Shareholders' Rights to Inspect the Books of the Company

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SHAREHOLDER PROTECTION

Shareholders do not generally have the right to intervene in the management of the company or to have their views considered in relation to the conduct of the company's business. However, they do have the right to vote at general meetings and ultimately to remove the directors if they feel this is warranted.

In this context, the *Corporations Act* 2001 provides some important specific protections for shareholders, such as the right to apply to the Court for an order allowing them to inspect the books of the company. In order to grant such an order, the Court must be satisfied that the applicant is acting in good faith and that the inspection is to be made for a proper purpose.

The directors can authorise a shareholder to inspect the company's books without the need for an application to the Court. However, that provision is of no use to oppressed minority shareholders.

There are a number of cases that have confirmed that in the right circumstances, shareholders are entitled to inspect a company's insurance policies in order to assess the commercial viability of commencing proceedings against the company or its directors.

There has been a recent decision that usefully summarises the principles to be applied by the Court when considering an inspection application.

MESA AND MIGHTY RIVER

The Full Court of the Federal Court delivered judgment on 26 February 2016 in *Mesa Minerals Limited v Mighty River International Limited***.**

Mighty River International Limited had obtained an order to inspect the books of Mesa Minerals Limited ("**Mesa**"), a company listed on the ASX. Since 2010, Mighty River has been a substantial (though minority) shareholder in Mesa.

At the time of its application, Mighty River held over 97 million ordinary shares in Mesa, representing about 15% of its share capital and was second largest shareholder after Mesa's parent company which held 67% of the shares.

Mighty River sought an inspection of books comprised as follows:

- documents relating to the use by third parties of Mesa's port capacity at Utah Point, Port Headland during a specified period, the right to stockpile ore at the Utah Point ore stockyard and to export the stockpile ore through the ore loader, and a general purpose lease at the Boodarie Industrial Estate;
- a Multi User Agreement, together with any amendments, variations or agreements relating to

it, between Mesa, the Port Headland Port Authority and others in relation to the granting of port capacity to Mesa; and

- the Utah Point Facility Agreement, being the agreement between Mesa, the Port Authority and others in relation to the granting to Mesa of the access right.

Mesa submitted that when regard was had to the relevant context, the application was not being made by Mighty River as a member of a company with a genuine concern to protect its investment or with any concern at all as to the use of the port rights. Rather, Mighty River's true or dominant purpose was to use section 247A as an instrument to usurp the powers of Mesa's board to control decisions of the company by obtaining a de facto seat at the board table and/or to extract financial gain from the parent company or the directors.

It argued that, as Mighty River continued to buy shares in the company, its putative concern about its shareholding was either not genuine or Mighty River anticipated a buyout at a premium, and the recent purchases were "an arbitrage". There had also been a delay in bringing the application.

APPLICABLE PRINCIPLES

The Federal Court summarised the principles applicable in determining whether a shareholder should be allowed access to the books:

1. The stipulation that an application be made in good faith and for a proper purpose is a composite notion rather than 2 distinct requirements.

2. Good faith and proper purpose must be proved objectively.

3. "Proper purpose" means a purpose connected with the proper exercise of the rights of a shareholder as shareholder and not, for example, as a litigant in proceedings against the company or as a bidder under a takeover scheme.

4. The onus of proof is on the applicant.

5. An applicant who has a significant holding and who has been a shareholder for "some considerable time" will more easily discharge the onus than one who has recently acquired a token holding.

6. It is not necessary that the applicant show that its interests are different to those of other shareholders.

7. Nor is it necessary that the applicant have sufficient evidence to bring or make out an action. It is enough that the issue raised by the applicant is "substantive and not fanciful", not "artificial, specious or contrived".

8. Pursuing a reasonable suspicion of breach of duty is a proper purpose;

9. Provided that the applicant's primary or dominant purpose is a proper one, it is not to the point that an inspection might benefit the applicant for some other purpose.

10. Applicants do not necessarily lack a proper purpose merely because they are hostile to other directors.

11. Neither the fact that an applicant may have had sufficient information earlier nor the fact that an applicant may have other means of obtaining the information is detrimental to an application under the section.

12. The procedure under section 247A is not intended to be as wide ranging as discovery so that the general rule is that inspection will be limited to such documents as evidence the results of board decisions, rather than all board papers leading to decisions, but there may be occasions when it is proper to permit inspection of board papers.

13. The Court has a residual discretion whether to order inspection.

OTHER POINTS TO NOTE

The Court of Appeal upheld the trial judge's decision to allow the inspection of the books. Points to note from the judgment:

- The factors raised by Mesa to show bad faith on the part of Mighty River were not sufficient. The Appeal Court was not prepared to interfere with the trial judge's findings about credibility or the exercise of his discretion.

- Delay in bringing an application may weigh against the grant of an inspection order if the delay is indicative of acquiescence. Mesa submitted that Mighty River had applied for access to documents previously, based on apparent concerns about Mesa's operations which it had entertained for at least five years before it filed the application. The Court said the fact that Mighty River had been concerned about Mesa's operations for some time tends to support

the conclusion that it was acting in good faith and its purpose was a proper one.

- The Corporations Act does not exclude foreign companies from making an application under section 247A and Mesa conceded there is no authority for the proposition that additional limitations should be placed on foreign investors in Australian companies.

- In relation to the scope of the books to be inspected, the Court said it is not appropriate to allow a wholesale and general inspection of the books. This would cause unnecessary disruption to the company.

- In any event the books to be inspected should be books that bear on, and be particularly relevant to, the purpose for which the inspection is sought.

CONCLUSION

The Court has to strike a balance between the necessity for shareholders to have a real and meaningful ability to keep the directors of the company honest and the legitimate commercial requirements of the company to keep its business affairs confidential.

An applicant seeking an inspection order will have to demonstrate why it is necessary for them to inspect those particular books and be prepared to limit the scope of the inspection to those records that are directly relevant to the issue in question.

Ideally, the terms of access to the books and accounts of a company should be made clear in a properly drafted shareholders agreement, as this will save the company and the shareholder time and money if an inspection is required.

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