

Shareholder Inspection Rights for Closely Held Corporations



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The North Carolina Business Court recently strengthened the hands of minority shareholders in closely-held corporations. N.C. Gen. Stat. § 55-16-02(b) affords qualified shareholders the right to “inspect and copy: (1) [r]ecords of any final action taken with or without a meeting of the board of directors . . . ; (2) [a]ccounting records of the corporation; and (3) [t]he record of shareholder.” In the recent case of *Sharman v. Fortran Corp.*, the Business Court not only enforced the minority shareholder’s right to inspect and copy corporate and accounting records, but also awarded attorneys’ fees and court costs to the shareholder plaintiff.^[1] The decision sends a strong message to the directors of closely held corporation: Shareholders have a right to know how you are running the corporation.^[2]

As the *Sharman* court recognized, shareholders have an absolute right to inspect certain records and qualified right to inspect additional records. N.C. Gen. Stat. § 55-16-02, subsection (a) provides an absolute right to inspect a corporation’s articles of incorporation, bylaws, board resolutions approving the issuance of shares, written communications with shareholders and meeting minutes, annual reports and the names and addresses of directors.^[3] Subsection (b), however, affords shareholders the right to inspect not only corporate records, but financial and accounting records, as well.^[4] Such records are obviously a key source of information regarding the corporation’s management and financial condition.

This qualified inspection right is only available to qualified shareholders – i.e., those holding at least five percent of the

corporation's shares – and may only be exercised “in good faith and for a proper purpose.”^[5] The *Sharman* decision confirms that determining whether “any improper transactions have occurred and to determine any possible mismanagement of [the Company] or any possible misappropriation, misapplication, or improper use of any property or asset of [the Company]” is a proper purpose.^[6] Furthermore, “the burden of proof rests upon the corporation . . . to allege and show facts, if it can, that the shareholder is motivated by some improper purpose.”^[7] Thus, minority shareholders clearly have the right to demand access to corporate and financial records if they suspect improper management or malfeasance.

Shareholders seeking to inspect corporate and financial records must request such records “with reasonable particularity.”^[8] Regarding the request for “accounting records,” the *Sharman* court relied on the Official Comments in deciding that the term includes “records that permit financial statements to be prepared which fairly present the financial position and transactions of the corporation.”^[9] This means that shareholders are not only entitled to annual financial statements,^[10] but also “the formal journals and ledgers, and the vouchers, invoices, correspondence, contracts, and other sources for such records.”^[11]

The *Sharman* decision is also rooted in the common law right of inspection based on the idea that shareholders are owners of a corporation and therefore entitled to information regarding the corporation's business.^[12]

[1] *Sharman v. Fortran Corp.*, 2018 N.C.B.C. 27 (NC Super. Ct. Apr. 2, 2018).

[2] *Id.* at ¶47 (“If the court orders inspection and copying of the records demanded, it shall also order the corporation to pay the shareholder's costs (including reasonable attorneys' fees) incurred to obtain the order unless the corporation proves that it refused inspection in good faith because it had a reasonable basis for doubt about the right of the shareholder to inspect the records demanded.” citing N.C. Gen. Stat. § 55-16-04(c)).

[3] N.C. Gen. Stat. § 55-16-02(a) (cross-referencing N.C. Gen. Stat. § 55-16-01€).

[4] N.C. Gen. Stat. § 55-16-02(b)(2).

[5] N.C. Gen. Stat. § 55-16-02(b-c).

[6] *Sharman* 2018 NCBC 27 at ¶26 (citing *Parsons v. Jefferson-Pilot Corp.*, 333 N.C. at 420, 428-430, 426 S.E.2d 685, 691-692 (1993)).

[7] *Sharman* 2018 NCBC 27 at ¶25 (quoting *Carter v. Wilson Constr. Co.*, 83 N.C. App. 61, 65, 348 S.E.2d 830, 832 (1986)).

[8] N.C. Gen. Stat. § 55-16-02(c)(2).

[9] *Sharman* 2018 NCBC 27 at ¶39, (quoting N.C. Gen. Stat. § 55-16-01 Official Comment 2).

[10] N.C. Gen. Stat. § 55-16-02(a).

[11] *Sharman* 2018 NCBC 27 at ¶39 (quoting *Parsons v. Jefferson-Pilot Corp.*, 106 N.C. App. 307, 318-19, 416 S.E.2d 914, 921 (1992)).

[12] *Parsons* 333 N.C. at 424, 426 S.E.2d at 688 (“[T]he rationale behind the common law right of inspection is that those in charge of the corporation are merely agents of the shareholders, and a shareholder's right to inspect a corporation's books and records is only the right to inspect and examine that which is his own.” (citing *Cooke v. Outland*, 265 N.C. 601, 610, 144 S.E.2d 835, 841 (1965))).