

## CG LITIGATION – JULY 2009 BULLETIN

### INSPECTING COMPANY BOOKS

The prevailing economic conditions will undoubtedly lead some shareholders to question the performance of directors and officers of companies in which they have an interest.

Shareholders have a statutory right to inspect a company's books under s 247A of the *Corporations Act 2001* (Cth) (**Corporations Act**). This right needs to be carefully balanced with the interests of a company as regards the disclosure and use of confidential or sensitive information. A shareholder must apply to the court for an order to inspect the company books, and the order will only be made if the court is satisfied the shareholder is acting in good faith and for a proper purpose.

This statutory right was recently considered and somewhat expanded by the Federal Court in *Style Limited, in the matter of; Megrim Pty Ltd v Style Limited* [2009] FCA 314.

#### BACKGROUND

Style Limited (**Style**) was a publicly listed company specialising in the manufacture and distribution of woven bamboo products. The sole director of Merim Pty Ltd (**Merim**), Mr Yunghanns, had become concerned about the conduct of the directors and officers of Style. Style had plans to use money obtained through a capital raising (to which Merim had contributed) to purchase a bamboo plantation in China. Style suffered a downturn in revenue for the financial year 30 June 2008, despite previous encouraging forecasts made to the ASX.

Merim's purpose in applying for an order to inspect Style's books was to investigate whether the directors and officers of Style exercised their powers reasonably, in good faith and for a proper purpose and whether Style's chairman and directors misled Style's members and the market regarding Style's performance. Merim was considering whether to take derivative action against Style, that is, action in Style's name against Style's own directors and officers. Mr Yunghanns had made various requests to Style for information and gave evidence that the responses he received were unsatisfactory.

#### WAS MERIM'S APPLICATION TO INSPECT MADE IN GOOD FAITH AND FOR A PROPER PURPOSE?

Style argued that Merim made the application to inspect in order to assist Merim to gain control of Style. Merim needed to show the Court that it was entitled to inspect the books because the information sought related to matters that it, as a shareholder, ought to have been informed of by Style – and not simply because Merim was questioning the decisions of Style's management.

#### THE COURT'S DECISION

Justice Goldberg of the Federal Court was satisfied that Mr Yunghanns had identified a case for investigation and that the financial issues he had raised regarding Style were substantive and not

fanciful. He was also satisfied that despite some evidence that Mr Yunghanns may have been contemplating action to gain control of Style, his dominant purpose was to inspect the books to assist in making a decision as to whether further action should be taken against Style. His Honour ordered that Mr Yunghanns and a number of his representatives were entitled to inspect the books of Style.

### **DIRECTORS AND OFFICERS LIABILITY INSURANCE POLICIES (D&O POLICIES)**

In addition to financial records, Merim also applied to inspect the D&O policies held by the directors and officers of Style. Even though neither party had included in its submissions previous cases for or against such an inspection, and despite the fact that such an order would be denied under an application for preliminary discovery, His Honour considered that information contained in the D&O policies would be relevant to Merim's decision whether or not to take derivative action, and ordered that Merim be given access to the policies, subject to a restriction on the use of the information.

### **WHAT DOES THIS MEAN FOR BUSINESS**

Shareholders of your business have broader access to company books.

Given the lack of previous authority on point, this decision can be seen as expanding the types of documents which may be made available to shareholders in certain circumstances.

It also affirmed that, even if a shareholder has a number of purposes for wishing to inspect company books, provided the Court is satisfied that the dominant purpose is proper, access will be granted.

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