Securities and Exchange Commission PHILIPPINES

BAGONG PILIPINAS

OFFICE OF THE GENERAL COUNSEL

21 May 2024

SEC OGC Opinion No.24-14
Re: Inspection Rights of Shareholders

MR. ARIEL CONDAT
Corporate Secretary,
Flexi Finance Asia, Inc.
3rd Flr, CIFC Tower, Juan Luna Ave. Extension
Cebu City, Central Visayas Philippines

Dear Sir:

This refers to your letter[1] requesting, on behalf of Flexi Finance Asia, Inc. (FFAI or Corporation), for an opinion on inspection of corporate books and records.

In your letter, you stated that Mr. Ronnie Katona, one of the shareholders of FFAI, demanded for the inspection of the following records and documents of the corporation:

a. Board Resolutions;
b. Articles of Incorporation, By-Laws, and Stock and Transfer Book;
c. Company valid procedures and policies;
d. Detailed accounting books and information (Including Journal, Balance Sheet, P/L for the years 2016-2019;
e. Auditors Report 2016-2018;
f. Contracts with current directors and officers and past directors or officers including independent directors;
g. Contracts with Supplies;
h. Contracts with Employees;
i. Contracts with Customers (Soft Copies);
j. Organizational Structure and Corporate Governance;
k. Read-only access to database of customers, employees, and accounting records;
l. Originals of Bank Account statements of all corporate bank accounts;
m. Report on the status of cash in HQ and other subsidiaries where cash is stored regularly;
n. Archives with hard copies of the customer's agreements;
o. Tax Returns since 2016;
p. Risk reports with credit policy events;
q. Detailed collection performance reports;
r. Cash Flow Reports;
s. Sales Reports;
t. List of Open Legal Cases with its statuses; and
u. Status of Existing Credit Lines.

You further stated that the list of documents Mr. Katona requested is, to your opinion, so extensive that it covers areas that are not allowed to be disclosed pursuant to relevant laws such as the Intellectual Property Code of the Philippines as amended and the Data Privacy Act of 2012. Moreover, you averred that you asked Mr. Katona the justifications for his request but he only gave sweeping general grounds (i.e., to

[1] Dated 05 December 2019.

ensure that the documents requested are in accordance with the by-laws and the laws of the country).

Your query is, whether the documents requested by Mr. Katona are covered by the right to inspection and if the reasons he gave for inspection are sufficient.

At the outset, please be advised that as a matter of policy, the Commission refrains from or does not render an opinion on: (a) litigious issues which may eventually be litigated in the future in an intra-corporate,[2] civil, and/or administrative case such as matters which involve the substantive and contractual rights of private parties who would, in all probability, contest the same in court or the appropriate body if the opinion turns out to be adverse to their interest;[3] (b) questions which are too general in scope or hypothetical, abstract, speculative and anticipatory in character and those pertaining to undisclosed entities;[4] and (c) requests that will entail the gathering of legal materials or writing abstract essay for the requesting party since the Commission should not function or resemble as legal counsel of private firms.[5]

Considering that the issue may already be the proper subject of a case under Section 73 of Republic Act (RA) No. 11232 otherwise known as the Revised Corporation Code (RCC), and that we cannot write abstract essays to advise or counsel on proper courses of action, especially those involving substantial rights of private parties, the Commission shall refrain from **categorically** rendering an opinion on the issues presented.

However, for purpose of information only, the following may be imparted:

The right to inspect corporate records is rooted in common law which dates back to the 1700s.[6] While legal title to assets and properties of the corporation are lodged with it being a separate legal entity, stockholders/members are nevertheless granted the right to inspect, in their capacity as the ultimate beneficial owners of the corporation. This right allows them to know how the corporation is being managed as well as to keep track of its assets. The common law origins of the right to inspect was recognized by the US Supreme Court in the case of *Guthrie vs. Harkness* which ruled that, *"the right of inspection rests upon the proposition that those in charge of the corporation are merely the agents of the stockholders who are the real owners of the property.* [7]*"*

Thus, Section 73 of the RCC provides the right of a stockholder, member, director or trustee (or their duly authorized representatives) to inspect and/or reproduce corporate books and records, to wit;

> SEC. 73. *Books to be Kept; Stock Transfer Agent.* – Every corporation shall keep and carefully preserve at its principal office **all information relating to the corporation including, but not limited to:**
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> (a) The articles of incorporation and bylaws of the corporation and all their amendments;
> (b) The current ownership structure and voting rights of the corporation, including lists of stockholders or members, group structures, intra-group relations, ownership data, and beneficial ownership;
> (c) The names and addresses of all the members of the board of directors or trustees and the executive officers;
> (d) A record of all business transactions;
> (e) A record of the resolutions of the board of directors or trustees and of the stockholders or members;
> (f) Copies of the latest reportorial requirements submitted to the Commission; and
> (g) The minutes of all meetings of stockholders or members, or of the board of directors or trustees. Such minutes shall set forth in detail, among others: the time and place of the meeting held, how it was authorized, the notice given, the agenda therefor, whether the meeting was regular or special, its object if special, those present and absent, and every act done or ordered done at the meeting. Upon the demand of a 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 yeas and nays must be taken on any motion or

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[2] Pursuant to Section 5.2 of the Securities Regulation Code (SRC), the Commission's jurisdiction over all intra-corporate disputes under Section 5 of Presidential Decree No. 902-A has been transferred to the courts of general jurisdiction or the appropriate Regional Trial Courts.
[3] SEC Memorandum Circular No. 15, Series of 2003, No. 5.2.
[4] Ibid. No. 5.4.
[5] Ibid. No. 5.10.
[6] Robin Hui Huang and Randall Thomas, The Law and Practice of Shareholder Inspection Rights: A Comparative Analysis of the United States and China. Vanderbilt Journal of Transnational Law., Vol. 53.
[7] 199 U.S. 148 (1905). Accessed at: https://supreme.justia.com/cases/federal/us/199/148/ on 29 April 2024 at 1:30 p.m.

> proposition, and a record thereof carefully made. The protest of a director, trustee, stockholder or member on any action or proposed action must be recorded in full upon their demand.
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> **Corporate records, regardless of the form in which they are stored, shall be open to inspection by any director, trustee, stockholder or member of the corporation** in person or by a representative at reasonable hours on business days, and a demand in writing may be made by such director, trustee or stockholder at their expense, for copies of such records or excerpts from said records. x x x
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> A requesting party who is not a stockholder or member of record, or is a competitor, director, officer, controlling stockholder or otherwise represents the interests of a competitor shall have no right to inspect or demand reproduction of corporate records.
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> Any officer or agent of the corporation who shall refuse to allow the inspection and/or reproduction of records in accordance with the provisions 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 punishable under Section 161 of this Code: Provided, That if such refusal is made 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: 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 any prior examination of the records or minutes of such corporation or of any other corporation, or was not acting in good faith or for a legitimate purpose in making the demand to examine or reproduce corporate records, or is a competitor, director, officer, controlling stockholder or otherwise represents the interests of a competitor.
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> If the corporation denies or does not act on a demand for inspection and/or reproduction, the aggrieved party may report such to the Commission. Within five (5) days from receipt of such report, the Commission shall conduct a summary investigation and issue an order directing the inspection or reproduction of the requested records.
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> Stock corporations must also keep a stock and transfer book, which shall contain a record of all stocks in the names of the stockholders alphabetically arranged; the installments paid and unpaid on all stocks 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, by and to whom made; and such other entries as the bylaws 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 by any director or stockholder of the corporation at reasonable hours on business days.
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It is evident that Section 73 recognizes the role that corporate data and information plays in ensuring that shareholders/members are fully aware of the state of a corporation as well as to assist shareholders/members in making informed business decisions and in exercising their right as shareholders/members.

Section 73 implements the Commission's mandate under the RCC of promoting corporate governance and protect minority investors through, among others, the issuance of rules and regulations consistent with international best practices.[8]

In *Gokongwei v. SEC*,[9] the Supreme Court emphasized that the general rule is to recognize and uphold the exercise of the right to inspect, or the right of the shareholders/members to have full access to information on the affairs and finances of the corporation to wit:

> The stockholder's right of inspection of the corporation's books and records is based upon their ownership of the assets and property of the corporation...
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> It appears to be the general rule that stockholders are entitled to full information as to the management of the corporation and the manner of expenditure of its funds and to inspection to obtain such information especially where it appears that the company is being mismanaged or that it is being managed for the benefit of officers or directors or certain of the stockholders to the exclusion of others.

Thus, "all information relating to the corporation" shall be open for inspection and/or reproduction by any stockholder, member, director or trustee of the corporation.

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[8] RCC, Sec. 179 (d).

[9] G.R. No. L-45911, April 11, 1979.

However, Section 73 of the RCC specifically provides that the right to inspect can be limited. It recognizes the defense available to a director, trustee, or officer for refusing to allow a shareholder or member to exercise the right to inspect or reproduce corporate records, namely, when:

(a) The person demanding to examine has improperly used any information secured through any prior examination of the records or minutes of such corporation or for any other corporation;
(b) The one requesting to inspect was not acting in good faith or for a legitimate purpose in making his demand; or
(c) The requesting party is a competitor, director, officer, controlling shareholder or otherwise represents the interests of a competitor.

The Supreme Court, in the case *of Terelay Investment and Development Corp. v. Yulo*[10], held that:

> "The right of the shareholder to inspect the books and records of the Petitioner should not be made subject to the condition of a showing of any particular dispute or of proving any mismanagement or other occasion rendering an examination proper, but if the right is denied, the burden of proof is upon the corporation to show that the purpose of the shareholder is improper, by way of defense. According to a recognized commentator:
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> **In general, however, officers and directors have no legal authority to close the office doors against shareholders for whom they are only agents, and withhold from them the right to inspect the books which furnishes the most effective method of gaining information which the law has provided, <u>on mere doubt or suspicion as to the motives of the shareholder</u>**. While there is some conflict of authority, when an inspection by a shareholder is contested, the burden is usually held to be upon the corporation to establish a probability that the applicant is attempting to gain inspection for a purpose not connected with his interests as a shareholder, or that his purpose is otherwise improper. **<u>The burden is not upon the petitioner to show the propriety of his examination or that the refusal by the officers or directors was wrongful, except under statutory provisions.</u>**

Finally, it is also worthy to note that while an inspecting or reproducing party may obtain corporate information not otherwise open to corporate outsiders [i.e. those deemed confidential such as trade secrets or processes under the Intellectual Property Code (Republic Act No. 8293) or personal information under the Data Privacy Act of 2012 (Republic Act No. 10173)], he shall remain bound by confidentiality rules under prevailing laws. Section 73 of the RCC is explicit, providing thus:

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> x x x. The inspecting or reproducing party shall remain bound by confidentiality rules under prevailing laws, such as the rules on trade secrets or processes under Republic Act No. 8293, otherwise known as the "Intellectual Property Code of the Philippines", as amended, Republic Act No. 10173, otherwise known as the "Data Privacy Act of 2012", Republic Act No. 8799, otherwise known as "The Securities Regulation Code", and the Rules of Court.
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Lastly, Section 73 of the RCC and its implementing guidelines, SEC Memorandum Circular No. 25, Series of 2020, provide that any stockholder who abuses his right to inspect shall be penalized under the RCC, to wit:

> "Any stockholder who shall abuse the rights granted under this section shall be penalized under Section 158 of this Code, without prejudice to the provisions of Republic Act No. 8293, otherwise known as the "Intellectual Property Code of the Philippines," as amended, and Republic Act No. 10173, otherwise known as the "Data Privacy Act of 2012."

We hope you find the foregoing in order.

Very truly yours,

Romuald C. Padilla
General Counsel

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[10] G.R. No. 160924, August 05, 2015.