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<td><strong>Citation</strong></td>
<td>Li, F. C. (2012). Corporate governance through disclosure: Inspection of company records by shareholders in Hong Kong (Outstanding Academic Papers by Students (OAPS)). Retrieved from City University of Hong Kong, CityU Institutional Repository.</td>
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<td><strong>Issue Date</strong></td>
<td>2012</td>
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<td><strong>URL</strong></td>
<td><a href="http://hdl.handle.net/2031/6857">http://hdl.handle.net/2031/6857</a></td>
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Corporate Governance through Disclosure: Inspection of Company Records by Shareholders in Hong Kong

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LL.B. 2008/12

Paper for

Outstanding Academic Papers by Students 2013
The Hong Kong court passed the first order allowing inspection of company records under section 152FA of the Companies Ordinance (Cap. 32) in August 2011. This has triggered shareholders’ interest in inspecting company records to investigate mismanagement which they have suspicion. Although the legislation providing for such right of inspect was enacted in 2005, the Hong Kong courts have only discussed this statutory right on a few occasions. Nevertheless, a significant amount of court jurisprudence is available for its counterparts in Australia and the United States. This article aims to provide a comparative analysis of section 152FA with the corresponding law in Australia and the United States, in particular the requirements of ‘good faith’ and ‘proper purpose’ under section 152FA(3), and to discuss its potential impact on corporate governance in Hong Kong.

The law stated in this article is accurate as of April 2012.

† This article was originally published in Macquarie Journal of Business Law, Volume 9, 51–64 (2012).
I. INTRODUCTION

While Hong Kong has recently been ranked first among other major global financial centres in the Financial Development Index 2011 for its excellent business environment, it ranked only 17th for protection of minority shareholders’ interests and recorded a drop in the score for corporate governance when compared with 2008. Nevertheless, the Hong Kong Government has always been trying to promote corporate governance in Hong Kong, and the Companies (Amendment) Bill 2004 (‘2004 Bill’) in fact represented a great leap forward in this regard. Among the various insertions made by the 2004 Bill, section 152FA of the Companies Ordinance (Cap. 32) (‘section 152FA’), which allows a member of a company to seek a court order for inspection of documents of the company, started gaining attention after the first inspection order was granted in August 2011.

There are currently three reported decisions by the Hong Kong courts which examined section 152FA in detail; they are Wong Kar Gee Mimi v Hung Kin Sang Raymond decided by the Court of First Instance of the Hong Kong High Court (where the inspection was allowed), and Re LehmanBrown Ltd decided by the Court of First Instance and affirmed by the Court of

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2 Corporate governance, for instance, was identified as one of the four aims in Phase I of the rewrite of the Companies Ordinance in early 2011; see Legislative Council, Legal Service Division Report on Companies Bill, LC Paper No. LS26/10-11 (11 February 2011) paras. 9-10.
3 See below note 5.
4 There was a decision in 2007, Hotung v Ho Yuen Ki [2007] 4 HKLRD 384 (HK CA), which touched upon the scope of ‘records’ in the Companies Ordinance, s 152FA(1).
5 [2011] 5 HKLRD 241 (HK Ct of First Instance) (‘Wong Kar Gee’). This decision was handed down by Harris J on 30 August 2011.
6 [2011] 4 HKLRD 237 (HK Ct of First Instance) (‘Re LehmanBrown in CFI’). This decision was handed down by Coleman DHCJ on 13 July 2011.
Appeal\textsuperscript{7} (where the inspection was refused). Although the jurisprudence encompassing this section is still developing in Hong Kong, similar provisions can be found in Australian\textsuperscript{8} and American\textsuperscript{9} law, which have been explored thoroughly by their courts.

The purpose of this article is to analyse the potential development of the criteria adopted by the Hong Kong court in respect of the inspection of company records under section 152FA in the light of Australian and American law. The analysis focuses on the requirements of ‘good faith’ in section 152FA(3)(a) and ‘proper purpose’ in section 152FA(3)(b). It will be concluded with a discussion of how such inspection of company records may enhance corporate governance.

II. \textbf{Elements of Section 152FA}

Section 152FA is the essential operative section in the inspection regime, which provides that:

\textsuperscript{7} [2011] 5 HKLRD 668 (HK CA) (‘\textit{Re LehmanBrown}’). This decision was handed down by Chu JA (Suffiad and Bharwaney JJ concurred) on 3 October 2011. Regrettably, as the date of hearing was 11 August 2011, the Court did not have the opportunity to consider Harris J’s judgment in \textit{Wong Kar Gee} [2011] 5 HKLRD 241.

\textsuperscript{8} Australian law is of particular importance as section 152FA is modelled on the Australian Corporations Act 2001 (Cth), s 247A; see Legislative Council, \textit{Report of the Bills Committee on Companies (Amendment) Bill 2003}, LC Paper No. CB(1)2264/03-04 (7 July 2004) para. 82 (the proposed section 152FA(2) is corresponding, but not equivalent, to the enacted section 152FA(3)).

\textsuperscript{9} American law in this regard varies across different states as the ways their statutes are formulated, or even the source of the power to inspect, are different; see 5A Fletcher Cyclopedia of the Law of Corporations § 2219. For instance, while the statute in Connecticut has drawn a clear distinction between ‘good faith’ and ‘proper purpose’ (see Connecticut General Statutes § 33-946; \textit{Pagett v Westport Precision Inc} 845 A 2d 455 (2004), 459-60 (Flynn J)), Illinois law considers ‘good faith’, together with ‘honest motive’ and ‘seeking to protect the interests of the corporation as well as the shareholder’, as an element under ‘proper purpose’ (see Illinois Business Corporation Act of 1983 § 7.75; \textit{Hess v Reg-Ellen Machine Tool Corporation} 423 F 3d 653 (CA(7\textsuperscript{th}Cir) of US 2005), 666 (Rovner J)).
(1) Subject to sections 152FD and 152FE, on application by such number of members of a specified corporation as is specified in subsection (2) (in this section referred to as “applicant”), the court may make an order—

(a) authorizing the applicant or any one or more of such members applying as applicant to inspect any records of the specified corporation; or

(b) authorizing a person (whether or not a member of the specified corporation) other than the applicant to inspect any such records on behalf of the applicant.

(2) For the purposes of subsection (1), an application may be made by—

(a) any number of members representing not less than one-fortieth of the total voting rights of all members having at the date of the application a right to vote at a general meeting of the specified corporation;

(b) any number of members holding shares in the specified corporation on which there has been paid up an aggregate sum of not less than $100000; or

(c) not less than 5 members.

(3) The court may only make an order under subsection (1) if it is satisfied that—

(a) the application is made in good faith; and

(b) the inspection applied for is for a proper purpose.

(4) Any person who is authorized by the court to inspect the records of a specified corporation may make copies of the records unless the court orders otherwise.

(5) A person who complies with an order made under this section or section 152FB to produce records for inspection shall not be liable for any civil liability or claim whatever to any person by reason only of that compliance.

As the other parts of the inspection regime, section 152FB provides that the court may make other ancillary orders. Section 152FC restricts the applicant’s use of the information disclosed by the company. Sections 152FD and 152FE restrict the applicant from accessing information subject to legal professional privilege and protection of personal data respectively.
A. Common Law Position Compared

Such right of inspection in circumstances where there might be mismanagement within the company is not created by section 152FA out of thin air, as the section only ‘codifies and expands upon the common law right of a company’s members to examine the company’s records.’\(^{10}\) Dating back to the 1830s in *R v Master and Wardens of the Merchant Tailors Co.*,\(^ {11}\) Littledale J held that:

> The master and wardens, who have the care of the documents in question, are bound to produce them if a proper occasion is made out, in a matter affecting the members of the corporation. But I think the members have no right on speculative grounds to call for an examination of the books and muniments, in order to see if by possibility the company’s affairs may be better administered than they think they are at present.\(^ {12}\)

The ‘proper occasion... in a matter affecting the members of the corporation’ referred to by Littledale J corresponds to the ‘proper purpose’ in subsection (3) as both of them require the applicant to demonstrate a justification to inspect the company document, but not for any arbitrary purposes.\(^ {13}\) Similar to the law as it now stands, inspection for speculative and fishing purposes simply for finding irregularity, if any, in the management is also disallowed.\(^ {14}\)

\(^{10}\) *Wong Kar Gee* [2011] 5 HKLRD 241, para. 9.

\(^{11}\) (1831) 2 B & Ad 115 (Ct of KB).

\(^{12}\) Ibid 127-28.

\(^{13}\) Littledale J also referred to *Rex v The Hostmen of Newcastle* (1744) 2 Strange 1223; 93 ER 1144 and held that the statement of law that ‘every member of the corporation had, as such, a right to look into the books for any matter that concerned himself, though it was in a dispute with others’ contained therein must be subjected to the case then before the court (Ibid 128).
B. Three Conditions To Be Met

To be entitled to an inspection order under section 152FA, subsection (2) requires the applicant(s) to have a certain degree of involvement in the company in terms of shares or investment, and subsection (3) requires the application to be brought in ‘good faith’ and for a ‘proper purpose’. These two subsections lay down the basic conditions for obtaining an inspection order. However, as there is no absolute right for a shareholder to inspect company records, the court may refuse to allow an inspection even if the basic conditions are met.\footnote{Snelgrove \textit{v} Great Southern Managers Australia Ltd (in liq) [2010] WASC 51 (SC of Western Australia), para. 68 (Le Miere J).}

Therefore, the third condition is that the case is one which the court is inclined to exercise its discretion.\footnote{The Australian courts, however, seldom exercise the discretion to refuse an application if both good faith and proper purpose have been established. Nevertheless, one may expect the court to refuse an application for inspection if it does no good to both the applicant and the company even if the applicant acts in good faith for a proper purpose. Such situation, though rare, may include an applicant bringing an application for inspecting more documents even when the information in his possession is suffice for his proper purpose.}

This has also been made clear by section 152FA(1) as it states that the court \textit{may} make an order if the criteria in subsection (3) are satisfied.

As held by the Hong Kong Court of Appeal in \textit{Re LehmanBrown}, the applicant bears the burden to prove both ‘good faith’ under subsection 3(a) and ‘proper purpose’ under subsection 3(b).\footnote{Re \textit{LehmanBrown} [2011] 5 HKLRD 668, para. 33.}

Despite there being some discussion as to whether ‘proper purpose’ and ‘good faith’ are indeed one single composite test meaning ‘acting and inspecting for a \textit{bona fide} purpose’.

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fide purpose’,\(^{18}\) it is now settled under Hong Kong law that an application being made with a proper purpose does not imply that it has also been brought in good faith.\(^ {19}\)

The difference between ‘good faith’ and ‘proper purpose’ has also been explained in *Wong Kar Gee*, where the court held that, ‘to some extent,’ ‘good faith’ is determined by a subjective test that ‘[the applicant] believes his purpose in applying for an inspection order is proper’\(^ {20}\) and ‘proper purpose’ is determined by an objective test that ‘the Court must believe the circumstances are such that the inspection applied for is for a proper purpose.’\(^ {21}\) In short, ‘good faith’ is established by looking into the applicant’s mind, and ‘proper purpose’ is established by looking into the circumstances.

Whether the distinction between these two elements can be maintained depends on the ‘extent’ of the inquiry into the matter. As contemplated by Brooking J in *Knightswood Nominees Pty Ltd v Sherwin Pastoral Co Ltd*:

> Once it is accepted that one can up to a point go on asking “Why do you want to do that?” in ascertaining purpose, I do find it hard to see how anything that could be investigated in relation to good faith could not also be investigated in relation to proper purpose.\(^ {22}\)

\(^{18}\) *Knightswood Nominees* (1989) 15 ACLR 151, 156 (Brooking J).

\(^{19}\) *Re LehmanBrown* [2011] 5 HKLRD 668, para. 34.

\(^{20}\) The court also defined ‘good faith’ as being ‘honesty and with no ulterior motive’ and ‘[acting] “honestly” with a purpose that he himself believes to be proper’ (*Wong Kar Gee* [2011] 5 HKLRD 241, para. 16).


\(^{22}\) (1989) 15 ACLR 151 (SC of Victoria), 156.
Although the Hong Kong courts have all rejected the view that ‘good faith’ always follows ‘proper purpose’, it appears that the deeper the inquiry into ‘good faith’ is, the test of ‘good faith’ will tend to be more objective thus being more akin to that of ‘proper purpose’.

III. ‘GOOD FAITH’ – SUBJECTIVE OR OBJECTIVE?

If the court makes a deeper inquiry into the reasons behind the applicant’s pleaded purpose, the applicant’s honest belief may be challenged by more circumstantial factors, which injects into the subjective test of ‘good faith’ more objective elements. This is because the court may question whether it is reasonable in the circumstance for the applicant to believe that he is making a proper application. For example, an applicant who insists on getting further information on top of what the company has been provided may be considered to have acted *mala fide* if the information provided by the company may on its face be sufficient, notwithstanding the genuine belief held by the applicant and the fact that the company may not have made a full disclosure as that under a court’s order. The very end to this inquiry will be that the court infers from the circumstances that the applicant ought to or ought not have believed that his purpose was proper, and this will bring the test for ‘good faith’ so close to that of ‘proper purpose’ as the assessment of ‘good faith’ also becomes dependent on the circumstances. In *Acehill Investments Pty Ltd v Incitec Ltd*, Debelle J even stated that an objective test is applied for both ‘good faith’ and ‘proper purpose’.23

In any case, the inquiry of ‘good faith’ may be too superficial if it focuses merely on the applicant’s belief without considering the whole course of conduct by the applicant. Some

23 [2002] SASC 344 (SC of South Australia), para. 29, where his Honour held that ‘[t]he requirement that the applicant is acting in good faith and that the inspection is to be made for a proper purpose expresses a composite notion and the court will determine whether each has been demonstrated by applying an objective test’ (emphasis added).
Australian cases show that the court will consider both the present circumstances and the previous relevant course of conduct by the applicant. For instance, in *Re Augold NL*, the applicant claimed that its application for inspection was to ascertain steps to be taken in order to ‘protect its investment in the light of such concerns [about mismanagement].’\(^{24}\) Although Williams J held that ‘good faith’ is established by looking ‘at the applicant’s state of mind, a subjective consideration,’\(^{25}\) his Honour also took into account the fact that there was an on-going takeover bid of the respondent company around the time when the application was made, interpreted the true purpose of such application in the way contrary to the applicant’s contention and concluded that it was for ‘destabilising the market for shares in the [respondent] company.’\(^{26}\) In *Quinlan v Vital Technology Australia Ltd*, the applicant claimed that he wished to examine whether there was basis to bring an action on behalf of the company to recover moneys from a contract which he alleged to be entered by directors with personal interests in the contract.\(^{27}\) Rejecting the application, Pidgeon J stated that the question of good faith is ‘to a degree subjective to the applicant’\(^{28}\) but also considered the fraudulent representation made by the applicant to the respondent company in the past\(^{29}\) as well as the

\(^{24}\) (1986) 5 ACLC 286 (SC of Queensland), 291.

\(^{25}\) Ibid 294.

\(^{26}\) Ibid 290-91, 295.

\(^{27}\) (1987) 5 ACLC 389 (SC of Western Australia).

\(^{28}\) Ibid 393.

\(^{29}\) Ibid. This involved the applicant defrauding the respondent company to employ him using fabricated qualifications, which led to the applicant being dismissed without being issued with the shares of the respondent company as promised.
applicant’s acquisition of 100 shares of the respondent company just before making the application in order to give him the standing.\textsuperscript{30}

If one considers ‘good faith’ in a different legal context, there is usually an objective element. For instance, in \textit{Central Estates (Belgravia) Ltd v Woolgar} concerning leasehold enfranchisement, Lord Denning MR described ‘in good faith’ as ‘honestly and with no ulterior motive’ but also drew ‘inference’ from the previous course of conduct of the tenant and concluded that the tenant had an ulterior motive.\textsuperscript{31} In \textit{Street v Derbyshire Unemployed Workers’ Centre} concerning unfair dismissal of employee, Auld LJ also opined that ‘in good faith’, even if being defined simply as ‘honesty of intention’, still requires ‘more than a reasonable belief in the truth of the allegations made.’\textsuperscript{32}

Therefore, most authorities would indicate that there must be certain circumstantial considerations in assessing ‘good faith’ even in the context of section 152FA, which allows the court to ask the question ‘[w]hy do you want to do that’. While being described as ‘subjective’, the test of ‘good faith’ may in future focus also on circumstances related to or surrounding the applicant, who should then be judged according to a reasonable man’s standard as to whether the purpose pleaded by the applicant is his true purpose. The applicant does not act in good faith if, when judging from the circumstances known to the applicant, his true purpose is not the pleaded purpose. Hence, the test for ‘good faith’ under section 152FA(3)(a) should be a subjective test with an objective assessment.

\textsuperscript{30} Ibid.

\textsuperscript{31} [1972] 1 QB 48 (Eng CA), 55-56.

\textsuperscript{32} [2005] ICR 97 (Eng CA), 112.
This construction can also gain support from some American authorities. In *Martin v Columbia Pictures Co*, the court held that ‘good faith’ is not just ‘an honest intent, the absence of malice, the absence of a design to defraud or to seek an unconscionable advantage,’ but also requires ‘an examination and evaluation of external manifestations as well’ and may be evidenced by ‘facts and surrounding circumstances existing prior and subsequent to the application.’

This suggests that when assessing ‘good faith’, the court is entitled to draw reasonable inference from facts which may support or rebut the applicant’s plea of good faith.

IV. WHAT PURPOSES ARE ‘PROPER’?

It has been observed that previous cases which laid down examples of when a purpose is proper may have no precedential value as the criterion of ‘proper purpose’ is ‘very much case-specific.’

Nevertheless, the starting point is stated in *Knightswood Nominees Pty Ltd* that the exercise of such statutory right should be ‘reasonably related to the interest of such person as a member or stockholder.’

The requirement of reasonable relation is interpreted generously in order to give full effect to the legislative intent of safeguarding shareholders’ interests. It is immaterial if the inspection will be hostile to the directors or give the applicant more information than other shareholders.

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33 133 NY S 2d 469 (SC of New York County 1953), 473 (Wasservogel SR).
36 *Wong Kar Gee* [2011] 5 HKLRD 241, para. 25.
Before discussing the substance of ‘proper purpose’, it may be interesting to note that, when the 2004 Bill was introduced into the Legislative Council of Hong Kong, ‘proper purpose’ was qualified with a criterion of ‘having regard to the interests of both the relevant specified corporation and the applicant.’ However, the criterion was subsequently removed as it was said that ‘the added phrase is vague in meaning and may give rise to a misunderstanding that an application must be in the interest of both the applicant and the company.’ It therefore seems that the legislative intent is not to constraint the court as to the factors which may be considered, and it may have been contemplated that in some circumstances it may not be in the company’s interest to make the inspection order.

A. Purposes Ancillary to Exercise of Shareholders’ Rights

From the Australian and American authorities, there are, in broad terms, three categories of proper purposes which can be considered as reasonably related to a shareholder’s interest. The first category is to facilitate the applicant in exercising his rights as a shareholder but not in any other capacity. Mischief in the management is not a prerequisite as shareholders have some rights which may be exercised in neutral circumstances. This proposition can gain support from Young J’s judgment in *Cescastle Pty Ltd v Renak Holdings Ltd*, where his Honour held that a purpose is proper if it is ‘connected with the proper exercise of the rights of a shareholder as a shareholder, as opposed to the purpose connected with some other interest,

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38 The 2004 Bill in its original form is accessible at [http://www.legco.gov.hk/yr02-03/english/bills/c032a-e.pdf](http://www.legco.gov.hk/yr02-03/english/bills/c032a-e.pdf).

such as an interest as a bidder under a takeover scheme, or as a litigant in proceedings against the company.\textsuperscript{40}

An Australian example of such is \textit{Tinios v French Caledonia Travel Service Pty Ltd}, where the applicant was allowed to inspect company records for the purpose of evaluating the price of his shares and selling his shares under the pre-emption clause in the company articles when he was removed as a director after the break down of the \textit{quasi}-partnership within the company.\textsuperscript{41} There were only two members in the company, one being the applicant and another one being a director. Jenkinson J took the view that in such circumstance the applicant was entitled to access information which the other member had access in her capacity as a director when the applicant wished to sell his shares.\textsuperscript{42} In an America case, \textit{NVF Co v Sharon Steel Corporation}, it was even held that a shareholder is entitled to inspect mailing lists of all shareholders in order to obtain proxies or make offers to buy their shares.\textsuperscript{43}

An applicant’s financial interest inherent in his substantial shareholding in the respondent company, however, will not create any favourable presumption to him. Although the Australian proposition is that ‘[i]f the application was being made by a substantial shareholder

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\textsuperscript{40} (1991) 6 ACSR 115 (SC of NSW).
\textsuperscript{41} (1994) 13 ACSR 658 (Federal Ct of Australia).
\textsuperscript{42} Ibid 661.
\textsuperscript{43} 294 F Supp 1091 (District Ct of WD Pennsylvania 1969), 1094 (Dumbauld J). It must however be noted that the Companies Ordinance, s 152FE prohibits collection, retention or use of personal data in contravention of the Personal Data (Privacy) Ordinance (Hong Kong) cap 486 by an order under section 152FA, and Principle 3 of the Data Protection Principles in the Personal Data (Privacy) Ordinance (Cap. 486), Schedule 1 provides that personal data cannot be used for purposes other than those for which the data were to be used at the time of the collection of the data, or a purpose directly related to such purposes.
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of long standing these facts in themselves may well be sufficient to discharge the onus,"\(^4^4\) in *Re LehmanBrown* the Hong Kong Court of Appeal appeared to have rejected this view, where Chu JA stated that '[t]here is no presumption in favour of a substantial shareholder of an entitlement to inspect.'\(^4^5\) This is reasonable as a majority shareholder may also exert undue influence on the management of the company to the prejudice of minorities, and there is no guarantee that such majority shareholder will always be acting in good faith. Nevertheless, it seems that if there is a case for investigation, which will be discussed below, substantial shareholding may make the court be inclined to grant the inspection order for the applicant to secure his financial interest in the company.\(^4^6\)

**B. Purposes Relating to a Case for Investigation**

The second category of proper purpose, which is more frequently pleaded for, is that there is a 'case for investigation'.\(^4^7\) The inspection may be necessary to protect the applicant’s personal economic interest in the company *vis-à-vis* his standing as a shareholder.\(^4^8\) Whether there is a

\(^4^4\) *Quinlan* (1987) 5 ACLC 389, 393 (Pidgeon J). See also Harris J’s observation in *Wong Kar Gee* [2011] 5 HKLRD 241, para. 23 that ‘an application made by a substantial and long-standing shareholder may in and of itself discharge the burden of establishing good faith and proper purpose’.

\(^4^5\) *Re LehmanBrown* [2011] 5 HKLRD 668, para. 33.


\(^4^7\) Although it seems that the court may also consider it separately as a discretionary ground to refuse inspection even when both good faith and proper purpose has been established; see *Wong Kar Gee* [2011] 5 HKLRD 241, para. 41.

\(^4^8\) *Wong Kar Gee* [2011] 5 HKLRD 241, para. 25. It will also be a proper purpose if the applicant is to protect the general interest of the company; see *Varney v Baker* 194 Mass 239 (Supreme Judicial Ct of Massachusetts 1907), 240 (Knowlton CJ).
case for investigation is essentially a question of fact, but it is also worth examining the threshold of proof required in establishing a ‘case for investigation’.

According to Brooking J in *Knightswood Nominees Pty Ltd* (which has been applied by the courts in *Re LehmanBrown*), the applicant should show that ‘there is at least a case for investigation as regards past or future wrongful or other undesirable conduct’ and that he has ‘some reasonable grounds for believing that misconduct or maladministration (or whatever else is suggested) has taken place, or is going to take place.’ The threshold has also been discussed in other Australian cases. It has been described as whether ‘a reasonable shareholder [could] take the view that his investment in [the respondent company] may be adversely affected by this transaction and wish to investigate whether he should take steps with a view to protecting, directly or indirectly, his investment’ in *Intercapital Holdings Ltd v MEH Ltd*, and whether there are ‘questions remaining unanswered that can reasonably be regarded as arousing genuine suspicion in the mind of a shareholder about the extent of the safety and security of his investment in the company’ in *Re Claremont Petroleum*.

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49 *Re LehmanBrown* [2011] 5 HKLRD 668, paras. 43-44.


52 (1988) 13 ACLR 595 (SC of Victoria), 601 (Brooking J). The inspection allowed in this case was in respect of an acquisition of some energy companies involving AU$6.7 million by a subsidiary of the respondent company. The circumstances of the acquisition was described as ‘highly unusual’ as the acquisition was a large one, views were equally divided among the board of directors, and one director of the subsidiary was appointed through telephone when the decision to proceed was also made, notwithstanding the strong opposition from the dissenting directors.

53 *Re Claremont Petroleum NL* (1989) 1 ACSR 494. The inspection was allowed, and the factors considered by the court seem to include the fact that the directors failed to respond, or even
From the statements of law cited above, the applicant should demonstrate, firstly, an element of suspicion that there is a transaction which a reasonable person will find it suspicious and, secondly, an element of proximity that there is a causal link between the transaction and the potential prejudice to the applicant’s interest as a shareholder which warrants an investigation by no one else but the applicant himself. The threshold required is not to demonstrate a solid case of mismanagement but appears to be only evidential, though the evidence presented must allow some ‘reasonable’ suspicion to subsist and such suspicion cannot be resolved with the materials already disclosed by the company.

C. Purposes to Ascertain Share Price

The last category of proper purpose is to obtain information to ascertain the value of the applicant’s shares, but whether this category exists is somehow less certain.\(^{54}\) As held in \textit{Re LehmanBrown}, an application for inspection should be ‘made not out of a mere desire to obtain information.’\(^{55}\) If the applicant was only interested to ascertain from the records disclosed the share price without applying this knowledge for other further purposes, it is arguably a ‘mere desire to obtain information.’ However, Harris J in \textit{Wong Kar Gee} did not shut the door on the possibility of bringing an action to ‘ascertain the fair market value of his shares.’\(^{56}\) When the ignored, doubts and questions raised by the applicant in the previous annual general meeting, and also during the hearing in court.

\(^{54}\) In some Australian cases the applicant failed to obtain an inspection order under this ground but it was for the reason that the court held that it was not the applicant’s primary purpose. See, for example, \textit{Garina Pty Ltd v Action Holdings Ltd} (1989) 7 ACLC 962 (SC of Western Australia), where Commissioner White (at 968) held that the primary purpose of the applicant was to facilitate its take-over bid rather than ascertaining the value of its shares.

\(^{55}\) \textit{Re LehmanBrown} [2011] 5 HKLRD 668, para. 35.

\(^{56}\) \textit{Wong Kar Gee} [2011] 5 HKLRD 241, para. 29.
2004 Bill was presented to the Legislative Council, the Hong Kong Government also considered ‘determin[ing] the value of shares’ as a proper purpose.\(^{57}\)

A *mere* desire to obtain information shall be prohibited as the management should not be encumbered by a shareholder’s fishing expedition or curiosity,\(^{58}\) but if the information obtained can facilitate the shareholder to exercise his rights including to dispose the shares, this should fall into the first category of proper purposes. In any case, the Hong Kong courts do not appear to have ruled out the possibility that an applicant may inspect company records for obtaining information in relation to some personal reasons unrelated to mischief in the management.

This category of proper purpose has in fact received a rather liberal interpretation in the United States. In *Bishop’s Estate v Antilles Enterprises*, the Court of Appeal allowed the successor of a deceased shareholder (with whom the legal title of the shares was vested in) to inspect company records in order to ascertain the book value of the deceased shareholder’s shares so to sell it to the surviving shareholders.\(^{59}\) In *Thomas & Betts Corporation v Leviton Manufacturing Co Inc*, the court also allowed an inspection for evaluating shares, though the scope of inspection was narrowed down, as the corporate applicant was a minority shareholder and it needed information to plan for its long term investment in order to be accountable to its own shareholders.\(^{60}\) The treatment of narrowing down the scope of inspection also suggests that a court may consider restricting the documents to be inspected

\(^{57}\) Report of the Bills Committee on Companies (Amendment) Bill 2003, above n. 8, para. 82.

\(^{58}\) R Tomasic, S Bottomley and R McQueen, *Corporations law in Australia* (2nd edn, 2002) 434.

\(^{59}\) 252 F 2d 498 (CA(3rd Cir) of US 1958), 500 (Maris J).

\(^{60}\) 685 A 2d 702 (Ct of Chancery of Delaware 1995), 712-14 (Jacob VC).
rather than rejecting the entire application, as this can balance the interest of the applicant and the respondent company.

Therefore, it seems that the Hong Kong courts may also be prepared to allow inspection of company record for ascertaining share price, though it is also equitable to place heavier weight on the interest of the respondent company as such application is not strictly relevant to corporate governance and it may also open the floodgate for similar applications. The scope of inspection should therefore be narrower, and an ancillary order may also be made under section 152FB(c) that the applicant should pay for the expenses reasonably incurred by the respondent company when allowing the inspection.

D. Improper Purposes

Some purposes are clearly improper, which include pretentious purposes and purposes which gives the applicant personal financial gain but prejudicing the respondent company. These purposes may also fail under the test for ‘good faith’ as an applicant can hardly convince the court that he believes such purposes to be proper.

There is, however, another improper purpose which the applicant may hold in good faith, which is to challenge the ‘day-to-day managerial decisions’ by the board of directors. This is considered as improper as such challenge should be made during the general meeting instead of in the court. It may be contrasted with the second category of proper purpose stated above,

61 Re LehmanBrown [2011] 5 HKLRD 668, para. 35.

62 For example, facilitating a take-over bid of a subsidiary to the company (Garina Pty Ltd v Action Holdings Ltd (1989) 7 ACLC 962) and obtaining confidential information for a competitor (Knightswood Nominees (1989) 15 ACLR 151, 156).

63 Re Augold NL (1986) 5 ACLC 286.
where inspection may be allowed if there is a case for investigation. Nevertheless, it is submitted that if it can be shown that there is suspicion in some day-to-day managerial decisions, inspection should not be disallowed simply because they were issues concerning routine management, although the court may dismiss the application under discretion if it considers the application to be abusive tactics.

Apart from that, once the applicant can establish that his primary or dominant purpose is proper, any potential secondary purpose, which may be improper, is irrelevant. However, if the secondary purpose claimed by the applicant was found to be the primary purpose (as the test is objective for proper purpose), the application will be denied.

V. SHAREHOLDER’S RIGHT WHICH CAN BE PROTECTED ONLY BY INSPECTION?

Different views have been expressed as to whether the order of inspection may be made only if the purpose is related to a shareholder’s right which can be protected only by an order of inspection under section 152FA. At the first instance of Re LehmanBrown, Deputy Judge Coleman SC took the view that it is necessary in ordinary cases, echoing the view of Breach J in Unity APA Ltd v Humes Ltd (No 2). However, Harris J in Wong Kar Gee took the view that


65 Re Claremont Petroleum NL (1989) 1 ACSR 494, 500 (McPherson J). It has also been suggested that a collateral purpose can taint good faith (see Cockburn and Wiseman, above n. 34, 241).

66 Re LehmanBrown in CFI [2011] 4 HKLRD 237, para. 37, where his Lordship held that ‘an order [of inspection] would ordinarily only be made where the applicant member had some specific and/or personal right which could only be protected by the making of such an order.’

67 [1987] VR 474 (SC of Victoria), 478. See also Czerwinski v Syrena Royal Pty Ltd (No. 1) [2000] VSC 125 (SC of Victoria), para. 14, where Warren J described the statutory right to inspect company records as ‘a remedial or last resort provision.’
it is not necessary and there can be a proper purpose if the shareholder has ‘a genuine and credible belief that there has been corporate mismanagement which is adversely affecting the economic welfare of the company’ or wants to ‘ascertain the fair market value of his shares.’

The question here is two-fold. Firstly, is it necessary for there to be a ‘personal right’ to be protected? If yes, secondly, shall the order of inspection under section 152FA be the only way of protection? As illustrated above, there are cases where an order of inspection was made just for making information available to the applicant to safeguard the applicant’s financial interests in the shares, rather than protecting a shareholder’s rights. Therefore, it does not appear that it is a compulsory requirement that there must be a personal right to be protected.

As to whether section 152FA should be the only way of protection, it is contemplated that the court will not lay down a hard-fastened rule in this regard as section 152FA, similar to its counterpart in other jurisdictions, is much about judicial discretion. This is a question of necessity rather than whether the applicant has exhausted all other remedies, and the court may focus on the question of how proximate the application is to the applicant’s interest as a shareholder. An approach similar to the balance of convenience in granting interlocutory

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68 Wong Kar Gee [2011] 5 HKLRD 241, para. 29, where his Lordship also held in the same paragraph that there might be cases where ‘no specific or personal right exists which may only be protected through the grant of an inspection order.’

69 See, for example, Tinios (1994) 13 ACSR 658 and Bishop’s Estate 252 F 2d 498 (1958). See also Vinciguerra v MG Corrosion Consultants Pty Ltd [2007] FCA 503 (Federal Ct of Australia), paras. 57-59, where Gilmour J allowed inspection of records to investigate the reason for the absence of distribution of dividends and the mismatch in retained profits or assets given that the company was making substantial profit.

injunction may also be adopted,\textsuperscript{71} and the court may balance the hardship caused to each of
the parties as to whether the applicant would suffer more hardship due to the lack of
information, or the respondent company would suffer more as the applicant’s query could
have been resolved by other means.

VI. CORPORATE GOVERNANCE THROUGH INSPECTION

Before the enactment of section 152FA, the Standing Committee on Company Law Reform in
Hong Kong observed that minority shareholders would face great difficulties in obtaining
information for pursuance of their action against the company as Regulation 126 of Table A
model company articles\textsuperscript{72} states that shareholders could not inspect documents other than
those being required by the Companies Ordinance (Cap. 32), unless the director or the
company authorised such inspection.\textsuperscript{73} Section 152FA is therefore enacted to address this
situation. The section provides a means for shareholders to keep an eye on the directors’ work
without directly interfering the management process. Inspecting records may not be a direct
remedy to a shareholder, but it increases the transparency of the operation of a company. As
stated by Harris J in \textit{Wong Kar Gee Mimi}:

In my view, s.152FA affords shareholders an often overlooked yet powerful right by which to
expose wrongful conduct in relation to the company’s affairs. Where the shareholders and
directors are at loggerheads, the right of access to corporate information is particularly
important: in these circumstances, even if a member suspects that something is amiss, for


\textsuperscript{72} It can be found in the Companies Ordinance, Schedule 1.

\textsuperscript{73} The Hong Kong Standing Committee on Company Law Reform, \textit{Corporate Governance
Review – A Consultation Paper on proposals made in Phase I of the Review} (Hong Kong, July
2001) para. 18.02.
example an egregious breach of fiduciary duty, he will be unable to protect his economic interest and financial investment within the company (through, for instance, a derivative action) unless he is able to obtain sufficient information.  

It appears that the Hong Kong courts are prepared to adopt a liberal approach in allowing inspection of records so to prevent the management of a company from misappropriating the company asset and prejudicing the interest of the shareholders. In fact, the wide-reaching definition of ‘record’ in section 2 of the Companies Ordinance (Cap. 32), covering ‘not only a written record but any record conveying information or instructions by any other means whatsoever,’ makes section 152FA a very effective mechanism to monitor the management. Some of these advantages will be illustrated below.

A. Supervising the Management

Together with section 168A of the Companies Ordinance (Cap. 32), which provides a statutory derivative action addressing unfair prejudice to shareholders, a minority shareholder’s right to access information and his financial interest in the company are safeguarded as he can firstly ascertain whether there are merits in the action he proposed to bring against the company. Furthermore, documents passed to the respondent company from its subsidiary may also be disclosed.  

While the scope of disclosure in this regard may not be extensive, it may nevertheless facilitate a multiple derivative action brought by a shareholder of the parent company against wrongdoers in the parent company who defrauded a subsidiary


75 Ibid para. 46.
as if they were defrauding the parent company itself.\textsuperscript{76} Section 152FA may even be interpreted in a way reciprocal to statutory derivative actions so that the shareholder can have the necessary information before initiating the corresponding statutory derivative action for mischief within the management.

In this regard, both the Hong Kong and Australian courts have observed that inspection of company records cannot be used as a ‘pre-action discovery exercise’\textsuperscript{77} or ‘inspection of documents after discovery on affidavit or answers to interrogatories in pending litigation.’\textsuperscript{78} Nevertheless, it appears that the courts only intend to prohibit the applicant from bypassing ordinary procedures or adopting abusive tactics to advance his position in contentious actions against the company. This does not seem to preclude an applicant from obtaining an inspection order if there is a genuine case for investigation but the materials available to the applicant is simply insufficient, which would have otherwise made the litigation premature.\textsuperscript{79}

Exposing company records which disclose mismanagement to the shareholders can also have an immediate effect on the management before further legal action is taken. Therefore, McPherson J in \textit{Re Claremont Petroleum} was willing to allow inspection so that the applicant could be ‘better placed at the forthcoming annual general meeting to ask more penetrating questions about these matters of concern, or failing that, to institute appropriate legal

\textsuperscript{76} cf. \textit{Waddington Ltd v Chan Chun Hoo} [2009] 4 HKC 381 (HK Ct of Final App), para. 67 (Lord Millett PJ). The highest court in Hong Kong, the Court of Final Appeal, confirmed in this case that multiple derivative action can be maintained under common law.

\textsuperscript{77} \textit{Wong Kar Gee} [2011] 5 HKLRD 241, para. 40.

\textsuperscript{78} \textit{Re Claremont Petroleum NL (No. 2)} (1990) 8 ACLC 548 (SC of Queensland), 552 (McPherson J).

\textsuperscript{79} In fact, in both \textit{Wong Kar Gee} [2011] 5 HKLRD 241 and \textit{Re Claremont Petroleum NL (No. 2)} (Ibid), the inspection orders were granted.
proceedings.' 80 This facilitates resolution of issues within the company and increases the sense of accountability of the directors towards the members.

B. Saving Public Resources

There is also a collateral advantage by allowing shareholders to inspect company records. A right to inspect company records not only creates incentive for the shareholder to actively participate in company affairs, but also saves public resources in monitoring any irregular behaviours within companies. As pointed out by Young J in *Cescastle Pty Ltd*, while an investigation of a potential mismanagement can be looked into by regulatory authorities, the authorities, however, have limited resources and a shareholder, particularly one with substantial shareholding thus substantial interest in the company, may make ‘at least a preliminary investigation’ before referring the case to the authorities. 81 This in turn requires the management of a company to be more cautious and prudent as they may be subject to constant ‘supervision’ from shareholders, especially when the substantial shareholders may also be professionals in corporate management.

C. Will It Allow Intervention in Business Management?

The above advantages concerning corporate governance indicate that shareholders have greater influence on the business management by the directors. There is, however, a fundamental rule that ‘a shareholder ought not ordinarily have recourse to the courts to challenge a managerial decision made by or with the approval of its directors’, 82 and it has been observed that allowing inspection of company records ‘cuts across the rule that


81  *Cescastle Pty Ltd* (1991) 6 ACSR 115, 118.

shareholders must really leave the entire management of the company to directors, and are not entitled to see the company's documents.⁸³

There is a policy reason behind enacting section 152FA, which is to enlarge the rights of shareholders in accessing company record.⁸⁴ Being consistent with this policy, it should come as no surprise that section 152FA deviates from the traditional common law position.⁸⁵ This is not to suggest that a shareholder can intervene in the management of the company, but he should at least be able to know what he is actually investing in,⁸⁶ which then allows him to safeguard his interest by taking active actions such as suing the management, or passive actions such as withdrawing his investment. In fact, section 152FA does not enable the shareholder to intervene the management per se, but merely facilitates the shareholder in his decision making. Therefore, provided that the directors have discharged their duties properly, an order of inspection does not seem to pose any threat to the separation of powers within a corporate structure.

VII. CONCLUSION

With a view to promoting corporate governance by increasing transparency within a company, section 152FA is enacted to confer upon shareholders a limited statutory right to inspect

⁸³ Cescastle Pty Ltd (1991) 6 ACSR 115, 117 (Young J).

⁸⁴ Legislative Council, Summary of the Proposals in the Companies (Amendment) Bill 2003, LC paper no. CB(1)2434/02-03(03) (9 September 2003) para. 6(c).

⁸⁵ cf. Cockburn and Wiseman, above n. 34, 239.

⁸⁶ Re Claremont Petroleum NL (No. 2) (1990) 8 ACLC 548, 552, where McPherson J held that inspection of company records ‘is intended to enable a member of a company to inspect its books in order to obtain information about matters that, as member or shareholder in the company, he ought to be informed of by the company.’
company records. This right may be exercised only if the applicant can demonstrate that he brings the application in good faith and for a proper purpose, but the court still retains the discretion to refuse an application. The test applied by the Hong Kong courts for good faith has focused on the subjective intent of the applicant, but the courts in other jurisdictions have also looked into the whole course of conduct pursued by the applicant objectively. This approach is preferable as it is consistent with the interpretation of good faith in other legal context and allows the court to ascertain the true motive of the applicant. The test for proper purpose is objective as in most other jurisdictions, and the purpose is likely to be proper if it is for the exercise of the applicant’s rights in his capacity as a shareholder, for looking into a case for investigation, or for ascertaining shares value.

While the jurisprudence under section 152FA is still developing in Hong Kong, it is argued that such statutory right should be given a liberal interpretation so to increase the transparency within a company. An application to inspect company record may be seen as an arena between the shareholder and the management prior to a full-scale contention, but it also provides an occasion in which the parties may have a better understanding of each other’s case. Therefore, section 152FA will be able to enhance corporate governance and accountability of the directors towards shareholders.
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