sconline.com/blog/post/2022/08/10/shareholder-derivative-action-suits-in-india-avoiding-the-influence-of-foss-v-harbottle-and-taking-cue-from-the-uk-law/>

¹² Roopam Dadhich and Sankalp Jain, Contextualising Derivative Action Suits in India, The Competition and Commercial Law Review, <https://www.tccr.com/post/contextualising-derivative-action-suits-in-india> (last visit July 10, 2025)

¹³ Anuraj Tiwari, Shareholder Derivative Action Suits in India: Avoiding the Influence of Foss v. Harbottle and Taking Cue from the UK Law, SCC Times (last visit July 10, 2025)

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