

Strengthening Stockholders’ Right to Inspect Corporate Records

Rodolfo V. Romero*

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I. PREFATORY STATEMENT

One of the most significant elements in the development of the world economy over the last 300 years has been the evolution of the corporation into the institution that it is known today. Such, indeed, is the importance attached to the role played by the corporation in the world economic development that some economic historians have suggested that the process would not have been as rapid in the absence of the corporate form of business enterprise. Adolf A. Berle, Jr. and Gardiner C. Means have written, for example, that “the true significance of the corporation can best be seen in the light of the development of business in the last three centuries.”¹

* ’79 LL.B., Ateneo de Manila University School of Law. The Author is currently the President & Chief Executive Officer of VIP Communications Ventures, Inc. and a Professor of Law at the Ateneo de Manila University School of Law. His previous works published in the *Journal* include *Towards More Economically Literate Law Graduates*, 24 ATENEO L.J. 42 (1977) and *Stockholder Inspection of Corporate Records: Making Section 51 a More Effective Safeguard*, 22 ATENEO L.J. 41 (1977). He has also written *Governance Without Glory: The Arroyo Administration, 2001-2007*, a book which is comprised of his various articles in *The Daily Tribune*. He was also the Business Editor of the *Manila Bulletin* in the Mid-1960’s.

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1. ADOLF A. BERLE, JR. & GARDINER C. MEANS, *THE MODERN CORPORATION AND PRIVATE PROPERTY* 18-19 (1932).

The evolution of the corporation as the dominant form of modern-day business enterprise has not been confined to the industrial societies, given that, if the relative rate of growth of large corporations were continuously maintained, all corporate wealth would be accounted for in only 200 companies within 50 years, resulting in “a concentration of economic power unknown in the world’s history.”²

The economic development of, what today are referred to as, the developing countries have been characterized by the emergence of the corporation as the dominant form of business enterprise.³ Recent listings of the largest business enterprises in many countries indicate that the economic development of the Philippines has not been the exception to the rule.⁴ In this country, the change in the legal structure of business has necessarily been accompanied by a shift in ownership pattern.⁵

II. INTRODUCTION

The principal factor in the progressive rise of the corporate form of business enterprise to a position of primacy has unquestionably been its ability to widen equity capital base and to provide greater access to financial markets.⁶ When the needs of nations were modest for, what have come to be termed as, infrastructural facilities, production and distribution processes were simple, markets for goods and services were essentially domestic, and the financial requirements of business enterprises were within the capacity of families and small groups of individual to meet.⁷

However, as the development of the entire transportation, power, and communication systems came to be the order of the day, industrial and distribution processes assumed greater complexity and the movement of goods and services became increasingly international in scope, the small-scale, modestly capitalized operation had perforce to give way to the large,

2. *Id.*

3. Ian Lifshitz, Balancing Sustainability with Economic Development in Developing Countries — The Case Study of Indonesia, *available at* <http://www.environmentalleader.com/2010/05/28/balancing-sustainability-with-economic-development-in-a-developing-countries---the-case-study-of-indonesia/> (last accessed Nov. 7, 2010).

4. See BUSINESSWORLD TOP 1000 CORPORATIONS IN THE PHILIPPINES (2009).

5. Florian A. Albuero & Maria Socorro Gochoco-Bautista, Chapter 8. The Philippines: The Underpinnings of East Asian Trade and Investment, *available at* http://www.idrc.ca/en/ev-68160-201-1-DO_TOPIC.html (last accessed Nov. 7, 2010).

6. Lee Drutman, The History of the Corporation, *available at* <http://www.citizenworks.org/corp/dg/s2r1.pdf> (last accessed Nov. 7, 2010).

7. *Id.*

well-financed enterprise.⁸ In legal terms, this transition involved the replacement of the single proprietorship, the family firm, and the partnership by the widely-owned corporation.⁹ In the majority of these instances, the equity capital base required by business enterprises undertaking large-scale industrial and trading operations ceased to be within the capacity of small or closely-held business enterprises to provide.¹⁰ This has been the case as much in the Philippines as in other countries.¹¹

An inevitable concomitant of this change has been the tendency for the ownership of business enterprises to be separated from their control, with the management function performed largely by persons with little or no personal equity stake in the enterprises.¹²

III. THE LEGAL PROBLEM

A. *The Laws Involved*

The key to accepting the idea of a business enterprise in which management is divorced from ownership is the ability of the small stockholder to reassure himself of the sound management of the enterprise whenever he feels a need for such reassurance. By this, investors will continue to buy minority stakes in broadly-owned corporations based on the knowledge that their management can be held to account for their acts by small stockholders as much as by large stockholders. The question of safeguarding of interests in general and of access to information in particular generally does not arise for the largest stockholders. This is understandable. They would, by definition, have holdings sufficient to entitle them to seats on their companies' boards of directors.¹³ If small investors were ever to come to feel that the managements of large corporations could not be made to account for their

8. *Id.*

9. The corporation has become the preferred medium of doing business over and above sole proprietorships and partnerships as "the commercial practice and jurisprudential law governing [such] tend to be more established and reliable." CESAR L. VILLANUEVA, PHILIPPINE CORPORATE LAW 23-24 & 29-41 (2010 ed.).

10. Drutman, *supra* note 6.

11. FRANK H. GOLAY, THE PHILIPPINES: PUBLIC POLICY AND NATIONAL ECONOMIC DEVELOPMENT (1961).

12. Drutman, *supra* note 6.

13. Applying the D'Hondt's Remainders Table as the formula for determining the number of seats that a block of stockholders is certain to have, the majority stockholders would be assured of, at least, one seat in the corporation's board of directors. This number would depend on the number of voting blocks, the voting power per block, and the total number of directors to be elected. See VILLANUEVA, *supra* note 9, at 353-55.

acts, the future of the concept of the corporations as we know it today would be in jeopardy, for such investors would thereafter want to invest their funds only in corporations in whose running they had some say.

Recognizing the implication of such a turn of events for the capacity of corporations to generate capital for expansion — and, therefore, for their industrial development — most countries have passed laws incorporating the right of stockholders to be given access to corporate records and books of accounts, with the right of inspection a condition precedent for the determination of whether or not a basis existed for proceeding against the management of the corporation for wrongdoing.¹⁴ The pertinent provision in the Corporation Code of the Philippines¹⁵ is Section 74, which reads in part as follows —

The records of all business transactions of the corporation and the minutes of any meeting shall be open to the inspection of any director, trustee, stockholder or member of the corporation at reasonable hours on business day and he may demand, [in] writing, for a copy of excerpts from said records or minutes, at his expense.

Any officer or agent of the corporation who shall refuse to allow any director, trustee, stockholder or member of the corporation to examine and copy excerpts from its records or minutes, in accordance with the provision of this Code, shall be liable to such director, trustee, stockholder or member for damages, and in addition, shall be guilty of an offense which shall be punished under Section 144¹⁶ of this Code: *Provided*, that if such refusal is pursuant to a resolution or order of the board of directors or trustees, the liability under this section for such action shall be imposed upon the directors or trustees who voted for such refusal: and *Provided, further*, That it shall be a defense to any action under this section that the person demanding to examine and copy excerpts from the corporation's records and minutes has improperly used any information secured through

14. 18A Am. Jur. 2d *Corporations* § 349 (Westlaw, 2010). In Malaysia, the stockholder's right to inspect records is statutorily provided for by Section 167 (3) of The Companies Act, 1965. The United Kingdom, on the other hand, has Sections 386 to 389 of the Companies Act 2006 with which to govern the exercise of said right.

15. The Corporation Code of the Philippines [CORPORATION CODE], Batas Pambansa Blg. 68 (1980).

16. Section 144 of the Corporation Code provides that —

[v]iolations of any of the provisions of this Code or its amendments not otherwise specifically penalized therein shall be punished by a fine of not less than one thousand (₱1,000.00) pesos but not more than ten thousand (₱10,000.00) pesos or by imprisonment for not less than thirty (30) days but not more than five (5) years, or both, in the discretion of the court.

Id. § 144.

any prior examination of the records or minutes of such corporation or of any other corporation, or was acting not in good faith or for a legitimate purpose in making his demand.¹⁷

It goes without saying that the right of inspection would be of no practical value if there were no corporate records for an inquiring stockholder to inspect, and so there has to be a companion provision requiring corporations to maintain records of all their meetings and business transactions. Thus, Section 74 likewise provides —

Sec. 74. Books to be kept; stock transfer agent — Every corporation shall, at its principal office, keep and carefully preserve a record of all business transactions, and minutes of all meetings of stockholders or members, or of the board of directors or trustees, in which shall be set forth in detail the time and place of holding the meeting, how authorized, notice given, whether the meeting was regular or special, if special its object, those present and absent, and every act done or ordered done at the meeting. Upon the demand of any director, trustee, stockholder or member, the time when any director, trustee, stockholder or member entered or left the meeting must be noted in the minutes; and on a similar demand, the yeays and nays must be taken on any motion or proposition, and a record thereof carefully made. The protest of any director, trustee, stockholder or member on any action or proposed action must be recorded in full on his demand.

...

Stock corporations must also keep a book to be known as the 'stock and transfer book,' in which must be kept a record of all stocks in the names of the stockholders alphabetically arranged; the installments paid and unpaid on all stock for which subscription has been made, and the date of payment of any installment; a statement of every alienation, sale or transfer of stock made, the date thereof, and by and to whom made; and such other entries as the laws may prescribe. The stock and transfer book shall be kept in the principal office of the corporation or in the office of its stock transfer agent and shall be open for inspection to any director or stockholder of the corporation at reasonable hours or business days.¹⁸

B. *The Factual Situation*

On the face of it, the interests of stockholders, particularly of small stockholders, seem to be well-protected. So long as he does so at *reasonable hours*, that is to say, the hours of the day during which the corporation regularly conducts business,¹⁹ the stockholder may inspect the records on "*all*

17. *Id.* § 74, ¶¶ 2 & 3.

18. *Id.* § 74, ¶¶ 1 & 4.

19. Reasonable hours have been defined as "reasonable hours on business days throughout the year, and not merely during some arbitrary period of a few days chosen by the directors." *Pardo v. Hercules Lumber Co. and Ferrer*, 47 Phil. 964, 966 (1924).

business transactions and [the] minutes of *all meeting of directors, members or stockholders*,”²⁰ which a corporation is required to keep along with a record of changes in its ownership.²¹ Section 74 does not speak of the records of some transactions and some meetings being open to the inspection of any director or stockholder; it speaks, rather, of a director or a stockholder having the right to inspect the records of each and every business transaction of the corporation and each and every meeting of its directors and stockholders. It would seem entirely reasonable to infer from the wording of the above-quoted provision that any stockholder with doubts about the way in which the affairs of his corporation were being conducted would expect in every instance to be given the records of its deliberations and transactions.

Expectation and reality are not always one and the same thing. In practice, it is by no means a certainty that the management of a doubting stockholder’s corporation would allow him, in every instance, either to prove his doubts baseless or to confirm them. More to the point, upon demand, the average stockholder is likely to find himself denied access to the corporate records that he wishes to examine; that this is the factual situation is not altogether difficult to comprehend.²²

The reason why corporate managements are in most cases reluctant and/or unwilling to allow stockholders to examine corporate record lies in the very nature of the action.²³ A person who exercises his right under Section 74 is, in the very nature of things, almost certain to be a person seeking either reassurance or confirmation. If he were satisfied with the picture of the corporation presented by the information made available by management on a normal basis, i.e., in annual, semi-annual and quarterly reports, or if he had no reason to believe that all might not be well with the manner in which the corporation was being run, he would not be asking that he be allowed to inspect the corporation’s records.²⁴ A reasonable inference from a stockholder’s desire to exercise his visitorial right, therefore, is either that he wants to be reassured that the picture of operations made available by the

20. CORPORATION CODE, § 74, ¶ 1 (emphasis supplied).

21. Securities and Exchange Commission, Revised Code of Corporate Governance, SEC Memorandum Circular No. 6, Series of 2009 [SEC Memo. Circ. No. 6], art. 8 (June 22, 2009).

22. See, e.g., Philippines’ GSIS Asks Stock Exchange to Suspend Metro Pacific, BLOOMBERG, Nov. 20, 2009, available at <http://www.bloomberg.com/apps/news?pid=21070001&sid=alpthuy6owEA> (last accessed Nov. 7, 2010).

23. The nature of the stockholder’s right to inspect draws itself from “his ownership of shares in the corporation and the necessity for self-protection.” *Puno v. Puno*, 599 SCRA 585, 591 (2009).

24. *Gokongwei, Jr. v. Securities and Exchange Commission*, 89 SCRA 336, 383 (1976).

management is the true picture or that he seeks confirmation for any unfavorable or baseless information that may have come to his knowledge.²⁵

Given these possibilities, all but the most self-assured and the most image-conscious of corporations, when confronted with a demand for the exercise of the right to inspect corporate records, would prefer to run the risk of a petition for a *mandamus* order²⁶ — the appropriate legal remedy in such a situation²⁷ — than to accede to the inquiring stockholder's demand. Stated differently, unless a corporation's management is absolutely certain that the inspection of corporate records will yield nothing damaging to the corporation or unless it is so sensitive about the corporation's public image that it would do anything to avoid a situation with bad-publicity potential, it will run the risk of a *mandamus* order rather than allow a stockholder to exercise his right under Section 74.

Even some corporate leaderships that can be said to meet the criteria of sound management, when confronted by a demand for the exercise of a stockholder's visitorial right, tend to take the view that there could be danger in allowing a stockholder to examine corporate records, it being possible that at one time or another, the corporation wittingly or unwittingly performed acts of a questionable nature, or was otherwise involved in such acts, there being no telling what will be done with such information by a stockholder who comes upon it in the course of his inspection of corporate records.²⁸ Given such a perceived danger, refusing to allow a stockholder to exercise his visitorial right is considered by many, otherwise well-managed corporations, to be the preferred course to take. As for corporations which operate in an unsound manner, stockholders obviously cannot expect to be granted access to their records; the management of such corporations really would have no choice but to deny them access.

What the foregoing discussion comes down to is that, whereas in theory, the right of the stockholder — and particularly that of the small stockholder — to determine for himself the condition of his stake in a corporation

25. *Id.* at 384 (citing 5 FLETCHER'S CYCLOPEDIA FOR CORPORATIONS, *Private Corporations* § 2223 (1976)).

26. 1997 RULES OF CIVIL PROCEDURE, rule 65, § 3.

27. *Uy Kiao Eng v. Lee*, 610 SCRA 211, 216-17 (2010) (citing *Abaga v. Panes*, 531 SCRA 56, 61-62 (2007)).

28. Eric Fryar, Shareholder Rights to Inspect Records, *available at* http://www.shareholderoppression.com/right_of_inspection (last accessed Nov. 7, 2010). Also, *see, e.g., Uvalde Rock Asphalt Co. v. Loughridge*, 425 S.W.2d 818, 819-20 (Tex. 1968) (U.S.); *News-Journal Corp. v. State ex rel. Gore*, 187 So. 271, 272 (Fla. 1939) (U.S.); & *State ex rel. Beaty v. Guarantee Mfg. Co.*, 174 P. 459, 460 (Wash. 1918) (U.S.), where the denial of the right to inspect records was due to the fact that the information sought to be obtained was to be used for the competitor's advantage.

appears assured, in practice his being able to exercise it tends to be the exception rather than the rule.

The most common grounds for denying access to corporate records are the demanding stockholder's probable antipathy toward the corporation or any of its officers and directors and his perceived intent to use whatever unfavorable information he may come across to embarrass the corporation.²⁹ Another ground on which stockholders are denied the exercise of their visitatorial right is the suspicion that they are motivated by an intent to get a hold of the corporation's secrets, particularly those of a trade or technological nature.³⁰ In some instances, the allegation made is that the stockholder seeking access to corporate records is prompted by nothing more than idle curiosity.³¹ Whatever be the basis for the denial of his visitatorial right, the effect of such denial on the stockholder is the same, to wit, the effective frustration of a right granted to him by law.

Unfortunately, a stockholder denied of his right to inspect corporate records has no choice but to go to court; many stockholders bent on exercising this right have done so. Litigation is hardly ever a short process, and by the time the courts have reached a final judgment on the merits of a *mandamus petition*, the inspection-refusing corporation will have accomplished its defensive purpose.³²

IV. JURISPRUDENCE

A. Domestic Jurisprudence

Accordingly, there is not an abundance of domestic jurisprudence on the issue of a stockholder's right to inspect a corporation's records. What jurisprudence there is tends to support the view expressed above. In a leading case it was held that —

pretexts may not be put forward by officers of corporations to keep a director or shareholder from inspecting the books and minutes of the corporation, and the right of inspection may be denied on the ground

29. Republic v. Sandiganbayan, 199 SCRA 39, 47 (1991).

30. 18A Am. Jur. 2d *Corporations* § 349 (Westlaw, 2010); see generally *Gokongwei, Jr.*, 89 SCRA 336 (1976).

31. M. E. Grey v. Insular Lumber Co., 67 Phil. 139, 142 (1939) (citing 14 C. J., 854, 855).

32. On one hand, for civil cases, litigation may take up to six to eight years. On the other hand, criminal cases may take up to three years. JAMES L. NOLAN, PHILIPPINE BUSINESS: THE PORTABLE ENCYCLOPEDIA OF DOING BUSINESS IN THE PHILIPPINES 218 (1996).

that the director or shareholder is on unfriendly terms with the officers of the corporation whose records are sought to be inspected.³³

But in three other leading cases, a limitation was placed by the Court on the exercise of the right. Thus, in *Philpotts v. Philippine Manufacturing Co. and Berry*,³⁴ which involved a process of utility not known to all, the Supreme Court held that "there are some things which a corporation may undoubtedly keep secret, notwithstanding the right of inspection given by law to the stockholder[.]"³⁵

In *Acuña v. Parlatone Hispano-Filipino*,³⁶ the Court of Appeals held that a stockholder's right of inspection may be denied when the examination for improper ends prejudicial to the corporation.³⁷ And in *Grey v. Insular Lumber Co.*,³⁸ the right of inspection was denied by the Court partly on the ground that the stockholder failed to show that the inspection was for the protection of his interests and not merely for the satisfaction of his curiosity or for speculative purposes.³⁹

Moreover, in *Teodoro v. Warns*,⁴⁰ the Supreme Court pointedly stated that while *mandamus* is the legal remedy, its issuance may be denied by the discretion of the courts.⁴¹

From the foregoing it can be seen that refusal to allow a stockholder to inspect a corporation's records by no means always results in the issue of a *mandamus* order.

B. Foreign Jurisprudence

In countries with legal systems founded on common law, there is no shortage of jurisprudence relating to the exercise of the stockholder's right of inspection, and there is, with regard to the right of inspection, a greater incidence of litigation in those countries than in countries whose legal systems have different foundations.⁴² Why this is so was explained by the

33. *Veraguth v. Isabela Sugar Co. et al.*, 57 Phil. 266, 270 (1932).

34. *Philpotts v. Philippine Manufacturing Co. and Berry*, 40 Phil. 471 (1919).

35. *Id.* at 474.

36. *Acuña v. Parlatone Hispano-Filipino*, 40 O.G. 283 (Court of Appeals 1940).

37. In this Case, the decision of the Court of Appeals is in Spanish. *See State v. Monida & Y. Stage Co.* 11 Minn. 193, 200-01 (1910) (U.S.).

38. *M. E. Grey v. Insular Lumber Co.*, 67 Phil. 139 (1939).

39. *Id.* at 142.

40. *Teodoro v. Warns*, G.R. No. L-9886, July 24, 1957.

41. *Id.*

42. Preference for common law jurisdiction with regard to corporate law litigation is based on "predictability of outcome, legal certainty, and fairness." Also, the preference can be attributed to its "ability to require exact performance and the

Supreme Court of the United States (U.S.) in one of the leading cases in that jurisdiction. The Court said that

[i]t is well established that a stockholder has a right to inspect the books and records of the corporation. This right has been said to exist independently of statutes securing such a right to stockholders, and such statutes are generally regarded as supplementing, rather than abrogating, the common-law right.

The common-law right of a stockholder to inspect corporate books and records is not, however, an absolute right; it must be exercised at a proper and reasonable time and place, and for a proper purpose.⁴³

This view was echoed by the Supreme Court of Delaware in *Saito v. McKesson HBOC, Inc.*⁴⁴ That Court said —

Stockholders of Delaware corporations enjoy a qualified common law and statutory right to inspect the corporation's books and records. Inspection rights were recognized at common law because, '[a]s a matter of self-protection, the stockholder was entitled to know how his agents were conducting the affairs of the corporation of which he or she was a part owner.'⁴⁵

The highest tribunal of Kentucky said in *Otis-Hidden Co. v. Scheirich*⁴⁶ that, "[t]he stockholder's right of inspection is founded on his beneficial interest through ownership of shares and the necessity of self-protection ... to ascertain how the affairs of [the] company are being conducted by its directors and officers."⁴⁷

However, like its Philippine counterpart, American jurisprudence in the matter of the right of stockholders to inspect the records of a corporation holds that the right of stockholders in demanding its exercise tends to be

absence of any general duty of good faith." Lord Falconer of Thoroton, Address at European Contract Law Conference (Sep. 26, 2005), transcript available at <http://www.dca.gov.uk/speeches/2005/lc150905.htm> (last accessed Nov. 7, 2010). See also Yeo Teong Min, A Note on Some Differences in English Law, New York Law, and Singapore Law, available at <http://www.singaporelaw.sg/content/SomeDifferences.html> (last accessed Nov. 7, 2010) & Theodore Eisenberg and Geoffrey P. Miller, The Flight to New York: An Empirical Study of Choice of Law and Choice of Forum Clauses in Publicly-Held Companies' Contracts, available at http://lsr.nellco.org/cgi/viewcontent.cgi?article=1128&context=nyu_lewp (last accessed Nov. 7, 2010).

43. 18A Am. Jur. 2d *Corporations* § 348 (Westlaw, 2010).

44. *Saito v. McKesson HBOC, Inc.*, 806 A.2d 113 (Del. 2002) (U.S.).

45. *Id.* at 116 (citing *Shaw v. Agri-Mark, Inc.*, 663 A.2d 464 (Del.1995) (U.S.)).

46. *Otis-Hidden Co. v. H. J. Scheirich*, 219 S.W. 191 (Ky. 1920) (U.S.).

47. *Id.*

tainted with impropriety.⁴⁸ This was entirely to be expected, considering that the Corporation Law of the Philippines⁴⁹ had an American progenitor.⁵⁰

The prevailing doctrine in U.S. jurisprudence on improper exercise by stockholders of the right to inspect corporate records has been stated in the following terms —

The paramount factor in determining whether a stockholder is entitled to inspection of corporate books and records is the propriety of the stockholder's purpose in seeking such inspection.

...

[T]he Court may deny inspection where the shareholder is shown to have possession of all the information that is requested, or where the request is made out of sheer curiosity, unrelated to any legitimate interest of the stockholder, or where the sole purpose of the inspection is to harass the corporation.⁵¹

Denying the right to inspect corporate books and records was sustained where there was a showing that the inspection was due to hostile motives so as to embarrass the corporation, injure the value of its assets by depressing the rate of its shares, and cause demoralization and dissention among its members.⁵²

V. DISCUSSION AND CONCLUSION

From the foregoing exposition, a number of points may be deduced. These are: (1) that it is by no means certain that a stockholder wishing to inspect the books of a corporation will be allowed to do so; (2) that the right to inspect such books may be denied on a variety of grounds, including bad faith; (3) that even *bona fide* stockholders desiring to exercise their right of inspection for perfectly legitimate reasons can be accused of bad faith by the corporate managements concerned; (4) that substandard corporate managements can deny stockholders their right of inspection, alleging bad

48. *Seinfeld v. Verizon Communications, Inc.*, 909 A.2d 117, 118 (Del. 2007) (U.S.) (citing *Security First Corp. v. U.S. Die Casting & Dev. Co.*, 687 A.2d 571 (Del. 1997) (U.S.)).

49. An Act Providing for the Formation and Organization of Corporations, Defining Their Powers, Fixing the Duties of Directors and Other Officers Thereof, Declaring the Rights and Liabilities of Shareholders and Members, Prescribing the Condition Under Which Such Corporations May Transact Business, and Repealing Certain Articles of the Code of Commerce and All Laws or Parts of Laws in Conflict or Inconsistent With This Act [Corporation Law], Act No. 1459 (1906).

50. *See Harden v. Benguet Consolidated Mining*, 58 Phil. 141, 145-46 (1933).

51. *CM & M Group, Inc., v. Carroll*, 453 A.2d 788, 792 (Del. 1982) (U.S.).

52. 18A Am. Jur. 2d *Corporations* §§ 383, 344 (Westlaw, 2010).

faith; and (5) that the burden of establishing the nature of the stockholder's motive in wanting to inspect a corporation's books does not rest on the latter solely, i.e., there must also be a showing of *bona fides* on the part of the stockholder.

In other words, there is no guarantee, indeed there is every possibility, that a *bona fide* stockholder wishing to inspect the records of a corporation for perfectly legitimate reasons will be prevented by its management from exercising that right on the ground that he is improperly motivated and the stockholder has to establish that his intention in seeking to exercise his right of inspection is *bona fide*, or, more to the point, is not *mala fide*.

The conclusion to which this inevitably leads is that, contrary to the dictate of Section 74 of the Corporation Code, the records of all the business transactions of a corporation and the minutes of any of its meetings are not always *open to inspection*, during reasonable hours, by any of its directors, members, or stockholders.⁵³ Indeed, one can go further and say that the records of corporations are, in the majority of instances, not open to the inspection of their directors, members, or stockholders. The basis for this belief, as already stated, is the very nature of the act of seeking to exercise the right of inspection.

Domestic and foreign jurisprudence on the question of stockholder inspection of corporate records show that such inspection is at times sought to satisfy idle curiosity or for some other trivial reason;⁵⁴ and it is virtually certain that in the days to come inspection will in some cases be sought on such basis. But when allowance has been made for such instances, it can be stated, as a general rule, that a stockholder's asking to be shown the records of the corporation is indicative of one of two things. At best, it indicates that the stockholder would like to obtain confirmation of one or more elements of the corporation's operations, e.g., a particular financial transaction or particular transactions of the corporation. At worst, it indicates that the stockholder is suspicious of wrongdoing on the part of the directors and/or officers of the corporation.

In both cases, the implication is that a stockholder is no longer prepared to accept at face value all the representations of its management, which in the case of publicly-held corporations, includes the data contained in financial statements that the law requires to be published.⁵⁵

53. *Contra* CORPORATION CODE, § 74, ¶ 2.

54. See generally *Pillsbury v. Honeywell*, 191 N.W.2d 406 (Minn. 1971) (U.S.); *Republic v. Sandiganbayan*, 199 SCRA 39 (1991); *Republic*, 199 SCRA 39; & *Veraguth*, 57 Phil. at 270.

55. Section 75 of the Corporation Code governs the stockholder's right to the financial statements which should include "a balance sheet at the end of the last taxable year and a profit or loss statement for said taxable year showing in

It is unrealistic to hold that most managements are incapable of appreciating the implications of a stockholder's asking to be shown the records of the corporation and not being allowed to inspect them. It is equally unrealistic to believe that they regard with no sense of anxiety the possibility that in the course of his inspection, the stockholder might come across data unflattering to the corporation or, worse, the possibility that he might use the data in a manner unfavorable to the corporation.

There is, in fact, general appreciation of the real meaning of a move to exercise the right embodied in Section 74 of the Corporation Code and of the implications of allowing it, and because there is such appreciation, the managements of most corporations cannot realistically be expected to allow the inspection of their records by stockholders capable of hostile action.⁵⁶ Corporations which operate on a consistently impeccable basis have, by definition, nothing to hide from anyone and prize the good public image that goes hand in hand with a taint-free existence; accordingly they are not disposed to do anything which has potential for public-image impairment. Conducive as such an action would be to public belief that their operational record was not unquestionable, such corporations regard with disfavor the idea of not allowing stockholders to inspect their books and records. But corporations that operate strictly according to law, and therefore can withstand scrutiny, are bound to be the exception rather than the rule. If this judgment is correct — if, that is to say, the majority of corporations operate in a manner that renders them unwilling to maintain a policy of total openness — it follows that most stockholders are likely to continue to be unable to exercise the right embodied in Section 74 of the Corporation Code.

VI. RECOMMENDATION

As stated at the outset, the wording of Section 74, and particularly its second paragraph, is such as to create an impression of security of a stockholder's right to inspect the records of all the business transactions of the corporation and the minutes of all its meetings. However, as the preponderance of both domestic and foreign jurisprudence indicates, such security is more apparent than real. For this, the explanation has to be found in the wording of Section 74.

reasonable detail its assets and liabilities and the result of its operations." CORPORATION CODE, § 75.

56. See, e.g., *Uvalde Rock Asphalt Co.*, 425 S.W.2d at 819-20; *News-Journal Corp.*, 187 So. at 272; & *State ex re. Beaty*, 174 P. at 460, where the denial of the right to inspect records was due to the fact that the information sought to be obtained was to be used for the competitor's advantage.

Section 74 requires that all business corporations *keep and carefully preserve* a detailed record of *all business transactions and minutes of all meetings of directors, members, or stockholders* and keep such a record *open to the inspection of any director, member, or stockholder of the corporation at reasonable hours*. The phraseology of the first requirement gives rise to no problems of implementation. Which business corporations are subject to the record-keeping requirement, what business transaction and minutes have to be recorded, and how the record-keeping has to be done are clearly spelled out.

All business corporations are required to keep and preserve *carefully* a record of *all* business transactions of the corporation and minutes of *all* meetings of directors, members, and stockholders. This, it need hardly be added, is as it should be; for it would be impossible for interested parties, including the government, to obtain a true picture of a corporation's operations on the basis of an incomplete record of corporate transactions.

What gives rise to difficulties in the implementation of Section 74 is the way in which its second requirement is worded. Provided that it is *done at reasonable hours*, any director, member, or stockholder of the corporation may conduct an inspection of the *records of all business transaction of the corporation and the minutes of any meeting*. The grant of the right of inspection is all-embracing — any *director, member, or stockholder* of the corporation — and all its directors, members, and stockholders, have the right to inspect the corporation's books. Considering that not all inspections are *bona fide* and that some stockholders who seek access to corporate records do so for reasons that have nothing to do with a legitimate protection of interests, a grant of the right of inspection that is indiscriminate clearly cannot be justified; and because it is their duty, in cases where a literal interpretation would give rise to injury, to apply the law in a protective manner, the courts have, of necessity, had to qualify *any director, member, or stockholder* so as to limit the right to inspect corporate records to directors, members, and stockholders who exercise the right *bona fide*.

The net result has been that, instead of serving to effectively safeguard what is almost certainly the most important of the inherent rights of a part-owner of a corporation, Section 74's second requirement as now worded has in practice worked to render uncertain the ability to exercise the right of inspection without judicial intervention.

This ironic outcome would have been avoided if, instead of a blanket approach to the protection of a stockholder's access to corporate records, the authors of the Corporation Code had adopted one that accorded due recognition to the fact that some grounds for refusal to allow inspection of corporate records are meritorious and of the fact that certain elements of a corporation's records are of a nature that renders them inappropriate objects

of stockholder inspection.⁵⁷ Thus, if they had worded Section 74 so as to remove from the ambit of its protection stockholders seeking access to corporate records *mala fide* and to place beyond inspectability corporate documents of a demonstrably confidential nature, they might very well be more disposed to limit the grounds for not allowing stockholder inspection of such records to cases involving a clear and ascertainable threat to the existence of the corporation.⁵⁸ In an age of rampant industrial espionage, the courts have unquestionably been right in upholding the right of a corporation to withhold the right of inspection from a stockholder who has a record of, or is strongly suspected to be engaged in, industrial espionage.⁵⁹

It is difficult to reach the same judgment in those cases where courts have ruled in favor corporations on the ground that the stockholder seeking access to the corporate records was not on friendly terms with some or all of the officers and directors, considering that failure on the part of the latter to furnish information on particular aspects of the corporation's operations may in fact have been the cause of the rise of unfriendly relations between them.⁶⁰ The same observation applies to those instances where courts have refused to grant a *mandamus writ* on the ground that in seeking access to the records of the corporation the stockholder was motivated by idle curiosity or by a desire to give vent to a vexatious disposition.⁶¹ Such an attitude is tantamount to saying that as a part-owner of the corporation the stockholder has the right to take whatever steps necessary to ensure its proper management but that it may be exercised only if the stockholder has a personality and a disposition that the management of the corporation considers acceptable.⁶²

Had the authors of the Corporation Code drawn a clear line, the Court would very probably have been far less prone to decide Section 74 cases in a manner suggesting belief that anything not demonstrably *bona fide* must be tainted with malice or mischievous intent.

If, then, Section 74 is in the future to be a more effective protector of the interests of stockholders without, in the process, placing in jeopardy the legitimate interests of corporations, its last sentence should be reworded to read as follows: "The record of all business transactions of the corporation and of minutes of all meetings of directors, members, or stockholders, *with the exception of all data relating to or forming part of technical processes and*

57. 18A Am. Jur. 2d *Corporations* § 363 (Westlaw, 2010).

58. *Id.* § 383.

59. *Id.* § 385.

60. *American Mortg. Co. v. Rosenbaum*, 151 N.E. 122 (1926) (U.S.).

61. *In re Steinway*, 159 N.Y. 250, 263 (N.Y. 1899) (U.S.).

62. On this particular point, see *Veraguth*, 57 Phil. at 270.

*technologies, whether belonging to the corporation or to its affiliates and clients, shall be open to the inspection, at reasonable hours, of any director, member, or stockholder unless there is a showing that information is being sought for the benefit and use of the corporation's competitors or that the director, member, or stockholder seeking to exercise the right of inspection has a record of malicious or vexatious conduct."*⁶³

The adoption of the above wording can be expected to go a long way toward eliminating the suspicion and fear that has prevented many would-be investors from contributing to the further development of corporate ethics in the Philippines, with all the implications of this for the Philippines' future economic development.

63. *Contra* CORPORATION CODE, § 74, ¶ 2.