Class-action vs. Derivative Shareholder Lawsuits

When shareholders suffer damages from the corporations in which they hold shares, they can pursue one of two legal remedies. The shareholders can bring a class-action suit, in which multiple plaintiffs belonging to a defined "class" join in a suit against defendants seeking compensation for similar damages. They can also bring a shareholder derivative lawsuit, in which shareholders sue company management on behalf of all shareholders. Each type of legal action has its advantages and drawbacks.

Purposes of Class-action Lawsuits

The main purpose of class-action lawsuits is to allow a group of individuals who have shared a common damage to pursue claims for damages, even when their individual claims would be redundant or insignificant. Class-action lawsuits also serve to eliminate redundancy in the judicial system and to bring efficiency to litigation. For example, when New York law firm Kurzon Strauss, now known as Kurzon LLP, filed class-action lawsuits against two New York law schools for allegedly providing inaccurate post-graduate job data, they brought claims on behalf of dozens of students at these schools.

Requirements of Class-action Lawsuits

Federal Rule of Civil Procedure 23(a) includes four requirements for class-action lawsuits. A major requirement is that the number of parties, either plaintiffs, defendants or both, must be so numerous it would be impractical for each plaintiff to pursue an individual claim. Another requirement is that a common question of law or fact must exist to make it more efficient to hear all the claims at once. A third requirement is that each case must have a common issue, such as product liability. The last requirement is that the class representatives must represent the entire class, rather than individual plaintiffs.

Purposes of Shareholder Derivative Lawsuits

The main purpose of shareholder derivative lawsuits is to allow shareholders to pursue claims against the corporation in which they hold shares. While class-action lawsuits allow a specific group of shareholders to sue the corporation -- for example, shareholders who purchased stock in a particular time period -- a shareholder derivative lawsuit encompasses the interests of all the shareholders. Shareholders frequently bring derivative lawsuits against their corporation as a means of settling disputes between shareholders and corporate management, especially in matters concerning corporate governance and allegations of mismanagement.

Requirements of Shareholder Derivative Lawsuits

Before shareholders can file a shareholder derivative lawsuit, they must first petition the corporation's management to rectify the behavior that prompted the suit. If the management refuses to comply, the shareholders must show that the corporate management's actions were sufficient to hurt their positions and that the corporation refuses remedy the situation. Shareholder derivative lawsuits can also serve to expose potential conflicts of interest within corporate management during the discovery process and show how this behavior damaged the stock value.

About the Author

Living in Houston, Gerald Hanks has been a writer since 2008. He has contributed to several special-interest national publications. Before starting his writing career, Gerald was a web programmer and database developer for 12 years.