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The Role of Comparative Law in Shaping Corporate Statutory Reforms

Marco Ventoruzzo[*]

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I. INTRODUCTION

A broad but useful definition of comparative law states that:

> Comparative Law is not a body of rules and principles. Primarily, it is a *method*, a way of looking at legal problems, legal institutions, and entire legal systems. By the use of that method it becomes possible to make observations, and to gain insights, which would be denied to one who limits his study to the law of a single country.[1]

More specifically, according to some scholars, comparative law "was not solely the isolated study of foreign legal systems by specialized scholars, but was seen as a commitment to comparative

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1. RUDOLF B. SCHLESINGER ET AL., COMPARATIVE LAW 1 (5th ed. 1988).

methodology throughout legal scholarship aimed to produce actionable knowledge for domestic reform."[2]

Based on these definitions, it is clear that comparative law can play an important role in shaping the development of national or state law. This is particularly true in the case of business law, and specifically corporate law, a field in which international and inter-states transactions are common and in which all the actors involved (legislatures and regulators, the judiciary and legal scholars) often have the opportunity, if not the need, to consider foreign systems and to understand their rules. From this knowledge a natural dialogue should follow among scholars, practitioners and policy-makers of different jurisdictions regarding the adoption (or rejection) of new rules or procedures unknown in one particular country but developed in others. This dialogue is essential to solve the practical problem of coordinating different regulations and legal approaches to specific issues. Legal history indicates an almost endless list of "legal transplants" (defined below) in this area.[3]

This Essay focuses on how comparative law played, and plays, a role in the statutory development of corporate laws. To be sure, comparative law also plays a role in the development of case law: often judges look at other systems, treating their legislation or case law as persuasive authority, especially when there is a lack of precedents helpful to resolve the case before them in their own jurisdiction. The role of comparative law in the development of judge-made law is, however, subtler than and often not as clear as in the case of statutory reforms. This is only natural, as judges are primarily required to apply the law of the land, and only in relatively rare situations do they explicitly turn to foreign examples, generally only as obiter dictum or as supporting argument to sustain a conclusion based on local law. In addition, as courts develop their own body of precedents, the influence of foreign deci-

2. Jedidiah Kroncke, *Law and Development as Anti-Comparative Law*, 45 VAND. J. TRANSNAT'L L. 477, 510 (2012).

3. *See* Alan Watson, THE MAKING OF THE CIVIL LAW 38 (1981); William Ewald, *Comparative Jurisprudence (II): The Logic of Legal Transplants*, 43 AM. J. COMP. L. 489 (1995) (considering Watson's theory of legal transplants). A very interesting look at the development of corporate law from a comparative perspective, and insights on the diffusion of rules elaborated in some jurisdictions to others is offered by Katharina Pistor et al., *The Evolution of Corporate Law: A Cross-Country Comparison*, 23 U. PA. J. INT'L ECON. L. 791 (2002).

sions tends to wane.[4] Several Justices of the U.S. Supreme Court, for example, are explicitly against the citation of foreign precedents in their decisions.[5]

The influence of laws of other systems on the development of statutory law is, on the contrary, more common and explicit. It represents a tradition that accompanied legal reforms since the very beginning of the development of legislation. For these reasons I will concentrate on statutory law.

Concentrating our attention on modern corporate law,[6] I argue that it is necessary to distinguish two basic ways in which comparative law influences legal reforms in a particular jurisdiction. The first one is through regulatory competition among different systems. In order to make a system more competitive and attractive, or to remove disadvantages affecting the economic development of a system, legislatures can respond to the threat of competition from foreign economies by changing their laws, either by borrowing rules and institutions from other systems ("legal transplants"), or by adopting rules designed to protect their own interests vis-à-vis the effects of foreign law.

The second "channel" through which comparative law plays a role in shaping local rules is a top-down harmonization process. Various factors can incentivize a harmonized regulation of corporations: the need to create a common market in which all economic actors can operate in a leveled playing field, the removal of barriers to commerce among states, the desire to reduce regulatory arbitrage, the goal of ensuring to all constituencies of different juris-

4. *See* Adam Liptak, *U.S. Court Is Now Guiding Fewer Nations*, N.Y. TIMES, Sept. 17, 2008 (observing the decreasing influence of U.S. Supreme Court decisions on the Supreme Courts of Canada or Australia).

5. Aharon Barak, *Foreword: A Judge on Judging: The Role of a Supreme Court in a Democracy*, 116 HARV. L. REV. 16, 114 (2002). For example, Chief Justice Rehnquist, in his dissent in *Atkins v. Virginia*, 536 U.S 304, 324-325 (2002), a capital punishment case addressing the execution of mentally retarded defendants, observed, "I fail to see, however, how the views of other countries regarding the punishment of their citizens provide any support for the Court's ultimate determination." Other justices have, on the other hand, advocated the utility of considering foreign law as a guide, especially in certain hard cases: for example Justice Breyer, but also Justices Stevens, O'Connor and Ginsburg. For a discussion of their positions, see Robert J. Delahunty & John Yoo, *Against Foreign Law*, 29 HARV. J.L. & PUB. POL'Y 291 (2005). An interesting article on the use of comparative law in judicial opinions in Europe is Martin Gelter & Mathias M. Siems, *Citations to Foreign Courts – Illegitimate and Superfluous, or Unavoidable? Evidence from Europe*, available on www.ssrn.com and forthcoming in 62 AM. J. COMP. L. ___ (2014); for a broader discussion of this issue, see Mary Ann Glendon, *Comparative Law in the Age of Globalization*, 52 DUQ. L. REV. 1 (2014) in this issue.

6. And the argument can obviously be extended to many other legal fields, from taxation to securities laws, from bankruptcy law to intellectual property, to name a few.

dictions a similar level of legal protection, and so on. Typically, international agreements can foster harmonization. The paradigmatic examples of this are corporate law (and securities regulation) directives in the European Union, but examples are also present in the U.S. Consider, for example, the Sarbanes-Oxley Act of 2002, which introduced some common rules into the field of corporate governance at the federal level, or the role played by the Model Business Corporation Act ("MBCA").[7] The rules contained in these legal instruments are rarely developed out of the blue. Generally, they take into account regulations already existing in one or more jurisdictions, and through a negotiation process, tend to extend them also to other systems.

In the following pages I will discuss several examples of how comparative law influenced the development of statutory corporate law either through the mechanism of regulatory competition or through harmonization, both in the U.S. and in the European Union. I will conclude by considering the role of comparative law in corporate law's statutory evolution. A final caveat is important: in this Essay, I will include in the definition of comparative law also comparisons among different legal systems belonging to the same nation, such as in the case of U.S. states, and not limit the notion of comparative analysis only to comparisons with foreign legal systems.

II. REGULATORY COMPETITION IN THE U.S. AND THE ROLE OF COMPARATIVE LAW: THE EMERGENCE OF DELAWARE

Regulatory competition among states has been defined as "the genius" of American corporate law.[8] In the U.S., corporations are free to choose the state of incorporation, and then simply file the governing documents of the corporation with the local secretary of that state.[9] Once the choice is made, the internal affairs of the

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7. For a critical overview of the corporate governance provisions of the Sarbanes-Oxley Act, see Roberta Romano, *The Sarbanes-Oxley Act and the Making of Quack Corporate Governance*, 114 YALE L.J. 1521 (2005); Houman B. Shadab, *Innovation and Corporate Governance: The Impact of Sarbanes-Oxley*, 10 U. PA. J. BUS. & EMP. L. 955 (2008). For a rich discussion of the evolution of the Model Business Corporation Act, see the contributions in James D. Cox & Herbert S. Wander (special editors), *The Model Business Corporation Act at Sixty*, 74 LAW & CONTEMP. PROBS. (2011).

8. *See* ROBERTA ROMANO, THE GENIUS OF AMERICAN CORPORATE LAW (1993).

9. On the features of the U.S. "market" for corporate charters, see Marco Ventoruzzo, *"Cost-based" and "Rules-based" Regulatory Competition: Markets for Corporate Charters in the U.S. and in the E.U.*, 3 N.Y.U. J. L. & BUS. 91, 102 (2006), where the reader can also find a bibliography.

corporation are governed by the laws of the state of incorporation, even if the corporation does not have any specific connection with that state, apart from being incorporated there.[10] States compete to attract corporations both because of franchise taxes paid by the corporation, and to maintain a vibrant market for legal services. Scholars have discussed whether this competition among states leads to a race to the top, i.e. the development of the most efficient corporate law rules, or a race to the bottom, to the advantage of states that offer a lower level of protection of shareholders. It is well known that the "winner" of this competition is Delaware. This feature of the American system has been discussed so extensively in the literature that it is not necessary here to offer a full account of how it works.[11]

It is, however, interesting to consider the role played by comparisons among different states' corporate statutes in this race among U.S. states. A phenomenon that is necessary to consider is the expectation that states that want to compete with Delaware for a slice of the "market for charters" would simply "copy" its statutory provisions. Interestingly enough, however, this is not so common.[12] One possible explanation is that the real advantage of Delaware is not so much in its statutory provisions (notoriously flexible, but also somehow vague and convoluted), but rather in the expertise and efficiency of its judiciary, an element that is much more difficult to replicate in other states, and in network externalities connected to the very fact that most publicly held corporations are incorporated in Delaware.[13] Notwithstanding this obser-

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10. *See* 1 JAMES D. COX & THOMAS LEE HAZEN, COX & HAZEN ON CORPORATIONS 123 (2d ed. 2003).

11. Among many contributions on the role of state competition in corporate law and securities regulation, as either a race-to-the-top or to-the-bottom, see the classical works by William L. Cary, *Federalism and Corporate Law: Reflections Upon Delaware*, 83 YALE L.J. 663 (1974); Ralph K. Winter, Jr., *State Law, Shareholder Protection, and the Theory of the Corporation*, 6 J. LEGAL STUD. 251 (1977); Daniel R. Fischel, *The "Race to the Bottom" Revisited: Reflections on Recent Developments in Delaware's Corporation Law*, 76 NW. U. L. REV. 913 (1982); Roberta Romano, *Empowering Investors: A Market Approach to Securities Regulation*, 107 YALE L.J. 2359 (1998); Merrit B. Fox, *Retaining Mandatory Securities Disclosure: Why Issuer Choice is Not Investor Empowerment*, 85 VA. L. REV. 1335 (1999). For a comprehensive bibliography on the role of regulatory competition in U.S. corporate law, see Kagan Kocaoglu, *A Comparative Bibliography: Regulatory Competition on Corporate Law* (Georgetown Law Working Paper 2008), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1103644.

12. Most states (thirty nine) have in fact preferred to adopt – with some local variations – a version of the Model Business Corporation Act. *See* DOUGLAS M. BRANSON ET AL., BUSINESS ENTERPRISES: LEGAL STRUCTURES, GOVERNANCE, AND POLICY 184 (2d ed. 2012).

13. *See* Peter V. Letsou, *The Changing Face of Corporate Governance Regulation in the United States: The Evolving Roles of the Federal and State Governments*, 46 WILLAMETTE L.

vation, comparisons among states have played a role in shaping modern corporate law. I will briefly discuss here three examples, in chronological order: the very initial stages of Delaware supremacy, the adoption of anti-takeover statutes, and the enactment of provisions aimed at increasing the power of shareholders in the election of directors.

In the 1880s, New Jersey was looking for a way to improve its finances. The state provided for a franchise tax for corporations incorporated there. Following the advice of a New York attorney, James B. Dill, the state decided to try to attract corporations by making its laws more appealing to managers. In particular, toward the end of the century, with a series of acts, New Jersey allowed corporations to buy, hold and sell the stock of other corporations, making it possible to create holding corporations. Legal reforms in those years also simplified other relevant aspects of corporate law, as other states began to feel the competitive pressure exercised by New Jersey.[14] In 1892, for example, New York granted a special charter to General Electric, containing provisions very similar to the ones of the New Jersey legislation; this charter was explicitly motivated by the fear that the corporation might reincorporate in New Jersey.[15]

In this context, Delaware was a follower of New Jersey. In 1899 it enacted a general corporation act that borrowed—in fact copied—many of the provisions of the New Jersey legislation that were more attractive to managers, such as the possibility of perpetual existence for a corporation, the fact that filing documents with the secretary of state was sufficient to incorporate (without judicial control), and rules allowing corporations to hold shares of other in-state and out-of-state corporations.[16] In the following years, Delaware started eroding the advantage of New Jersey, in part due to its lower taxes for business incorporated in the state, and in part because of additional legislative measures designed to

REV. 149, 196 (2009). "Network externalities" are defined by economists as positive or negative effects on the user of a product or service of others using the same or compatible products. A good and simple example is the effect of owning a popular car: it is easier and often cheaper to find spare parts and mechanics able to work on the car.

14. William E. Kirk, III, *A Case Study in Legislative Opportunism: How Delaware Used the Federal-State System to Attain Corporate Pre-Eminence*, 10 J. CORP. L. 233, 246-50 (1984). *See also* Andrew A. Schwartz, *The Perpetual Corporation*, 80 GEO. WASH. L. REV. 764, 820 (2012); Joel Seligman, *A Brief History of Delaware's General Corporation Law of 1899*, 1 DEL. J. CORP. L. 249 (1976).

15. Kirk, *supra* note 14, at 249.

16. *Id.* at 255.

favor corporate insiders. Particularly important in this respect was the 1911 amendment of its general corporation law limiting directors' liability for illegal payments of dividends or capital reductions to cases of willful or negligent violation.[17]

The true watershed came, however, with Woodrow Wilson, then governor of New Jersey. As part of his presidential campaign in 1912, while he was still governor, Wilson took a strong position against monopolies.[18] As a consequence, state legislation against monopolies and holding companies was enacted in New Jersey.[19] Almost immediately New Jersey started losing its competitive edge in the market for corporate charters, and most corporations turned to neighboring Delaware for a more business-friendly legal environment. New Jersey saw a strong decline in the number of businesses incorporating in the state, and Delaware became the new leader. Although New Jersey repealed the anti-monopolistic statutes adopted in 1912 just a few years later, it never regained its original preeminence.[20]

The rise of Delaware as the most important state for corporations, especially publicly held ones, was largely the result of a comparative study of the legislation of the sister state of New Jersey. By borrowing the measures that were attractive to corporations, and rejecting the ones unfriendly to business, Delaware built its competitive advantage and attained a position that lasts to these days.[21] We can, therefore, observe that the very phenomenon of regulatory competition in U.S. corporate law developed through legal transplants made possible by a comparative understanding of corporate statutes.

A. *Anti-takeover Statutes*

Another interesting and more recent example of how the corporate laws of one jurisdiction can influence, through regulatory competition, the development of legal rules in other systems concerns anti-takeover statutes. Beginning in the 1960s, due to a wave of hostile acquisitions, states' legislatures started to attempt

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17. *Id.*
18. *Id.* at 256.
19. *Id.* at 256-57.
20. *Id.* at 257-58.
21. Mark J. Roe, *Delaware's Competition*, 117 HARV. L. REV. 588, 609-10 (2003) (observing how Delaware "copied" New Jersey's corporate laws in order to attract corporations).

to protect corporations doing business or incorporated in the state from possible hostile takeovers.

A "first generation" of anti-takeover statutes adopted a very simple, and somehow naïve, approach introducing specific disclosure requirements, waiting periods to launch a tender offer, and the need for a merit-based approval of the acquisition by a state authority.[22] A good example of this first generation of statutes was the Illinois Business Takeover Act.[23] The Supreme Court declared this statute unconstitutional in *Edgar v. Mite*,[24] both because it violated the Commerce Clause of the federal Constitution, and because it was pre-empted by the Williams Act,[25] the federal statute regulating takeovers, which aimed at creating a level playing field between the acquirer and the target corporation.[26]

Other states, observing the outcome of this case, drafted anti-takeover rules designed to avoid the constitutional hurdles raised by the Illinois Act (so-called "second and third generation" statutes).[27] The key feature of these statutes was that they implemented defensive barriers regulating the internal affairs of the corporation, a subject strictly within the competence of states, and that they only applied to domestic corporations (i.e., corporations incorporated in the state).[28] These statutes take several forms: most of them are modeled after one of the following regulatory schemes. There are "control share acquisition statutes" that prevent a bidder acquiring more than a set threshold of the shares from voting her shares unless a majority of disinterested shareholders votes in favor of the acquisition. "Business combination statutes" limit certain transactions that typically follow a successful acquisition, such as mergers, sale of assets, and liquidation for a number of years after the acquisition if the board of the target

22. Under a "merit-based" approach, a state authority is granted the power to review the tender offer and allow it to go forward only if it determines that the price and conditions offered are fair for the shareholders. The first anti-takeover statute was enacted in Virginia in 1968; soon enough more than thirty states followed in its footsteps. *See* John C. Anjier, *Anti-Takeover Statutes, Shareholders, Stakeholders and Risk*, 51 LA. L. REV. 561, 69 (1991).

23. Ill.Rev.Stat., ch. 121 1/2, ¶ 137.52-9 (1979), *invalidated* by Edgar v. MITE Corp., 457 U.S. 624 (1982). *See* Guhan Subramanian, Steven Herscovici & Brian Barbetta, *Is Delaware's Antitakeover Statute Unconstitutional? Evidence from 1988-2008*, 65 BUS. LAW. 685, 692 (2010).

24. 457 U.S. 624 (1982).

25. Pub. L. No. 90-439, 82 Stat. 454 (1968) (codified at 15 U.S.C. §§ 78m(d)-(e), n(d)-(f)).

26. *See* Edgar, 457 U.S. at 639.

27. *See* THOMAS LEE HAZEN, THE LAW OF SECURITIES REGULATION 675 (3d ed. 1996).

28. *Id.*

corporation does not approve the transaction. "Fair price statutes" require a bidder to offer a "minimum price" if the acquisition is not approved by a supermajority of the shareholders. "Cash-out statutes" provide that the acquirer of a set threshold of shares must buy all the remaining shares at the highest price paid.[29] "Other constituencies' statutes" allow the directors of the target to take into account the interests of stakeholders different from shareholders, like employees or the local community, in adopting defensive measures. Finally, some statutes explicitly allow and regulate the use of "poison pills" by the target corporation.[30]

One of the most significant examples of these second generation statutes is the Indiana Control Share Acquisition Act of 1986.[31] Under this piece of legislation, the board of directors of an Indiana corporation could opt into a regime in which, if a buyer passed a specific threshold of the voting shares (twenty percent, thirty percent, or fifty percent), she would not have the right to vote her shares unless a majority of the remaining disinterested shareholders granted her the right to vote.[32] In this case, the corporation might redeem the shares from the buyer at their fair value, if authorized by the articles of incorporation or the bylaws.[33]

The constitutionality of this statute was challenged before the Supreme Court in the famous case of *Dynamics Corp. of America v. CTS Corp.*[34] In this case Dynamics, a New York corporation, intended to raise its stake in CTS, an Indiana corporation, from approximately ten percent to almost twenty-three percent.[35] Because CTS had opted into the Indiana Control Share Acquisition Act, Dynamics sued, arguing the unconstitutionality of the statute.[36] The Court of Appeals ruled that the statute was invalid, following *Edgar*.[37] The Supreme Court, however, granted certiorari and ultimately decided that the statute was valid, both with

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29. *See* STEPHEN M. BAINBRIDGE, CORPORATE LAW 411 (2d ed. 2009).

30. *See* Guhan Subramanian, *The Influence of Antitakeover Statutes on Incorporation Choice: Evidence on the "Race" Debate and Antitakeover Overreaching*, 150 U. PA. L. REV. 1795, 1827 (2002).

31. IND. CODE ANN. § 23-1-42 (West 1986).

32. *See* STEPHEN M. BAINBRIDGE, *supra* note 29, at 411.

33. *See* Russell D. Garrett, *Third-Generation Anti-Takeover Statutes in Oregon and Indiana after Dynamics: Target Corporations Control the Ship and Raiders are Foiled*, 24 WILLAMETTE L. REV. 73, 83-84 (1988).

34. 481 U.S. 69 (1987).

35. *Id.* at 75.

36. *Id.*

37. Dynamics Corp. of America v. CTS Corp., 794 F.2d 250, 263 (7th Cir. 1986), *rev'd.*, 481 U.S. 69 (1987).

respect to the Commerce Clause and to the issue of preemption by the Williams Act.[38]

What is relevant to our discussion is how other states adopted the Indiana approach after it passed constitutional scrutiny: Oregon, for example, introduced its first anti-takeover statute on the basis of the approach followed by the Indiana legislature.[39]

It is not necessary in this Essay to dissect the technicalities of these laws, and it would be beside the point here to discuss the economic effects of these provisions on the different stakeholders.[40] It is interesting, however, to observe how quickly different states copied legal instruments developed through experimentation in other jurisdictions, yet another indication of how comparative analysis led legislatures to use legal transplants to regulate the market for corporate control.

B. *Proxy Access and the (Failed) Challenge of North Dakota.*

Continuing our analysis of examples of the influence of comparative law through regulatory competition in the U.S., another interesting case is offered by the recent debate on proxy access. In short, in the last few years, institutional investors have been pressing corporations to allow shareholders to include their nominees in the proxy statement sent out by the corporation for the election of directors. Traditionally, in fact, corporations could exclude shareholders' proposals concerning the election of directors from the corporate proxies.[41]

In 2007, North Dakota tried to exploit investors' requests for a stronger voice in the election of directors by enacting the North

38. *Dynamics,* 481 U.S. at 94. *See* Garrett, *supra* note 33, at 85.

39. Garrett, *supra* note 33, at 89.

40. It is worth noting, however, that the adoption of anti-takeover statutes tells us something about the dynamics of regulatory competition in the U.S., and more specifically about whether it leads to a race to the top or to the bottom. According to a very interesting study by Subramanian, in fact, corporations seemed to stay away, or move, from states with anti-takeover statutes too favorable for the target (such as Massachusetts, Ohio and Pennsylvania). This empirical evidence suggests that the incumbents that make the decision on where to incorporate or reincorporate do not necessarily choose the jurisdiction that offers them the highest level of protection, but look for systems that also protect adequately the interests of minority shareholders to receive, under certain conditions, a premium for control. *See* Subramanian, *supra* note 30, at 1801.

41. *See* Marco Ventoruzzo, *Empowering Shareholders in Directors' Elections: A Revolution in the Making,* 8(2) EUR. CO. & FIN. L. REV. 105 (2011).

Dakota Publicly Traded Corporation Act ("NDPTCA").[42] In brief, the Act is a sort of investors' "wish list" that includes shareholders' access to corporate proxy statements, majority voting in directors' elections, shareholders' advisory votes on executive compensation, and limitations to supermajority rules and antitakeover provisions. The rationale was to enter the competition for corporate charters by offering a legal regime valued by institutional investors, with the idea that some corporations might opt to incorporate in the state under pressure from these institutional investors. In this way, North Dakota hoped to compete against Delaware in attracting corporations offering a new "product": its pro-investors rules. As far as we can tell a few years after the enactment of the North Dakota Act, the experiment has not really been successful.[43] It is, however, interesting for our purposes to point out that, once again, an idea derived from comparative analysis of corporate statutes formed the basis of statutory reform in the field.[44]

Even more interesting and relevant to our discussion is that, shortly after the enactment of the NDPTCA, Delaware responded. In particular, in 2009 the Delaware legislature amended Section 112 of the Delaware General Corporation Law to provide that the bylaws of a corporation can grant shareholders access to the corporate proxy statement in directors' elections under certain conditions.[45] Two caveats are important. First, the Delaware move did not really add much to the pre-existing regime because, even before this amendment, the governing documents of the corporation could allow proxy access to shareholders. Secondly, as also pointed out in general by Mark Roe,[46] the Delaware legislature probably did not act out of fear of competition from North Dakota, but rather to avoid federal rules on this issue that might preempt state law (federal rules were in fact introduced later on).[47]

Once again, however, the point of this story is not so much about the specific rules adopted, but rather to emphasize how regulatory competition (either horizontal, among states, or vertical,

42. N.D. Cent. Code § 10-35 (2010). For a critique of the possible success of the Act in attracting corporations, see Stephen M. Bainbridge, *Why the North Dakota Publicly Traded Corporation Act Will Fail*, 84 N.D. L. REV. 1043 (2008).

43. Ventoruzzo, *supra* note 41, at 112.

44. *Id.*

45. DEL. CODE ANN. tit. 8, § 112 (West 2013)

46. Roe, *supra* note 21, at 600.

47. Ventoruzzo, *supra* note 41, at 117.

between state and federal law) creates the conditions through which comparative analysis influences the development of statutory corporate reforms.

III. HARMONIZATION OF CORPORATE STATUTES IN THE U.S. AND THE ROLE OF COMPARATIVE LAW

Corporate statutes develop not only due to competitive pressure among legislatures, but also as a result of harmonization efforts. One of the best examples of successful harmonization that can be found in the U.S. is the MBCA. This is a peculiar type of harmonization in the sense that it is not imposed top-down, as in the case of the European Union's directives, but rather, it is a spontaneous harmonization. The MBCA is not in fact a statute but, as the name suggests, is instead a model adopted by the Committee on Corporate Laws of the Section of Business Law of the American Bar Association in 1950 and frequently updated and revised throughout the following decades.[48] States are free to borrow all or part of the provisions of the Act. As of 2005, approximately twenty-four states had adopted—to a large extent, even if often with some local variations—the MBCA.[49] Other calculations suggest a higher number of states following the MBCA.[50] It might be argued, as mentioned before, that more states have preferred to turn to the MBCA rather than copying the Delaware General Corporation Law, notwithstanding the role of Delaware in the market for corporate charters.

A comparison of the structure of the MBCA with that of the Delaware corporate statute illustrates why this is not surprising. To the extent that it is possible to generalize, Delaware statutory provisions leave a lot of room to case law, while the MBCA offers a more detailed and comprehensive set of statutory provisions. It is therefore easier for a state to copy the latter model, which gives guidance to businesspeople, practitioners and judges. In addition,

48. For a recent collection of contributions discussing different aspects of the development of the MBCA, see Cox & Wander, *supra* note 7. Interestingly enough, Canada also shows a degree of harmonization with the MBCA. *See also* Cally Jordan, *The Chameleon Effect: Beyond the Bonding Hypothesis for Cross-Listed Securities*, 3 N.Y.U. J. L. & BUS. 37, 71 n.126 (2006).

49. *See* Lucian Arye Bebchuk, *The Case for Increasing Shareholder Power*, 118 HARV. L. REV. 833, 844 (2005).

50. Thirty nine, according to BRANSON ET AL., *supra* note 12.

at least, according to its drafters, the MBCA was (and arguably is) "better organized and more clearly drafted than the DGCL."[51]

The MBCA, however, was not born and did not develop out of the blue. Quite the contrary, it can be considered something between a restatement of the best corporate laws and a compilation of new rules designed to address specific problems emerging from existing corporate laws. From this perspective, if one takes a closer look, it is clear that between the MBCA and the DGCL itself there is a "symbiotic" relationship, because one influenced the other.[52] In other words, the MBCA and its harmonizing strength derive from comparative law.

For example, due to a historical accident, the first drafters of the MBCA were predominantly members of the Chicago bar and, therefore, the original structure of the MBCA resembled the Illinois Business Corporation Act of 1933[53] quite closely.[54] This Act, however, had in turn been at least partially inspired by the Delaware General Corporation Law, as were other modern corporate statutes enacted during that period.[55] The MBCA quickly became very successful, and several states amended their corporation laws to adopt provisions and approaches of the Act.[56] Partially as a response to this development, in the 1960s Delaware revised its corporation statute, and the 1967 reform of Delaware law paid close attention to the MBCA.[57]

The development of the MBCA has also been influenced by changes in the business environment. As an illustration, one can consider that in 2006 the MBCA was amended to provide for majority voting to elect directors in response to growing pressure from investors to adopt majority voting as opposed to plurality voting.[58]

The MBCA represents a form of spontaneous harmonization. Convergence of corporate rules toward one single model can, how-

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51. Jeffrey M. Gorris, Lawrence A. Hamermesh & Leo E. Strine, Jr., *Delaware Corporate Law and the Model Business Corporation Act: A Study in Symbiosis*, 74 LAW & CONTEMP. PROBS. 107, 108 (2011). *See also* Jule E. Stocker, Book Review, 16 BUS. LAW. 748, 748 (1961) (reviewing Model Business Corporation Act Annotated).

52. Gorris et al., *supra* note 51, at 107.

53. 1933 Ill. Laws 310.

54. Gorris et al., *supra* note 52, at 109.

55. *Id.*

56. *See* BRANSON ET AL., *supra* note 12, at 7-8.

57. Gorris et al., *supra* note 52, at 109-11.

58. John F. Olson & Aaron K. Briggs, *The Model Business Corporation Act and Corporate Governance: An Enabling Statute Moves toward Normative Standards*, 74 LAW & CONTEMP. PROBS. 31, 38 (2011).

ever, also be achieved, somewhat more effectively, by the federal government, to the extent that it can impose, directly or indirectly, standards of corporate governance. This is what happened with the Sarbanes-Oxley Act of 2002[59] ("SOX"), a statute adopted to respond to corporate scandals with, among other measures, new governance rules.[60]

Some of the most important reforms introduced in this area by the SOX are: (a) the provision of an audit committee composed of independent directors, (b) limits on the non-auditing services that the audit firm can render to the corporation, (c) limitations on corporate loans to executives, (d) executive certification of financial statements, and (e) the creation of an accounting industry regulator.[61] The common denominator among these provisions was to increase the independence of corporate actors in order to empower them to react to accounting frauds. It is interesting to point out that no U.S. state has mandated any of the governance rules introduced with the SOX.[62]

There is no strong evidence in the legislative history of the SOX to suggest that Congress took into account foreign experiences in crafting the new rules. It cannot be ignored, however, that several foreign jurisdictions already provided for rules similar to those enacted in the SOX. For example, most civil law countries have a system of corporate governance in which the shareholders' meeting appoints both a board of directors and a separate controlling body composed of independent members (such as Italy's "collegio sindacale"). This controlling body has functions at least partially overlapping with the ones entrusted to the audit committee regulated by the SOX.[63] Again, in most European jurisdictions, even before the SOX, auditing firms were subject to public oversight by independent agencies (often the local equivalent of the Securities and Exchange Commission).[64] It seems natural to think that

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59. Pub. L. No. 107-204, 116 Stat. 745 (2002) (codified as amended in scattered sections of 15 U.S.C. and 18 U.S.C.).

60. *See generally* Romano, *supra* note 7; Shadab, *supra* note 7.

61. For an analytical discussion of these new rules, see Romano, *supra* note 7.

62. *Id.* at 1528.

63. In fact, the SEC rules list the Italian "collegio sinadacale" as a body that satisfies the government requirements of the Sarbanes-Oxley Act. *See* Maria Camilla Cardilli, *Regulation Without Borders: The Impact of Sarbanes-Oxley on European Companies*, 27 FORDHAM INT'L L.J. 785, 803 n.96 (2004).

64. David A. Skeel, Jr. et al., *Inside-Out Corporate Governance*, 37 J. CORP. L. 147, 181 (2011); Lorenzo Segato, *A Comparative Analysis of Shareholder Protections in Italy and the United States: Parmalat as a Case Study*, 26 NW. J. INT'L L. & BUS. 373, 407 (2006); Luca

these comparative insights played a role in shaping the new rules introduced in 2002 in the U.S.

IV. REGULATORY COMPETITION IN EUROPE AND THE ROLE OF COMPARATIVE LAW

Regulatory competition in the European Union does not play the same role that it plays in the U.S. The difference is due to a number of factors that I have discussed in another article.[65] To the extent that a market for corporate charters exists in the European Union, however, its features are very different from those of the American market. More specifically, in the U.S., corporations that shop around for more favorable corporate laws generally do so when they decide to go public.[66] Small, closely held corporations tend to incorporate locally, where the actual seat of the corporation is located; only at a later stage, when they are about to be listed, do they reincorporate (often in Delaware). In Europe, on the contrary, the corporations that have their real seat in one Member State and incorporate in another are generally small, closely held corporations that often opt for a different jurisdiction that offers more flexible rules on capital formation and on incorporation.[67] Empirical evidence suggests, for example, that in the last few years a significant number of firms located in continental Europe decided to incorporate in the U.K., due—among other reasons—to less strict rules concerning the legal capital (the minimum capital that the corporation needs to maintain in order to operate) and a swifter incorporation process.[68]

It is interesting to note how this particular kind of regulatory competition prompted legal reforms in continental Europe. Several states in particular relaxed their rules on legal capital and amended their corporate statutes to curb the attractiveness of the U.K.[69]

Enriques, *Bad Apples, Bad Oranges: A Comment from Old Europe on Post-Enron Corporate Governance Reforms*, 38 WAKE FOREST L. REV. 911, 923 (2003).

65. *See generally* Ventoruzzo, *supra* note 9.

66. *Id.* at 102.

67. *Id.*

68. Marco Becht et al., *Where Do Firms Incorporate?* 24 (European Corporate Governance Inst., Working Paper No. 70/2006, 2007), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=906066.

69. Evidence of regulatory competition responses to the U.K.'s ability to attract closely held corporations have been found in Germany, the Netherlands, and France. *See* Becht, *supra* note 68, at 29. As reported by Giuseppe B. Portale, *La riforma delle società di capitali tra diritto comunitario e diritto internazionale privato*, 1 EUROPA E DIR. PRIV. 101, n.70

Once again, regulatory competition leads to the circulation of legal rules and models among different countries: comparative analysis is a key element of this competition and states quickly adapt their corporate statutes due to competitive pressure from other jurisdictions, often mimicking, at least partially, the more attractive rules adopted abroad.

Regulatory competition in the field of corporate law does not only occur vis-à-vis the concrete fear of incorporation or reincorporation abroad. Virtually every major corporate law reform presents an occasion to study the rules adopted in other jurisdictions and imitate the ones that might contribute to the efficiency and competitiveness of the business legal environment. The history of corporate law (but also of other fields) clearly demonstrates this comparative attitude of legislators. A good and relatively recent example of this dynamic in Europe is offered by the reform of corporate law enacted in Italy in 2003.

The reform was largely inspired by comparative corporate law. In fact, it introduced into the Italian legal system several rules borrowed from other jurisdictions. Just to mention two of the most relevant cases, consider the rules on governance models and on preemptive rights in the case of the issuance of new shares. Traditionally, the Italian legal system was characterized by a corporate governance model that provided that the shareholders' meeting would appoint both a board of directors, entrusted with the task of managing the corporation, and a board of statutory auditors with controlling functions.[70] The reform of 2003 introduced a richer menu. The bylaws can now opt for one of three alternative models of corporate governance: the traditional one mentioned above, a two-tier model inspired by German law, and a one-tier model inspired by British (and generally Anglo-Saxon) governance models. In the case of the two-tier system, the shareholders' meeting appoints a supervisory board of directors, and this body appoints a managing board. The former is entrusted with

(2005), in France, a statute, Article L. 223-2 of the Commercial Code (as modified by the law of August 1, 2003), abolished minimum legal capital for limited liability corporations. In Spain, law No. 7/2003 of April 1, 2003, allows the "Sociedad Limidada Nueva Empresa" to be incorporated with a capital of little more than 3,000 euros. *See* RODRIGO URÍA ET AL., CURSO DE DERECHO MERCANTIL, VOL. I 1131 (2006); *see also* Marco Ventoruzzo, *Experiments in Comparative Corporate Law: The Recent Italian Reform and the Dubious Virtues of a Market for Rules in the Absence of Effective Regulatory Competition*, 40 TEX. INT'L L.J. 113 (2004) (noting that amendments to Italian law in 2003 have added flexibility to the rules governing the formation of capital and the financial structure of the corporation).

70. For a more detailed discussion, see Ventoruzzo, *supra* note 69, at 146.

controlling functions; the latter manages the corporation. In the case of the one-tier model, the shareholders only appoint a board of directors, which must include a certain number of independent directors. The board appoints, among its members, an auditing committee that closely resembles the one that can be found in common law systems.[71]

As mentioned above, rules concerning the financial structure of the corporation have also been overhauled in light of foreign experiences. For example, before 2003, a corporation that wanted to issue new shares had to offer them to existing shareholders with a preemptive right to purchase the new shares.[72] There were only three exceptions to this mandatory preemptive right: when the corporation issued shares for consideration in kind, when the "interests" of the corporation required the exclusion of the right (for example, in the case of an IPO, when it is necessary to distribute the shares among many investors in order to be listed on a stock exchange), and in the case of shares issued to employees. Mandatory preemptive rights protect existing shareholders against the risk of dilution, but they might also adversely affect the ability of the corporation to raise funds quickly when market conditions are favorable, if nothing else because the corporation needs to offer the shares to the existing shareholders before other possible investors. The reform of 2003 liberalized this procedure to some extent for listed corporations. It introduced a new basis for limiting preemptive rights: now the bylaws of a listed corporation can exclude the shareholders' preemptive rights for up to ten percent of the existing legal capital, provided that the issuing price equals the market value of the shares and that this prerequisite is verified by a report issued by the auditing firm.[73] This new rule was almost entirely copied from the German corporation law, clearly in an effort to make the financing of Italian listed corporations more flexible and competitive.[74]

71. *Id.*

72. *Id.* at 125.

73. *Id.*

74. *See* Gaia Balp & Marco Ventoruzzo, *Esclusione del Diritto d'Opzione nelle Società con Azioni Quotate nei Limiti del Dieci per Cento del Capitale e Determinazione del Prezzo di Emissione*, 49 RIVISTA DELLE SOCIETÀ 795 (2004) (It.).

V. HARMONIZATION IN EUROPE AND THE ROLE OF COMPARATIVE LAW

Traditionally, European corporate law systems have differed among themselves more than the corporate laws of the individual states in the United States. Notwithstanding the existing differences among U.S. states with respect to their corporate laws, their common legal origins and shared language contribute to create a rather harmonized patchwork of legal rules in this field. On the contrary, the different legal origins and legal systems of Europe have produced corporate statutes with more profound differences. As part of the effort to create a common market, and in order to reduce regulatory arbitrage, the European Union has engaged in a significant effort to harmonize corporate law and securities regulation in Europe.[75] Several directives have contributed to create a common regulatory framework in this area in Europe, notwithstanding that some scholars have dismissed the importance of European law in harmonizing the legal systems of the Member States.[76]

Obviously, European directives are not created out of the blue. They often embrace regulatory solutions adopted in some States, or at least take into account the differences among single jurisdictions in order to create a level playing field. From this perspective, E.U. directives can be influenced by comparative law considerations, and through the harmonizing efforts of the Union, comparative law plays an important role in shaping the corporate laws of the different Member States. In other words, sometimes European law is a "Trojan horse" through which rules and models developed in one system gain entry into others.[77] Of course, as with any legal transplant, this technique has both upsides and downsides.

An excellent example of this dynamic is offered by the Thirteenth Directive on Takeovers ("the Directive"), which finally saw

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75. Christian Kersting, *Corporate Choice of Law--A Comparison of the United States and European Systems and a Proposal for a European Directive*, 28 BROOK. J. INT'L L. 1, 1-2, 51 (2002).

76. Luca Enriques, *EC Company Law Directives and Regulations: How Trivial Are They?*, 27 U. PA. J. INT'L ECON. L. 1 (2006).

77. The image of directives as "Trojan horses" for some rules is used, with respect to the Thirteenth Directive, by Heribert Hirte, *The Takeover Directive: A Mini-Directive on the Structure of the Corporation: Is it a Trojan Horse?*, 2 EUR. COMPANY AND FIN. L. REV. 1 (2005).

the light in 2004 after almost twenty years of discussion.[78] The Directive is in many ways a compromise among the different views of Member States with diverging opinions concerning the role of the market for corporate control. Its two most important pillars are the mandatory tender offer and the board neutrality rule.[79] The mandatory tender offer rule provides that anyone who acquires control of a listed corporation (defined, in most states, as a set threshold of voting shares, generally around thirty percent), is obliged to launch a bid on all the outstanding voting shares at the highest price paid for the shares by the bidder over a period of six to twelve months preceding the acquisition of the requisite threshold.[80] The board neutrality rule, on the other hand, provides that the directors of the target corporation cannot adopt any defensive measure to fend off the takeover without the authorization of the shareholders' meeting.[81] This rule is actually optional in the sense that the bylaws of listed corporations can opt out of it and grant more freedom to incumbent directors in protecting the corporation from hostile acquisitions.

For the purposes of this Essay, it is important to consider that the basic framework of the Directive is modeled after the British takeover regulation. The British approach has become the law all over Europe, once again demonstrating the role of comparative law in the harmonization process.[82] There is, however, an important and interesting twist. In the U.K., due to the existence of widespread ownership structures, most corporations are controlled with a percentage of shares significantly lower than the threshold

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78. Directive 2004/25/EC of the European Parliament and of the Council on takeover bids. On this piece of legislation, see Jesper Lau Hansen, *When Less Would Be More: The EU Takeover Directive in its Latest Apparition*, 9 COLUM. J. EUR. L. 275 (2003); John Elofson, *Lie Back and Think of Europe: American Reflections on the EU Takeover Directive*, 22 WIS. INT'L L.J. 523 (2004); Dmitry Tuchinsky, *The Takover Directive and Inspire Art: Reevaluating the European Union's Market in the New Millenium*, 51 N.Y.L. SCH. L. REV. 689 (2006-2007); Marco Ventoruzzo, *Europe's Thirteenth Directive and U.S. Takeover Regulation: Regulatory Means and Political and Economic Ends*, 41 TEX. INT'L L.J. 171, 203 (2006). On the limited success of the directive in harmonizing the regulation of takeovers in Europe, especially with respect to defensive measures, see Andrew Zwecker, *The EU Takeover Directive: Eight Years Later, Implementation But Still No Harmonization Among Member States on Acceptable Takeover Defenses*, 21 TUL. J. INT'L & COMP. L. 233 (2012).

79. *See* Ventoruzzo, *supra* note 78, at 191-203, 205-09.

80. *Id.* at 206-07.

81. *Id.* at 208.

82. For a discussion of how the British regulatory paradigm on takeovers has been incorporated into the Thirteenth Directive and therefore, to some degree, transplanted in continental Europe (and the consequences of this transplant), see Marco Ventoruzzo, *Takeover Regulation as a Wolf in Sheep's Clothing: Taking U.K. Rules to Continental Europe*, 11 U. PA. J. BUS. & EMP. L. 135 (2008).

that triggers the mandatory bid.[83] In the U.K., in other words, it is still possible that both friendly and hostile acquisitions occur without any need to launch a tender offer on all the outstanding shares. The rationale of the mandatory tender offer in its country of origin is to grant to shareholders an exit at a fair price when someone acquires a share so large that it makes future (hostile) acquisitions unlikely.

This rule, however, has also been transplanted through the Directive into continental European systems, where ownership structures are more concentrated and the controlling shareholder generally owns more than the triggering threshold of the mandatory tender offer.[84] One of the possible unintended consequences of the mandatory tender offer, therefore, is to operate as a sort of statutory defensive measure in favor of existing controlling shareholders. In fact, whoever intends to acquire control must be ready to buy all of the outstanding shares – a significant financial burden. Interestingly enough, the European mandatory offer rule resembles quite closely some of the anti-takeover statutes or measures adopted in the U.S. and mentioned above.[85]

A similar observation can be made with respect to the board neutrality rule. In the U.K., first of all, directors generally have greater freedom than their continental European counterparts to adopt defensive measures.[86] On the other hand, in continental Europe, general corporate laws give the shareholders control over several of the most typical defenses, such as issuing new shares or approving a merger.[87] In this respect, therefore, one might argue that in continental European systems the board neutrality rule did not change the normal division of competencies between the board and the shareholders' meeting in a very significant way. But there is more: due to the presence of a strong controlling shareholder, in these countries the fact that the shareholders'

83. *Id.* at 139-43.

84. *Id.*

85. *See supra* Part II.A.

86. Even if, as persuasively argued by David Kershaw, *The Illusion of Importance: Reconsidering the UK's Takeover Defence Prohibition*, 56 INT'L & COMP. L.Q. 267 (2007), in the U.K. most defensive measures would require shareholders' approval also in the absence of the board neutrality rule, due to the application of general corporate law rules.

87. On the competences of shareholders vis-à-vis directors in some continental European systems, see Ventoruzzo, *supra* note 69, at 130; Ignacio Lojendio Osborne, *La Junta general de accionistas, in* DERECHO MERCANTIL 344 (Guillermo J. Jiménez Sánchez ed., 2006); MAURICE COZIAN, ALAIN VIANDIER & FLORENCE DEBOISSY, DROIT DES SOCIÉTÉS 223 (2006); *see also* GERHARD WIRTH, MICHAEL ARNOLD & MARK GREENE, CORPORATE LAW IN GERMANY 117 (2004).

meeting must approve defensive measures does not take the power to decide whether to resist the takeover away from whoever actually controls the corporation. In fact, it basically gives a say on the adoption of defensive measures to the very subject in conflict with minority shareholders. This result is quite contrary to the experience in the U.K., where the rule was adopted. In this system, due to the prevailing widespread ownership structures and the presence of institutional investors as minority shareholders, letting the shareholders' meeting decide really means taking into account the opinion of minority investors, because the controlling shareholder often does not have enough votes to oppose a value-maximizing offer in order to retain the private benefits of control. Finally, as mentioned above, one of the compromises of the Directive is that the board neutrality rule is optional and corporations can opt out of it. For these reasons, several commentators have questioned whether the directive really empowers minority shareholders in continental European countries as it does in the U.K.[88]

This example shows how the use of comparative law affects the harmonization process of European corporate statutes, but it also shows the possible shortcomings of legal transplants: the effects of a rule developed in a system with certain features can be very different, and have unintended consequences, when the rule is exported to systems with different characteristics.

VI. CONCLUSION

In this Essay we have observed how the evolution of statutory corporate law can be determined by two forces: regulatory competition, generally a spontaneous effort by single legislatures to render their systems more attractive than others; and harmonization, sometimes imposed in a top-down manner. Actually, the distinction between these two "channels" is much more nuanced, and they often intertwine. Regulatory competition can push toward greater harmonization as some states copy the rules developed in other systems, and harmonization can affect the possibility of regulatory arbitrage and, therefore, the level of competition among different jurisdictions to attract corporations. What is interesting, however, is to recognize the powerful role that comparative law, with its tendency to circulate legal models, plays in the case of

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88. *See* Ventoruzzo, *supra* note 82, at 172.

both regulatory competition and harmonization in the U.S. and in Europe.

Often legal reforms are at least partially modeled on foreign experiences. This is sometimes beneficial, as more efficient solutions experimented in one jurisdiction become available in other systems. However, the circulation of models also presents the risk implicit in any legal transplant: similar rules, adopted in different economic contexts, can have very different—sometimes even opposite—effects than the ones they had in their country of origin.

Another conclusion that can be drawn from the discussion is how comparative law in statutory reforms often—and not surprisingly—tends to look more attentively at systems and models that are more similar to the local one. As the reader has noticed, in the U.S. most of the comparative considerations looked at other U.S. states, and the same can be said about European legal reforms. For this reason, it is fair as a final conclusion to observe that "regional comparisons" (i.e., comparisons with systems that are closer geographically, culturally or economically) tend to be the predominant source of legal transplants in corporate law reforms.[89]

In any case, awareness of comparative law is a key element for any statutory innovation. The cases discussed in this Essay demonstrate the role that comparative considerations have always played, and will always play, in the evolution of corporate law, and in particular in case of statutory reforms, both as an instrument of regulatory competition and to support harmonization efforts.

89. Obviously, there are some notable exceptions. It is well known among comparative corporate law scholars, for example, that "[t]he Model Business Corporation Act and the modern Japanese Commercial Code were both created in 1950 and based on the Illinois Business Corporation Act of 1933," as explained in an article by Mark D. West, *The Puzzling Divergence of Corporate Law: Evidence and Explanations from Japan and the United States*, 150 U. PA. L. REV. 527, 527 (2001), even if, as pointed out by Professor West, the systems tended to diverge over the course of the last few decades.