

New Jersey Supreme Court Affirms the Proper Scope of Shareholders' Right to Inspect Books and Records

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The New Jersey Supreme Court affirmed per curiam the Appellate Division's decision in *R.A. Feur v. Merck & Co., Inc.* and its strict adherence to the New Jersey corporate statute N.J.S.A. 14A:5-28 governing "books and records" inspection demands.

Case Background

Plaintiff Feur owned shares of Merck stock and made a demand on its Board for certain documents related to Merck's acquisition of another pharmaceutical company. Feur wanted to obtain documents to prove that Merck's acquisition was ill advised and reckless. In response, the Board appointed a "Working Group" that retained counsel and undertook an investigation. Ultimately, the Working Group—in exercising its business judgment—rejected all of Feur's demands.

Feur then made demands for 12 broad categories of books and records related to the Working Group's denial of the initial request, relying on N.J.S.A. 14A:5-28(4). The demand was similarly denied. Thereafter, Feur filed a complaint seeking: (1) books and records pursuant to N.J.S.A. 14A:5-28 and the common law right of inspection; and (2) a declaratory judgment that Merck wrongfully rejected his demand for books and records related to the Working Group. The trial court granted Merck's motion to dismiss, holding that Feur had a "proper purpose" under N.J.S.A. 14A:5-28 for making the demand, but the request was outside the scope of "books and records of account." Further, the trial court held the common law did not expand Feur's rights to books and records beyond what is provided under the statute.

Appellate Division Decision

The Appellate Division agreed the request was outside the scope of books and records under the statute and noted the shareholder making the demand cannot use the subsequent demand to circumvent the denial of the first. Shareholders' entitlement to books and records is limited to the enumerated scope of the statute: books and records of account, minutes, and record of a corporation's shareholders. The demand for books and records of account, according to the court, encompasses accounting or financial documents. By contrast, Feur's demand for the Working Group documents exceeded that limited scope.

In reaching its conclusion, the Appellate Division considered two additional avenues of potential relief—a broad subsection of the statute and the common law right to inspection. Subsection 4 of

the statute authorizes the court to order equitable relief regarding books and records demands. But the court held as a matter of statutory construction the subsection relates only to the “books and records of account, minutes, and record of shareholders of a corporation” and does not confer a general right to inspect additional or broader categories. Indeed, the court specifically held the subsection actually granted the court power to restrict rather than expand. Second, the court held the common law right to inspection may provide a right to broader categories of documents but it also requires the shareholder to first prove good faith and a germane purpose, which Feur did not do. Regardless, the documents Feur sought were not within the common law right to inspection because they were not financial data. The court also declined to address whether the statute abrogated the common law right of inspection, but in dicta, it indicated that it may have.

The Appellate Division also addressed whether Feur was entitled to the books and records as a means of prediscovery for filing a derivative suit. Delaware follows this approach and encourages plaintiffs to use state inspection statutes prior to commencing a derivative action. However, New Jersey does not and the court noted such a holding would defeat New Jersey’s requirement that a plaintiff in a derivative suit submit security (bond) and make a preliminary showing of lack of good faith or independence by the corporation. Plaintiffs can flout those threshold requirements if they can obtain the same discovery via a books and records demand.

New Jersey Versus Delaware Approach

The New Jersey Supreme Court’s approach is distinct from that of the Delaware Supreme Court, which repeatedly pushed for the books and records request to become a prerequisite for filing a derivative action. The purposes of a robust books and records procedure, according to the Delaware Supreme Court, are multifaceted. It encourages transparent corporate governance by making the Board aware of potential wrongdoing, strikes a balance between shareholders’ rights to information and indiscriminate fishing expeditions, and prevents expensive and time-consuming derivative suits that lack merit. New Jersey’s requirement of making litigants post security and demonstrate a preliminary showing also seeks to temper excessive derivative suits and curb unnecessary litigation costs. For example, as a precondition of a suit, plaintiffs must first make a written demand on the Board and allow them 90 days to cure the wrongdoing alleged.

Key Takeaways

The divergent paths of the New Jersey and Delaware Supreme Courts might be explained by the sheer volume of derivative suits in Delaware. Given the lack of recent jurisprudence in this area of corporate law in New Jersey and the differing body of Delaware case law, it is welcomed guidance by the Court.