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ECG Secures First Amendment Victory for California Corporate Directors in Published Appellate Decision

By Katherine Galdos

Corporate directors have a right to see the company's business records—and to share them with stockholders—unless the company can show that directors will use the information to hurt the firm, a state appellate court ruled Tuesday.

The ruling, coming during waves of national corporate accounting scandals, clears up state case law on the rights of directors to view and use corporate records.

"I think yesterday's holding was an important message to both directors and shareholders," said David A. Robinson of Enterprise Law Group, attorney for the suit's plaintiff. "To directors, it said you have the right to inspect, and in light of what's going on in the rest of the world, you have the duty to inspect records."

"And if you find something that's askew, you better come clean with it, and you better break ranks and tell the shareholders," Robinson said.

Robinson's client, Joseph Saline, is a member of the board of directors for Tustin-based Commonwealth Energy Corp. Saline is not allied with the company's other directors and Chief Executive Officer Ian Carter, because of Saline's ties to the company's former CEO, who resigned in 2002.

As Commonwealth considered going public in 2001, officials began arguing internally about the best way to proceed.

To learn more about the company's plans, Saline requested 14 kinds of company records.

"The current CEO, Ian Carter, wrote in an e-mail to the other directors that he did not trust Saline and purposefully chose to 'work around him...as much as

possible," Justice Eileen C. Moore wrote for the 4th District Court of Appeal panel.

Saline claimed that he was the target of a negative campaign which sought to persuade the company's shareholders to oust him and that he was looking for information to help provide the shareholders with a dissenting view. Commonwealth, however, refused to hand over the documents Saline sought.

Orange County Superior Court Judge Randell Wilkinson ordered that Saline be given access to the information he wanted—but on the proviso he share it only with his attorneys, not with Commonwealth's shareholders.

Saline appealed the order, arguing that it violated California corporations law. He also contended that the order was unlawful prior restraint on his right of free speech.

Commonwealth countered that Saline had shown that he would have used the contested information to damage the company and to disclose trade secrets. Saline, the company argued, had posted some confidential information on the Internet and had a conflict of interest because of the stock he held in the New World Power Corp., another energy company.

According to the appellate court, Commonwealth's complaints against Saline weren't enough to keep a member of the board of directors out of the company files.

"The evidentiary showing offered by [Commonwealth] in the lower court was woefully inadequate to establish the necessity limiting Saline's access to corporate documents," Moore wrote. "There was no evidence that Saline intended to use the

documents to disclose trade secrets, compete with or otherwise harm CEC.” *Saline v. Superior Court* G029761 (Cal. App. 4th Dist. July 30, 2002).

Moore was joined by Justices William F. Rylaarsdam and Kathleen E. O’Learly.

Eliot Disner, counsel for Commonwealth, said the company was not sure whether it would appeal the ruling. Saline was re-elected to the board in November 2001 and since has signed a new, stricter confidentiality agreement, Disner said.

“We’re cautiously optimistic that Mr. Saline will obey the new confidentiality agreement that he has signed and that this matter will be moot,” Disner of Manatt Phelps & Phillips said.

The appellate court may have been influenced by recent corporate accounting scandals, Disner added.

“Most companies are law-abiding... Those companies are under the same sort of suspicion that

the other companies are. No one is above this now,” Disner said. “And so Commonwealth Energy, which was clean as a whistle... they’re held to a very high standard.”

Commonwealth, an energy company which thrived in the wake of state’s energy deregulation, never had an official public offering. However, it did begin filing forms with the Securities and Exchange Commission.

The company has been embroiled in internal and legal wrangling since its former CEO, Fred Bloom, resigned in early 2000 as part of a settlement with the Public Utilities Commission. Bloom, who once controlled 6 million shares of the company, used them all to vote Saline onto the board in November 2000.

Saline has been a project manager at Litton Industries. He is also a former chairman of the Orange County Chamber of Commerce.



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