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Pileggi Lecturer Analyzes Importance of Del. Corporate Law

By Elizabeth Bennett

Of the DLW

This year's Francis G. Pileggi Distinguished Lecture in Law contemplated the beating heart of the Delaware legal community: the near dominance enjoyed by Delaware in terms of corporate charters.

Mark J. Roe, the David Berg professor of corporate law at Harvard Law School, delivered the lecture and PowerPoint presentation at the Hotel DuPont in Wilmington.

The professor is "one of the world's leading scholars of corporate law," according to Justice Jack B. Jacobs, who introduced him to a crowd of about 200 at the end of September.

Jacobs also mentioned two *Harvard Law Review* articles by Roe: "Delaware's Competition" and "Delaware's Politics." The justice said they have become "classics in their field."

Roe first noted that there is a longstanding debate among academics on state competition and whether states overly favor managers or create an efficient corporate law.

One camp in this debate describes the competition as a race to the bottom and sees states "pandering to managers and insiders."

For example, Roe mentioned William L. Cary, one-time Securities and Exchange Commission chairman and a law professor at Columbia University, who in the 1970s called Delaware a pygmy that "denigrates corporate policy."

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Lecture

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The other camp in the debate however, sees competition for charters as a race to the top, including Senior Judge Ralph K. Winter, once an academic and now on the 2nd U.S. Court of Appeals.

This camp argues that while the rules may appear to overly favor insiders over shareholders, "if a rule really damaged the cost of capital, then companies would not be in the state," Roe said.

As the debate progressed a new school developed. This camp holds that other

states can't realistically challenge Delaware in terms of corporate charters, which gives the tiny state an effective monopoly. These academics include Lucien A. Bebchuk, Roe's colleague at Harvard.

Quite a few scholars have taken a look at why this may have happened, Roe said, adding that a corporate center has to be a small state. Corporate franchise fees are not going to drive New York or California, for instance.

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warring constituencies of a large state, Roe said.

In addition, Delaware can easily copy whatever other states do, Roe said. Therefore, although some states take a stab at it every once in a while, the competition is mild.

"Companies decide, when they grow up, to move to Delaware," Roe said, getting some laughter.

The professor then introduced his thesis: "The claim I am going to try to advance is that Delaware competes, even if no one else does," he said.

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The competition comes in three "modes," according to Roe. Delaware must compete for an inflow of businesses, and with other states and the federal government.

At this stage, Roe got into the data on money.

"I want to point out that there are more things in life than money," he said. Drivers such as professionalism, pride and the desire to be relevant can also push events, but they are hard to quantify.

With that, Roe explained how he had examined the numbers.

"One reason Delaware can't sit on its laurels is that 10 years from now, half of the Fortune 500 will disappear ... New firms will arise," Roe said.

Using figures provided by the Delaware Secretary of State's Office, Roe said that every year about 10 percent of businesses leave and 10 percent more enter. Roe wondered if it was "the fringe" that turned over, and what its contribution might be to the state treasury.

A cursory examination of press reports from the past few years, however, revealed

major companies moving to Delaware: for example, Sun Microsystems, Amazon.com and The Gap.

Using the 2006 franchise fee figure of \$500 million as his starting point, Roe calculated the contribution of the businesses that got their charters in 2005 and found they accounted for \$37 million of it,

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or in the range of 5 percent to 7 percent.

"It was a much more compressed rate of turnover than I thought," Roe said.

The professor then went back a decade. Of the \$300 million in franchise fees paid in 1996, he found once again that 5 per-

cent to 7 percent had come from firms that had incorporated the year before.

Next, Roe examined the maximum franchise fee payers. He found that 5 percent of Delaware business entities had paid the maximum franchise fee for the previous 10 years.

In 2006, half of the maximum payers had become Delaware corporations within 11 years. This figure remained roughly the same all the way back to 1986, went it shot up to 18 years, Roe said.

Going back to 1983 revealed a more dramatic difference: That year half the maximum franchise fee payers had become Delaware corporations within 25 years.

So what do these numbers tell us? Roe said that, "In terms of dollars, there is more pressure for incorporation dollars in 2007 than 20 years ago. American business has become more volatile. ... There are more incorporation decisions being made in the [United States] more often than there was in 1983."

Roe went on to note that there may be weaknesses in his data — for example, corporation name changes he was unable to detect — and he welcomed feedback.

After painting his picture of the fluid nature of American business today, Roe said he believed the competition from other states is weak, but not zero.

The federal government, however, is a different story, he said.

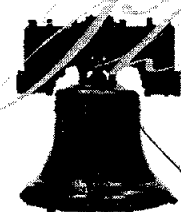
"There are two prime corporate law makers, one in Washington and one in Delaware," Roe said. "They blur. ... Washington can do anything it wants at any time."

In a way, this situation is beneficial: "Delaware can't really make a corporate law antithetical to the country. ... It can't race to the bottom," Roe said, because the U.S. Congress would likely do something.

"It may make it worse," Roe said, "But it would do something."

After providing a few examples of such federal measures, Roe offered some "big picture advice" for Delaware: Act as if you are in Washington making national law, he said.

The annual lecture is presented by the *Delaware Journal of Corporate Law of the Widener University Law School*. It is sponsored by Francis G. Pileggi, a founding attorney of Pileggi & Pileggi and father of Francis G. X. Pileggi of the Wilmington office of Fox Rothschild. •





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