August 20, 2010

New Jersey Appellate Court Holds that Shareholders May Gain Access to Minutes of the Board of Directors and Executive Committees Upon Proof of a 'Proper Purpose'

On August 17, 2010, the New Jersey Appellate Division ruled in a case of first impression that under the New Jersey Business Corporation Act, N.J.S.A. 14A:5-28(4), shareholders are entitled to inspect not only minutes of shareholders meetings but also the minutes of meetings of the board of directors and of executive committees, *provided* the shareholders present sufficient credible evidence of a "proper purpose" for accessing the records. *Cain v. Merck & Co*., Dkt. No. A-2138-08T2, 2010 N.J. Super. LEXIS 170 (App. Div. Aug. 17, 2010). However, shareholders' examination must be limited to only those portions of the minutes that address their "proper purpose." *Id.* at *21-22. Shareholders are not permitted to examine minutes simply to explore "unsubstantiated allegations of general mismanagement." *Id.* Plaintiffs, owners of eleven shares of common stock of defendant Schering-Plough Corporation ("Schering"), filed a shareholder-derivative complaint in federal court against Schering, its board of directors, and certain executive officers. The complaint alleged corporate mismanagement and wrongdoing in connection with the allegedly delayed disclosure of the results of a clinical trial known as the ENHANCE study. Plaintiffs made a written demand to inspect certain books, minutes, and records of the company "germane to our interest as Shareholders to review the manner in which the Company is being managed," pursuant to N.J.S.A. 14A:5-29(4). Plaintiffs subsequently clarified their purpose in seeking the documents, alleging that Schering had engaged in wrongful conduct that harmed investors and others when it delayed "for twenty-one months the release of the results of the ENHANCE trial." *Id*. at *3-4. Ultimately, plaintiffs commenced an action in New Jersey state court and obtained an order compelling Schering to provide "any non-privileged portions of the minutes of and any documents made part of the minute books for meetings of the Company's Board of Directors and Executive Committee." *Id*. at *4-5. On appeal, Schering contended that N.J.S.A. 14A:5-28 did not apply to the minutes of a corporate board of directors or its executive committee, and even if it did, examinations should have been limited to documents relevant to the shareholders' proper purpose, which was regarding the ENHANCE trials. *Id*. at *5-6. Plaintiffs asserted that they were entitled to inspect Schering's books and records "to learn the depth and breadth of mismanagement" and that this was a "proper purpose." *Id*. at *17. In a case of first impression, after reviewing the legislative history of the statute and based upon statutory construction principles, the Appellate Division broadly defined the meaning of the term "minutes" in N.J.S.A. 14A:5-28(4) to include not only shareholder meeting minutes but also board and executive committee meeting minutes. *Id.* at *16.? However, the Appellate Division found the trial court's order overly broad. *Id.* at *17-23. After considering Delaware and older New Jersey case law, the Appellate Division reaffirmed "that unsupported allegations of mismanagement do not present a 'proper purpose' entitling a shareholder to examine corporate documents." *Id.* at * 21. A proper purpose does not include suspicion or curiosity. *Id.* at *18-19. "Any other rule would further a 'fishing expedition' with the attendant unnecessary costs and potential harm to the corporation." *Id*. at *21-22.