UCLA
UCLA Law & Economics Series

Title
Shareholder Protection Across Time

Permalink
https://escholarship.org/uc/item/0fj3w82h

Authors
Bank, Steven A.
Cheffins, Brian R.
Wells, Harwell

Publication Date
2015

eScholarship.org Powered by the California Digital Library
University of California

Legal Studies Research Paper Series

UNIVERSITY OF CAMBRIDGE
Faculty of Law



PAPER NO. 17/2015

APRIL 2015

Shareholder Protection Across Time

Brian R. Cheffins, Steven A. Bank & Harwell Wells

Further information about the University of Cambridge Faculty of Law Legal Studies Research Paper Series can be found at http://www.law.cam.ac.uk/ssrn/

Electronic copy available at: https://ssrn.com/abstract=2595693
Electronic copy available at: http://ssrn.com/abstract=2595693

Shareholder Protection Across Time

Brian R. Cheffins[a]

Steven A. Bank[b]

Harwell Wells[c]

(to be published in the *University of Florida Law Review*)

Abstract

This Article offers the first systematic attempt to measure the development of shareholder protection in the United States across time. Using three indices developed to measure the relative strength of shareholder protection across nations, we evaluate numerically the protections corporate and securities law have offered shareholders from the beginning of the twentieth century to the present day. We do so by tracking the rights accorded to shareholders across time under three important sources of corporate law, Delaware and Illinois and the Model Business Corporation Act.

Our novel study yields novel results. First, we find that the protections afforded to shareholders by state corporation law have decreased since 1900 but only modestly so. This implies that, contrary to the assumptions of many scholars, state competition in corporate law has not significantly eroded shareholder rights. Second, when we add in measures that count protections provided by federal as well as state law, we find that shareholder protection improved across time. This implies that federal intervention has played a crucial and perhaps underappreciated role in shaping U.S. corporate law. Beyond its specific findings, this study illustrates how empirical analysis of legal trends provides scholars with a new means for analyzing and resolving fundamental questions in corporate law.

Keywords: corporate law; shareholder protection; leximetrics; regulatory competition

JEL Codes: G38, K22, N22

[a] S. J. Berwin Professor of Corporate Law, University of Cambridge, Faculty of Law.

[b] Paul Hastings Professor of Business Law, UCLA School of Law.

[c] Associate Professor of Law, James E. Beasley School of Law, Temple University.

This is a substantially revised version of Brian R. Cheffins, Steven A. Bank and Harwell Wells, *The Race to the Bottom Recalculated: Scoring Corporate Law Over Time*, available at http://ssrn.com/abstract=2475242 (2014). The authors are grateful for feedback from Stephen Bainbridge, Marcel Kahan, Lynn LoPucki and Mathias Siems and participants at a seminar at Harvard Business School as well as for the research assistance of Nathan Davis, Brendan Mace, Samuel Moniz, and Padideh Zargari

Electronic copy available at: https://ssrn.com/abstract=2595693
Electronic copy available at: http://ssrn.com/abstract=2595693

Table of Contents

I. Introduction

II. Methodology

- **A. Selecting the Indices**
- **B. Selecting the Legal Regimes**
- **C. Coding Protocol – In General**
- **D. The Relevant Variables**
  - **1. ADRI**
  - **2. ASDI**
  - **3. CBR SPI**
- **E. Which Types of Rules Qualify?**
- **F. Who Made the Rules?**

III. Hypotheses and Findings

- **A. Hypotheses**
- **B. Present-Day Scores**
  - **1. ADRI**
  - **2. ASDI**
  - **3. CBR SPI**
- **C. Historical Trends**
  - **1. ADRI**
  - **2. ASDI**
  - **3. CBR SPI**
- **D. Our Hypotheses Revisited**

IV. "Present-Day" Bias?

- **A. Reasons for Concern**
- **B. What Shareholder Rights Mattered in 1929?**
- **C. What Shareholder Protections Were Displaced?**

V. Conclusion

Electronic copy available at: https://ssrn.com/abstract=2595693
Electronic copy available at: http://ssrn.com/abstract=2595693

I. INTRODUCTION

This Article constitutes the first systematic attempt to measure the development of shareholder protection in the United States across time. The study is set against a background of strong presumptions concerning both present levels of protection and trends over time. Corporate law scholars tend to assume that shareholders in U.S. public companies are poorly protected in relation to their peers in comparable countries. Lucian Bebchuk, in a 2005 article, argued in favor of increasing the power of shareholders in U.S. corporations on the grounds that "the corporate law system of the United States is the one that stands out among the corporate law systems of developed countries in how far it goes to restrict shareholder initiative and intervention."[1] Martin Gelter suggested in a 2009 article that U.S. corporate and securities law is "highly unusual in the extent to which it disenfranchises shareholders from both explicit and implicit influence."[2] Christopher Bruner, in a 2013 book in which he contrasted corporate governance arrangements in the United States with those in a number of other common law countries, indicated "The defining attributes of U.S. corporate law are shareholders' marginal role and very weak governance powers…."[3]

Underlying this view that U.S. shareholder protection is relatively weak is the assumption that the current situation is the product of a decline in shareholder rights across time. For instance, William Roy observed in a 1997 book on the rise of the industrial corporation that "From the post-Civil War period onward stockholders and directors have gone to battle over many issues, and the directors have usually won."[4] Mary Sullivan argued similarly in a 2007 article on the historical development of stock markets in the United States

---

1 Lucian A. Bebchuk, *The Case for Increasing Shareholder Power*, 118 HARV. L. REV. 833, 848 (2005).

2 Martin Gelter, *The Dark Side of Shareholder Influence: Managerial Autonomy and Stakeholder Orientation in Comparative Corporate Governance*, 50 HARV. INT'L L.J. 129, 134 (2009).

3 CHRISTOPHER M. BRUNER, CORPORATE GOVERNANCE IN THE COMMON-LAW WORLD: THE POLITICAL FOUNDATIONS OF SHAREHOLDER POWER 37 (2013).

4 WILLIAM G. ROY, SOCIALIZING CAPITAL: THE RISE OF THE LARGE INDUSTRIAL CORPORATION IN AMERICA 158 (1997).

Electronic copy available at: https://ssrn.com/abstract=2595693

"…the statutory rights accorded to shareholders substantially diminished during the period 1885-1930."[5] Or as Julian Velasco said in a 2006 article on shareholder rights, "The history of corporate law has been one of increasing flexibility for directors and decreasing rights for shareholders."[6]

If shareholder protection has indeed eroded over time, the logical culprit is the U.S.'s state-based system of corporate law. Companies are incorporated under the laws of one of the fifty states rather than under a federal statute and a business can incorporate in a state other than the one in which it is headquartered.[7] States correspondingly can and at least to some extent do compete for incorporation business by altering their corporate law to attract incorporations, with Delaware being the clear winner.[8] The regulatory competition which is a feature of U.S. corporate law has been the source of widespread and enduring debate amongst corporate law scholars,[9] with more than half of all law review articles on corporate law engaging with the topic.[10] There has been vigorous disagreement whether the "race" between the states has been to the "bottom," in the sense that states competed by adopting

---

5 Mary O'Sullivan, *The Expansion of the U.S. Stock Market, 1885-1930: Historical Facts and Theoretical Fashions*, 8 ENTERPRISE & SOC'Y 489, 529 (2007).

6 Julian Velasco, *The Fundamental Rights of the Shareholder*, 40 U.C. DAVIS. L. REV. 407, 409 (2006).

7 JAMES D. COX AND THOMAS LEE HAZEN, THE LAW OF CORPORATIONS, § 3.02 (3rd ed., 2010); see also Part II.A, *infra*.

8 Lucian A. Bebchuk and Assaf Hamdani, *Vigorous Race or Leisurely Walk: Reconsidering the Competition Over Corporate Charters*, 112 YALE L.J. 553, 554, 561 (2002) [hereinafter Bebchuk & Hamdani, *Vigorous Race*]; Mark J. Roe, *Is Delaware's Corporate Law Too Big to Fail?*, 74 BROOKLYN L. REV. 75, 76 (2008) [hereinafter Roe, *Is Delaware*]; John Armour, Bernard Black and Brian Cheffins, *Delaware's Balancing Act*, 87 IND. L.J. 1345, 1346, 1348 (2012).

9 Lucian A. Bebchuk and Assaf Hamdani, *Federal Corporate Law: Lessons from History*, 106 COLUM. L. REV. 1793, 1794 (2006) [hereinafter Bebchuk & Hamdani, *Federal Corporate Law*]; see also Marcel Kahan, *The State of State Competition for Incorporations*, NYU LAW AND ECONOMICS RESEARCH SERIES, Working Paper No. 14-19 3 (2014) ("The competition by states for incorporations has long been the subject of extensive scholarship"); Daniel J.H. Greenwood, *Democracy and Delaware: The Mysterious Race to the Bottom/Top*, 23 YALE L. & POL'Y REV. 381, 381 (2009) ("Corporate law scholarship has focused on the role of the state as competitive actors in producing corporate law"); Robert B. Ahdieh, *Trapped in a Metaphor: The Limited Implications of Federalism for Corporate Governance*, 77 GEO. WASH. L. REV. 255, 257 (2009) [hereinafter Ahdieh, *Trapped*] (referring to "the corporate law literature's singular emphasis on a race among the states").

10 Robert B. Ahdieh, *The (Misunderstood) Genius of American Corporate Law*, 77 GEO. WASH. L. REV. 730, 731-32 (2009) (indicating that in a search of articles published in leading law reviews, almost three-quarters referred to one of a series of topics relevant to regulatory competition).

Electronic copy available at: https://ssrn.com/abstract=2595693

counterproductively manager-friendly laws, or the "top," in the sense that states competed by adopting laws that served investors' interests.[11] It has been generally accepted, though, that the race has resulted in a net reduction in the rights corporate law provided to shareholders, either because states were cynically watering down existing shareholder protection to appeal to managers (i.e., racing to the bottom) or because states were displacing superfluous or inefficient rules (i.e., racing to the top).[12]

While the general consensus has been that the Delaware-led competition between the states in the corporate law realm has prompted a substantial erosion of shareholder rights and thus shareholder protection, there have been dissenting voices. Walter Werner argued in a 1977 article that over the previous four decades "[s]hareholders' legal rights within the corporation have been made meaningful."[13] Edward Herman suggested similarly in 1984 that "corporate standards of behavior and attention to the welfare of the shareholders are substantially greater than they were in 1925."[14] Bringing the story up-to-date, the success that activist hedge funds have had in challenging boards of publicly traded companies in recent years suggests shareholders are hardly weaklings under U.S. corporate law. For instance, the *New York Times* said in 2014 of these shareholder insurgents, "They have

---

[11] *Compare* William L. Cary, *Federalism and Corporate Law: Reflections Upon Delaware*, 83 YALE L. J. 663, 701 (1974) (arguing that there was a race to the bottom) and Ralph K. Winter, Jr., *State Law, Shareholder Protection, and the Theory of the Corporation*, 6 J. LEGAL STUD. 251, 275-76 (1977) (responding to Cary with what became known as the race to the top hypothesis); ROBERTA ROMANO, THE GENIUS OF AMERICAN CORPORATE LAW 21 (1993) (providing support for the race to the top hypothesis). For further discussion of this debate, *see* Roe, *Is Delaware*, *supra* note 8, at 76-77; J. Robert Brown, *The Irrelevance of State Corporate Law in the Governance of Public Companies*, 38 U. RICH. L. REV. 317, 324, (2004).

[12] Roe, *Is Delaware*, *supra* note 8, at 76-77; Ahdieh, *Trapped*, *supra* note 9, at 263 (indicating that a leading critic of the "race to the bottom" view did not dispute the "observation of declining levels of shareholder protection").

[13] Walter Werner, *Management, Stock Market and Corporate Reform: Berle and Means Reconsidered*, 77 COLUM. L. REV. 388, 398 (1977).

[14] Edward S. Herman, *The Limits of the Market as a Discipline in Corporate Governance*, 9 DEL. J. CORP. L. 530, 538 (1984).

Electronic copy available at: https://ssrn.com/abstract=2595693

amassed huge war chests to take on some of the biggest names in corporate America – and win more often than not."[15]

Werner and Herman both drew attention to federal securities legislation, first introduced in the mid-1930s,[16] to buttress their claims that shareholder protection had become more robust during the 20th century. Recognition of the federal dimension has more recently shifted fundamentally the terms of debate on the merits of regulatory competition in the corporate law realm. In particular, Mark Roe reframed the discourse when he argued in the mid-2000s that actions of the federal government on the corporate governance front had done more to shape Delaware corporate law than had potential competition from other states.[17]

Roe's contribution to the literature, while insightful and influential, raises at least two significant, and as yet unanswered, questions. First, has Washington's contribution to the shape of U.S. corporate law in fact been pivotal or only a side-show? Second, assuming that competition between states has over time diminished the rights corporate statutes provide to shareholders, has federal intervention bolstered shareholder protection sufficiently to cancel out moves in the other direction at state level?

With respect to the first question, Roe argues "[t]here is a large federal presence in corporate law,"[18] but this claim has been contested. Roberta Romano, for instance, has challenged what she has referred to as "the federal supremacy hypothesis," saying that the dynamics of corporate law in the United States can still be explained best by the working of

---

15 Michael J. de la Merced and Alexandra Stevenson, *Sotheby's Yields to Hedge Fund Mogul and Allies*, N.Y. TIMES, May 6, 2014, B1.

16 *Infra* notes 112 to 113 and related discussion.

17 Mark J. Roe, *Delaware's Competition*, 117 HARV. L. REV. 588 (2003); Mark J. Roe, *Delaware's Politics*, 118 HARV. L. REV. 2491 (2005). On the nature of Roe's contribution to the discourse, see Note, *The Case for Federal Threats in Corporate Governance*, 118 HARV. L. REV. 2726, 2726 (2005) ("reframed (the) debate"); Lawrence A. Hamermesh, *The Policy Foundations of Delaware Corporate Law*, 106 COLUM. L. REV. 1749, 1767 (2006) ("pathbreaking observation").

18 Mark J. Roe, *Delaware and Washington as Corporate Lawmakers*, 34 DEL. J. CORP. L. 1, 33 (2009) [hereinafter Roe, *Delaware and Washington*].

Electronic copy available at: https://ssrn.com/abstract=2595693

competition between states.[19] Law professors Marcel Kahan and Ed Rock struck a middle ground in a 2005 article, suggesting the federal "threat" to Delaware is only potent at moments when, due to the political climate, federal lawmakers can reap populist political dividends by supporting corporate governance reform.[20]

With the second question, again there is disagreement. According to some observers, the interaction of state-based corporate law and periodic federal intervention provides shareholders with ample and appropriate protection. Brett McDonnell has suggested the U.S.'s mixed system of state and federal corporate law produces under many circumstances results better than a pure state or pure national system would yield.[21] Leo Strine, Chief Justice of the Delaware Supreme Court, maintains that investors benefit from a combination of Delaware courts enforcing fiduciary duties expertly and the federal government vigorously policing laws mandating disclosure to investors.[22]

Others are less sanguine. Lucian Bebchuk and Assaf Hamdani argue that, even when federal intervention is taken into account, "regulatory competition tends to produce insufficient investor protection."[23] J. Robert Brown maintains similarly that "neither the states nor the federal government adequately regulates the behavior of officers and directors."[24]

---

19 Roberta Romano, *Is Regulatory Competition a Problem or Irrelevant for Corporate Governance?*, 21 OXFORD. REV. ECON. POL'Y 212, 213, 223 (2005) [hereinafter Romano, *Regulatory Competition*].

20 Marcel Kahan and Edward Rock, *Symbiotic Federalism and the Structure of Corporate Law*, 58 VAND. L. REV. 1573, 1576 (2005) [hereinafter Kahan and Rock, *Symbiotic Federalism*].

21 Brett H. McDonnell, *Recent Skirmishes in the Battle Over Corporate Voting and Governance*, 2 J. BUS. & TECH. L. 349, 353 (2007). *See also* Kahan and Rock, *Symbiotic Federalism*, *supra* note 20, at 1622 ("[Federal] regulations help ward-off crises and thus provide a lightning rod for a populist backlash that could produce severe harm to Delaware's position as the creator of our de facto national corporate law").

22 Leo E. Strine, *The Delaware Way: How We Do Corporate Law and Some of the New Challenges We (and Europe) Face*, 30 DEL. J. CORP. L. 673, 686 (2005).

23 Bebchuk and Hamdani, *Federal Corporate Law*, *supra* note 9, at 1796.

24 Brown, *supra* note 11, at 320-21.

Electronic copy available at: https://ssrn.com/abstract=2595693

Empirical analysis of the development of U.S. corporate law across time could help to resolve the foregoing controversies. As Todd Henderson has suggested, empirical research could bring "the debate down to the level of the real-world merits and applicability of…conflicting visions of corporate law."[25] Nevertheless, until now only a tiny handful of studies have attempted to measure quantitatively changes in U.S. corporate law across time and those studies have typically sought to measure the pace of change rather than to quantify the level of protection afforded to shareholders.[26] In this Article we break new ground with a pioneering empirical analysis that provides insights concerning the evolution of shareholder rights across time. We do so by measuring the evolution of shareholder protection from 1899 to the present day using tools developed to engage in quantitative measurement of law ("leximetrics").[27]

To execute our historically-based leximetric analysis of the development of shareholder protection we draw upon methodologies developed by academics researching comparative corporate governance. In particular, we rely on three indices constructed to measure aspects of corporate law across borders. These are a six element "anti-director rights index" (ADRI), an "anti-self-dealing index" (ASDI), and a 10 variable shareholder protection index constructed by an academic team associated with the Cambridge, U.K.-based Centre for Business Research (CBR SPI).[28] We use each of these indices to measure shareholder

---

25 M. Todd Henderson, *Two Visions of Corporate Law*, 77 GEO. WASH. L. REV. 708, 713 (2009).

26 See Brian R. Cheffins, Steven A. Bank, and Harwell Wells, *Law and History by Numbers: Use, But With Care*, [2014] U. ILL. L. REV. 1739, 1742-43 [hereinafter Cheffins, Bank, and Wells, *Law by Numbers*], discussing William J. Carney, *The Production of Corporate Law*, 71 S. CAL. L. REV. 715 (1998); Roberta Romano, *The States as a Laboratory: Legal Innovation and State Competition for Corporate Charters*, 23 YALE J. ON REG. 209 (2006) [hereinafter Romano, *States as a Laboratory*].

27 Priya P. Lele and Mathias Siems, *Shareholder Protection: A Leximetric Approach*, 7 J. CORP. L. STUD. 17, 18 (2007) (hereinafter *Shareholder Protection I*). The term "leximetrics," described as the "systematic quantitative analysis of law," was apparently coined in a 2003 working paper by Robert Cooter and Tom Ginsburg, *Leximetrics: Why the Same Laws are Longer in Some Countries than Others*, U. OF ILLINOIS LAW & ECONOMICS WORKING PAPER LE03-012 (June 2003).

28 Mathias Siems, *Shareholder Protection Around the World (Leximetric II)*, 33 DEL. J. CORP. L. 111 (2008) [hereinafter Siems, *Shareholder Protection II*].

Electronic copy available at: https://ssrn.com/abstract=2595693

protection under three different corporate law regimes: Delaware, Illinois and the Model Business Corporations Act ("Model Act"), the model statute promulgated by the Committee on Corporate Laws of the Section of Business Law of the American Bar Association that more than 30 states have adopted in whole or substantial part.[29]

To anticipate, our empirical analysis casts doubt on some aspects of the received wisdom concerning regulatory competition in the corporate law realm while affirming others. Some caution is warranted in drawing inferences from our results. As we have acknowledged in prior related work, deploying leximetrics to measure U.S. corporate law accurately is challenging, particularly when one goes back through time.[30] Nevertheless, leximetric analysis should be capable of generating sufficiently accurate scores to identify quantitatively key trends.[31] Correspondingly, the empirical analysis in which this Article engages is a valuable benchmarking exercise that provides novel insights concerning the development of shareholder protection over time.

Part II of the Article sets the scene for our leximetric analysis. It explains why we chose the jurisdictions we did. It also describes our leximetric methodology, doing so in part by summarizing who makes law under the United States' system of corporate law federalism.

The leximetric analysis occurs in Part III, which identifies formally the hypotheses we test, sets out the present day ADRI, ASDI and CBR SPI scores for Delaware, Illinois and the Model Act and concludes by describing our historical results. Our core findings are that state law protections of shareholders have diminished since 1900, but not substantially, and

---

29 See *infra* note 58.

30 Cheffins, Bank and Wells, *Law by Numbers*, *supra* note 26, at 1763.

31 *Ibid.*

Electronic copy available at: https://ssrn.com/abstract=2595693

that shareholder protection overall *increased* over time due to a federally-prompted surge in shareholder rights.[32]

With respect to state law trends, ADRI scores, which are governed purely by state law, drop over time but generally only modestly. This trend is what would be anticipated, given that competition between states on the corporate law front has reputedly eroded shareholder rights. On the other hand, the modest rate of change indicates there was not much of a "race" between states in the period we covered.

When we take into account the federal angle using the ASDI and the CBR SPI, we find that federal intervention not only was significant but, contrary to what one would expect if vigorous state competition was eroding shareholder rights generally, more than offset any erosion of shareholder protection at the state level. Specifically, whereas the state-law based ADRI scores of Delaware, Illinois and the Model Act dropped, albeit modestly, from 1899 onwards, the aggregate ASDI and CBR SPI scores for these jurisdictions, which measure aspects of federal as well as state law, *increased* over time, dramatically in the case of the CBR SPI. Moreover, once federal reforms, introduced either directly by the federal government or by national stock exchanges working in tandem with federal regulators, are taken into account, the level of shareholder protection the U.S. currently offers is, contrary to what observers such as Bebchuk, Bruner and Gelter imply, quite high by global standards.

Part IV of the Article offers a robustness check of our findings. One point we make in Part IV is that while the indices we focus on have only been developed over the past two decades they provide a suitable departure point for analyzing trends extending back more than a century. We do this in part by using as a benchmark a 14-point list of shareholder rights promulgated in 1929, thereby countering the possibility that the variables in the indices

[32] We partially anticipated these findings in prior work. *See* Brian R. Cheffins, Steven A. Bank, and Harwell Wells, *Questioning "Law and Finance": U.S. Stock Market Development, 1930-70*, 55 BUS. HIST. 598, 605 (2013) [hereinafter Cheffins, Bank & Wells, *Questioning*].

Electronic copy available at: https://ssrn.com/abstract=2595693

we use are too modern in orientation to rely upon for historical analysis. We also identify key changes to state law occurring during the 20th century to ascertain whether reform displaced the protection of shareholders in fundamental ways not captured by our indices or by the 1929 14-point list. Our analysis suggests, corroborating what our indices reveal about trends concerning state law, that while there was erosion of some forms of shareholder protection arising under state law, there was no decisive curtailing of shareholder rights. It seems that if the rights corporate law provided to shareholders were ever compromised markedly, this occurred primarily as the 19th century drew to a close, rather than continuing during the 20th century.

Part V concludes. Here we underscore the contributions the Article makes to theoretical debates concerning corporate law. We also acknowledge that we are leaving it to others to gauge the normative implications of the trends we have identified empirically.

II. METHODOLOGY

A. Selecting the Indices

In the mid-1990s, as corporate governance first emerged as a topic of international interest,[33] academics began to develop indices to quantify the protection the corporate laws of various countries offered investors. These efforts have continued to the present day. Here we deploy three different indices originally developed for cross-country comparison to examine the development of U.S. corporate law over time.

There are several reasons we chose to rely on existing indices rather than construct an entirely new one of our own. First, there is familiarity. The audience for this Article is likely to be aware already of one or more of the indices we use, which will increase the accessibility

[33] On the relevant chronology, see Brian R. Cheffins, *The History of Corporate Governance* in THE OXFORD HANDBOOK OF CORPORATE GOVERNANCE 46, 56-58 (Mike Wright, Donald Siegel, Kevin Keasey and Igor Filatotchev, eds., 2013).

Electronic copy available at: https://ssrn.com/abstract=2595693

of our results. Second, drawing upon existing indices means our Article "speaks the same language" as the modern literature on quantitative analysis of corporate law. Correspondingly, future scholars will be able to compare readily our historically-oriented results with those for a wide range of present-day jurisdictions. Third, relying on existing indices saves us from the distraction of having to make the case that our new index is superior to previous indices. We can correspondingly focus our energy on correct historical coding rather than index comparison.

The first of the three indices we deploy is the six element anti-director rights index. It was constructed in the mid-1990s by financial economists Rafael La Porta, Florencio López-de-Silanes, Andrei Shleifer, and Robert Vishny.[34] The second is an anti-self-dealing index which La Porta, López-de-Silanes, and Shleifer developed in the mid-2000s with Simeon Djankov. It focuses on regulation of transactions between a company and those who control it.[35] The third is a 10 variable shareholder protection index Mathias Siems initially constructed in the late 2000s in tandem with an academic team associated with the Cambridge, U.K.-based Centre for Business Research.[36]

Combining discussion of these indices by multi-author groups in the manner we do results in deployment of a slew of acronyms referring to both indices and authors. At the risk of some confusion to the reader we proceed because usage of the various acronyms has become standard in the scholarly literature. For the sake of clarity, the key acronyms we

---

[34] The ADRI was initially fully deployed in a published paper in Rafael La Porta, Florencio López-de-Silanes, Andrei Shleifer and Robert Vishny ("LLSV"), *Law and Finance*, 106 J. POL. ECON. 1113 (1998). Aworking paper version was distributed in 1996 as part of the NBER Working Paper Series: http://www.nber.org/papers/w5661.pdf.

[35] Simeon Djankov, Rafael La Porta, Florencio López-de-Silanes and Andrei Shleifer, *The Law and Economics of Self-Dealing*, 88 J. FIN. ECON. 430, 442, 454 (2008) [hereinafter DLLS, *Law and Economics*]. A working paper version of this article was distributed in 2005 as part of the NBER Working Paper Series: http://www.nber.org/papers/w11883.

[36] *See generally* Siems, *Shareholder Protection II*, *supra* note 28.

Electronic copy available at: https://ssrn.com/abstract=2595693

deploy are set out in Table 1. Drawing the elements together, LLSV produced the ADRI; DLLS produced the ASDI; and Siems/CBR produced the CBR SPI.

Table 1: List of Acronyms

Index/Author Group	Acronym
Anti-Director Rights Index	ADRI
Rafael La Porta, Florencio López-de-Silanes, Andrei Shleifer, and Robert Vishny,	LLSV
Anti-Self-Dealing Index	ASDI
Simeon Djankov, Rafael La Porta, Florencio López-de-Silanes and Andrei Shleifer	DLLS
Shareholder protection index constructed by the Centre for Business Research	CBR SPI
Mathias Siems and the CBR academic team that constructed the CBR SPI	Siems/CBR

Why did we choose each index? With the ADRI, its wide acceptance strongly influenced us. The publication of the original ADRI in a 1998 article sparked the development of a rapidly burgeoning "law and finance" literature oriented around quantitative comparative analysis which aims to trace the relationship between nations' laws and legal institutions, on the one hand, and corporate governance outcomes, on the other.[37] In the law and finance realm, the ADRI has achieved the greatest prominence with respect to the measurement of corporate law.[38] As far back as 2010, over a hundred academic papers had used the ADRI to test theories concerning the interaction between law and markets.[39] Correspondingly, with our quantitative analysis of the historical development of U.S. corporate law the ADRI was an obvious metric to deploy.

---

[37] For an overview of the literature and its popularity, see John Armour, Simon Deakin, Priya Lele and Mathias Siems, *How Do Legal Rules Evolve? Evidence from a Cross-Country Comparison of Shareholder, Creditor and Worker Protection*, 58 AM. J. COMP. L. 579, 582-85 (2009).

[38] Lucian Bebchuk and Assaf Hamdani, *The Elusive Quest for Global Corporate Governance Standards*, 157 U. PA. L. REV. 1263, 1276 (2009) (saying of the ADRI it was "[a]mong academic researchers the most influential metric for evaluating governance arrangements worldwide.")

[39] Holger Spamann, *The "Antidirector Rights Index" Revisited*, 23 REV. FIN. STUD. 467, 468 (2010) [hereinafter Spamann, *Antidirector*].

Electronic copy available at: https://ssrn.com/abstract=2595693

Relying solely on the ADRI could, however, yield a seriously incomplete picture. This index fails to take into account numerous key corporate law topics, including powers shareholders have to remove directors, the scope shareholders have to exercise managerial powers and the legality of takeover defences.[40] It is hardly surprising that the ADRI is not comprehensive, given that it only has six components. The problem is compounded, however, because of the manner in which the components were selected. Several years after the ADRI was first developed, three of its creators, La Porta, López-de-Silanes, and Shleifer, writing in tandem with Simeon Djankov, conceded that the ADRI was "based on an ad hoc collection of variables."[41] The ADRI in isolation is thus a less than ideal proxy for the level of protection corporate law has provided for shareholders over time.

Djankov, La Porta, López-de-Silanes, and Shleifer, when they criticized the original ADRI, were putting forward a second index designed to measure shareholder protections, the ASDI. There are good reasons why the ASDI should be part of a project to code shareholder protection historically.[42] First, DLLS explicitly proffered this index as a superior alternative to the ADRI, saying that the ASDI dealt "with corporate self-dealing in a more theoretically grounded way."[43] Second, in empirical tests DLLS ran on the relationship between stock market development and corporate law the ASDI delivered more robust results than the ADRI.[44] Third, the ASDI has proven popular in its own right among those carrying out

---

40 Lele and Siems, *Shareholder Protection I*, *supra* note 27, 20-21; Detlev Vagts, *Comparative Company Law – The New Wave* in FESTSCHRIFT FÜR JEAN NICOLAS DRUEY 595, 601 (Rainer J. Schweizer, Herbert Burkert and Urs Gasser, eds., 2002).

41 DLLS, *Law and Economics*, *supra* note 35, at 432.

42 For a more detailed analysis, see Cheffins, Bank and Wells, *Law by Numbers*, *supra* note 26, at 1751-52.

43 DLLS, *Law and Economics*, *supra* note 35, at 432.

44 *Id*. at 456.

Electronic copy available at: https://ssrn.com/abstract=2595693

empirical law and finance research and could indeed be supplanting the ADRI as the most accepted numerical measure of the quality of corporate law.[45]

Whatever the merits of the ASDI are in comparison with the ADRI, because of its narrowness the ASDI is, in isolation, an insufficient measure of shareholder protection for our purposes. The ASDI addresses a solitary legal topic, the regulation of related party transactions involving a company and its dominant shareholder, who is also a director. The underlying scenario is a classic example of the sort of conflict of interest that can bedevil corporations.[46] Nevertheless, it is unrealistic to be confident that regulation of this particular topic will be broadly representative of the level of protection corporation law affords to shareholders.

While the narrow scope of the ASDI partly compromises its utility, breadth of coverage provides a compelling rationale for including the third index, the CBR SPI, in our inquiry. The CBR SPI we deploy encompasses 10 variables, selected by the index's creators partly on the basis that the variables represented the full range of shareholder protections used in the countries coded.[47] Correspondingly, the CBR SPI is potentially a more reliable proxy for shareholder protection levels than either the ADRI or the ASDI.

Although the range of issues the CBR SPI addresses is wider than those covered by the ADRI or ASDI, it would be imprudent for us to use the CBR SPI as the exclusive measure of corporate law for our historically-related leximetric exercise. One consideration

---

45 Cheffins, Bank, and Wells, *Law by Numbers*, *supra* note 26, at 1752.

46 Mary A. Jacobson, *Interested Director Transactions and the (Equivocal) Effects of Shareholder Ratification*, 21 DEL. J. CORP. L. 981, 986-87 (1996); Eric G. Orlinsky, *Corporate Opportunity Doctrine and Interested Director Transactions: A Framework for Analysis in an Attempt to Restore Predictability*, 24 DEL. J. CORP. L. 451, 453 (1999).

47 Siems, *Shareholder Protection II*, *supra* note 28, at 119; John Armour, Simon Deakin, Prabirjit Sarkar, Mathias Siems and Ajit Singh, *Shareholder Protection and Stock Market Development: An Empirical Test of the Legal Origins Hypothesis*, 6 J. EMPIRICAL LEGAL STUD. 343, 355 (2009) [hereinafter Armour *et al.*, *Shareholder*]. The initial CBR SPI was a highly detailed 60 variable index coded for five countries: Lele and Siems, *Shareholder Protection I*, *supra* note 27, at 45-49.

Electronic copy available at: https://ssrn.com/abstract=2595693

is that, whatever the CBR SPI's merits might be as a corporate law index, it is not as well-known and has not been as influential as the ADRI and ASDI.[48] Also, the CBR SPI's designers selected variables thought to form the core of international corporate governance "best practice" between 1995 and 2005.[49] In so doing they intentionally focused on a period when proposals to strengthen shareholder protection were high on the policy agenda in numerous countries and deliberately biased the selection of variables in favor of ones they expected would exhibit a relatively high degree of change during the decade they focused on.[50] No explicit equivalent "present-day" bias affects the ADRI and ASDI, meaning that for a historically oriented study such as ours they provide a useful cross-check against this feature of the CBR SPI.

Minimal overlap between the three indices reinforces the utility of each as a cross-check against the others. Neither the ADRI nor the CBR SPI, for example, explicitly addresses rules governing transactions between a corporation and one of its directors or dominant shareholders, which means they cover different ground than the ASDI. There is overlap between the ADRI and the CBR SPI in that they both take into account the extent to which corporate law facilitates shareholder voting by way of proxies and the degree to which the law protects against minority shareholder oppression, defined largely in terms of the procedure governing shareholder derivative suits.[51] However, a majority of the six topics the

---

48 The number of citations each of the papers where the indices were initially deployed provides an admittedly crude illustration of this point: LLSV, *supra* note 34 (14,966 citations); DLLS, *Law and Economics*, *supra* note 35 (1815 citations); Lele and Siems, *Shareholder Protection I*, *supra* note 27 (163 citations). Cite counts were generated by using Google Scholar.

49 Armour *et al.*, *Shareholder*, *supra* note 47, at 355, 374.

50 *Id.* at 353, 355.

51 The variables comprising both indices are identified individually in Part III.C, *infra*. The regulation of multiple voting rights attached to shares, which is an element of the CBR SPI, was taken account of empirically by LLSV. They did not treat this form of regulation, however, as part of the ADRI: LLSV, *supra* note 34, at 1126-27.

Electronic copy available at: https://ssrn.com/abstract=2595693

ADRI addresses are not components of the CBR SPI.[52] Similarly, the bulk of CBR SPI elements lack an ADRI counterpart.[53]

In sum, in isolation each index we use has drawbacks as a mechanism for measuring the historical development of U.S. corporate law. Nevertheless, taken together the ADRI, ASDI and the CBR SPI canvass a wide range of mechanisms that afford protection to shareholders and collectively should offer a sufficiently representative picture of shareholder rights to allow us to execute a fruitful historical analysis. This may well be the best that can be achieved given the tools at hand. A more exhaustive empirical analysis of corporate law developments impacting upon shareholder rights is unlikely to be feasible since evaluating fully "the substance of state corporation law [is] a daunting task."[54]

B. Selecting the Legal Regimes

When seeking to ascertain trends concerning shareholder protection in the United States it would be unwise to restrict the analysis to one state. As William Roy observed in his 1997 book on the emergence of large industrial corporations, historically "[s]tockholders' rights were actively protected in some states and ignored in others."[55] Yet we also cannot survey all 50 states. Coding corporate law using the three indices we deploy is a labor-intensive process involving not only careful research of the applicable law but also difficult judgment calls on appropriate coding. The challenges multiply with historically-oriented analysis because tracking down relevant statutory provisions, administrative rules and case

---

52 The elements of the ADRI are set out in Table 2, *infra*. To anticipate, the components of the ADRI which are not addressed in the CBR SPI are the rights individual shareholders have to call shareholder meetings, the ability of companies to block share transfers immediately prior to shareholder meetings, the fostering of a director election system known as cumulative voting and "pre-emptive" rights shareholders can be vested with in relation to the issuance of shares.

53 The CBR SPI components are summarized inTable 3, *infra*. The CBR SPI components which are not part of the ADRI are the regulation of shares with multiple voting rights attached, requirements concerning the appointment of independent directors and rules forcing shareholders to make a takeover offer after they have acquired a large minority stake ("mandatory bid").

54 Wells M. Engledow, *Handicapping the Corporate Law Race*, 28 J. CORP. L. 143, 153 (2002).

55 ROY, *supra* note 4, 156.

Electronic copy available at: https://ssrn.com/abstract=2595693

law decisions back to 1900 is often far from straightforward.[56] We have therefore restricted our analysis to three legal regimes, namely Delaware, the Model Act and Illinois. The three we have selected should nevertheless collectively provide a highly representative sampling of trends affecting U.S. corporate law.

Delaware was an obvious choice for us, given that for nearly a century more publicly traded companies have been incorporated under its laws than the laws of any other state.[57] The Model Act was an obvious second choice, given that it has been a highly influential model statute adopted substantially in more than 30 states.[58] Due to the high degree of uniformity between the Model Act and the corporate law statutes of numerous states, it has been referred to as "the backbone of U.S. statutory corporate law."[59]

Illinois we chose primarily to foster continuity in our analysis. We score Delaware's corporate law back to 1899, the year when the state first enacted a new general incorporation statute intended to attract incorporation business.[60] The first Model Act was only produced in 1950, however,[61] so we needed a proxy for developments occurring before its promulgation. We chose Illinois because the Illinois Business Corporations Act of 1933 was the primary precedent for the 1950 Model Act, partly due to the principal drafters of the initial Model Act

---

56 See Siems, *Shareholder Protection II*, *supra* note 28, at 116 ("the compilation and coding of legal rules across time is very complex and time consuming"); Cheffins, Bank, and Wells, *Law by Numbers*, *supra* note 26, 1748-51, 1759-63 (providing examples of the challenges involved with coding historically).

57 Cheffins, Bank and Wells, *Questioning*, *supra* note 32, at 605.

58 MODEL BUS. CORP. ACT, INTRODUCTION, GENERAL DESCRIPTION OF THE MODEL ACT ix (2008) (saying 30 states had adopted all or substantially all of the provisions of the current Act and three others had statutes based on the 1969 version of the MBCA).

59 Mark D. West, *The Puzzling Divergence of Corporate Law: Evidence and Explanations from Japan and the United States*, 150 U. PA. L. REV. 527, 548 (2001); see also Michael P. Dooley and Michael D. Goldman, *Some Comparisons Between the Model Business Corporation Act and the Delaware General Corporation Law*, 56 BUS. LAW. 737, 738 (2001) (referring to "The relatively greater success of the Model Act in terms of adoptions…"); STEPHEN M. BAINBRIDGE, CORPORATE LAW 9 (2d ed. 2009) ("The most important alternative to Delaware law is the American Bar Association's Model Business Corporation Act.").

60 Cheffins, Bank and Wells, *Questioning*, *supra* note 32, at 605.

61 COX & HAZEN, *supra* note 7, § 2.3 ("The Model Act first appeared in completed form in 1950"); Romano, *States as a Laboratory*, *supra* note 26, 236, n. 73 (2006) ("the 1950 revision of (a 1946) draft statute is now considered the first Model Act").

Electronic copy available at: https://ssrn.com/abstract=2595693

being from Illinois.[62] Moreover, the 1933 Illinois legislation was considered to be innovative and influential in its own right[63] and, seemingly contrary to the 20th century trend of states reducing shareholder rights in corporate law,[64] was ostensibly structured to give shareholders more protections than the laws of Delaware and other "chartermongering" states.[65] As with Delaware, we score Illinois law back to 1899.

C. Coding Protocol – In General

For each of the three indices we have deployed the same coding protocol to score shareholder protection going back through time. We began with the present-day score for each of the three corporate law regimes we are focusing on, namely Delaware, the Model Act and Illinois. Having ascertained their present-day scores, we worked backwards to identify changes to the law that would have caused the score for any of the relevant variables to move up or down.

---

62 West, *supra* note 59, at 543; Romano, *States as a Laboratory*, *supra* note 26, at 236, n. 53. *Cf.* Jeffrey M. Gorris, Lawrence A. Hamermesh and Leo E. Strine, *Delaware Corporate Law and the Model Business Corporation Act: A Study in Symbiosis*, 74 LAW & CONTEMP. PROBS. 107, 109 (acknowledging the Illinois influence but saying the statutes the Model Act drafters used as their departure point had been modelled largely on the Delaware General Corporation Law).

63 COX & HAZEN, *supra* note 7, at 140; West, *supra* note 59, at 542-43.

64 *Supra* notes 4-6, *infra* notes 264 to 268 and related discussion.

65 Harwell Wells, *The Modernization of Corporation Law, 1920-1940*, 11 U. PA. J. BUS. L. 573, 594 (2009) [hereinafter Wells, *Modernization*]. While the fact that Illinois has reputedly placed more emphasis on shareholder rights than other states helps to explain why we focus on this jurisdiction, continuity with the Model Act was the key consideration. If our primary concern had been tracing developments in a state with a reputation for protecting shareholders we likely would have chosen California. A significant proportion of the largest U.S. companies are incorporated under California law; as of the mid-2000s 20% of *Fortune* 500 companies were incorporated in California compared with 60% incorporated in Delaware: Matt Stevens, *Internal Affairs Doctrine: California versus Delaware in a Fight for the Right to Regulate Foreign Corporations* 48 BOSTON COLL. L. REV. 1047, 1049 (2007). Also, California has long had a reputation for having corporate law that offered significant protection to shareholders. *See, e.g.*, Francis G. Wilmarth, *Choice of a Corporate Domicile*, 49 CALIF. L. REV. 518, 523-27 (1961); Andrew J. Collins, *Choice of Corporate Domicile: California or Delaware*, 13 U.S.F. L. REV. 103, 106 (1977). On the other hand, California has never been influential as a source of corporate law nationally in the same way as Delaware and the Model Act. See, for example, Guhan Subramanian, *The Influence of Antitakeover Statutes on Incorporation Choice: Evidence on the "Race" Debate and Antitakeover Overreaching*, 150 U. PA. L. REV. 1795, 1854 (2002) (remarking upon California's "poor showing in the market for corporate charters"); Lucian Arye Bebchuk & Alma Cohen, *Firms' Decisions Where to Incorporate*, 46 J.L. ECON. 383, 396 (2003) ("California appears unable to 'sell' its corporate law system to any significant number of out-of-state firms.").

Electronic copy available at: https://ssrn.com/abstract=2595693

With one of our indices, the ADRI, our efforts were complicated by the fact that it has been reworked since its initial deployment. The ADRI LLSV originally promulgated was significantly rescored not once but twice, by DLLS in a 2008 article and by Holger Spamann for a project culminating in an article published the following year.[66] The rationale for recoding and the key differences between the scoring methodologies for each version of this index are discussed in sub-section II.E. It suffices for present purposes to say that we take the scorings by DLLS and Spamann as our departure point and do not take LLSV's analysis into account.

In determining present-day scores for the ADRI, ASDI and CBR SPI, Delaware was the obvious place to start because reliable present-day scoring for Delaware was readily available for all three indices. The ADRI was already scored for Delaware because the authors who developed or reworked that index—LLSV, DLLS and Spamann—had taken Delaware as representative of U.S. corporate law.[67] The ASDI and CBR SPI were also already scored for Delaware because both DLLS and Siems and his Centre for Business Research co-authors likewise treated Delaware as their proxy for U.S. corporate law.[68]

With Delaware's present-day scores we drew verbatim from the work of DLLS, Spamann, and Siems/CBR. Since we adopted the scoring from each source without variation, even if we had qualms about how a particular variable was scored we refrained from recoding. We scored Illinois and the Model Act ourselves, although whenever the applicable rule in these jurisdictions was substantially similar to Delaware's to promote consistency the Delaware coding of DLLS, Spamann and Siems/CBR was used.

---

66 DLLS, *Law and Economics*, supra note 35; Spamann, *Antidirector*, supra note 39.

67 LLSV, *supra* note 34, at 1119; DLLS, *Law and Economics*, *supra* note 35, 454; Spamann, *Antidirector*, *supra* note 39, at 472, n. 12.

68 DLLS, *Law and Economics*, *supra* note 35, at 442 (ASDI); Siems, *Shareholder Protection II*, *supra* note 28, at 120 (CBR SPI).

Electronic copy available at: https://ssrn.com/abstract=2595693

It might be assumed that, given our extensive borrowing from DLLS, Spamann and Siems/CBR, ascertaining present-day scores would be a straightforward exercise. In fact, identifying the suitable scores posed various challenges that influenced the approach we took with historical scoring. The remaining sections in this Part illustrate the point in the course of summarizing the key elements of the ADRI, the ASDI and the CBR SPI and identifying the sources of law that need to be taken into account to code shareholder protection using each index.

D. The Relevant Variables

1. ADRI

To ascertain appropriate present-day coding for our three indices we began by identifying the variables that comprise each index and the basic scoring regime used for each variable. The ADRI, which was constructed and initially deployed by LLSV in a 1998 *Journal of Political Economy* article to compare the protection afforded by corporate law to shareholders in 49 countries,[69] has six variables, each described briefly in Table 2.

Table 2: ADRI Elements

ADRI variable	**Definition**
Vote by Proxy Allowed	The ability of shareholders to mail in a proxy vote, rather than to vote only in person at a meeting of the shareholders.
No Block	The absence of a requirement that shareholders intending to vote their shares at a shareholder meeting deposit those shares before the meeting, rendering them non-transferable.
Cumulative Voting	The availability of cumulative voting, which permits minority shareholders to "bundle" their votes and thereby increases the likelihood they can elect their representatives to the board of directors.
Oppressed Minority	The availability of mechanisms offering relief to minority shareholders who have been oppressed or unfairly prejudiced.
Pre-emptive Rights	Rules obliging a company to give existing shareholders a right of first refusal when new shares are issued.
Ability to Call General Meeting	The ability of shareholders owning 10 per cent or more of a company's shares to

[69] LLSV, *supra* note 34.

Electronic copy available at: https://ssrn.com/abstract=2595693

	call an extraordinary shareholders' meeting

LLSV, in their 1998 study, awarded jurisdictions either "0" or "1" with respect to each variable, with a higher cumulative score for a country signalling a more shareholder-friendly legal regime. The maximum score any country could receive was "6", though "5" in fact was the highest score LLSV awarded in their 1998 paper.[70] When DLLS recoded the ADRI for 49 countries for the purposes of their 2008 article, they scored the law as of 2003.[71] The highest score they awarded remained "5."[72] The DLLS recoding, however, changed quite often the scores awarded to individual countries for particular variables, with the correlation with the original LLSV coding being 0.60.[73] Also, while LLSV scored each ADRI variable as either "0" or "1", DLLS were prepared with the oppressed minority shareholder variable to award a score of 0.5 where this improved the accuracy of coding.[74]

2. ASDI

For DLLS the primary purpose of their 2008 article was not to recode the ADRI but rather to deploy a new measure of corporate law, the ASDI, for which they assessed the law of 72 countries.[75] The departure point for coding the ASDI is a hypothetical transaction that implicates self-dealing. The transaction involves Buyer Co., a publicly traded food manufacturer of which a Mr. James is a director and 60% shareholder.[76] Following a proposal by Mr. James, Buyer Co. agrees to purchase an unused fleet of trucks from Seller

---

70 *Id.*, 1128.

71 DLLS, *Law and Economics*, *supra* note 35, at 455.

72 On the data, see Andrei Shleifer's webpage: http://scholar.harvard.edu/shleifer/publications/law-and-economics-self-dealing Revised Antidir tab (last visited Dec. 17, 2014) (nine countries were awarded a score of "5") [hereinafter Shleifer, *Data*].

73 DLLS, *Law and Economics*, *supra* note 35, at 455.

74 *Id*. at 455, Table 9.

75 *Id.* at 432

76 *Id*. at 433.

Electronic copy available at: https://ssrn.com/abstract=2595693

Co., a privately held retailer of which Mr. James is a 90% shareholder. Though all required approvals were obtained and all required disclosures were made, Buyer Co. shareholders sue on Buyer Co.'s behalf the interested parties and the body that approved the transaction.[77]

To measure the law governing their hypothetical self-dealing transaction, DLLS compiled two anti-self-dealing indices, one measuring public enforcement (fines and other criminal sanctions) and the other private enforcement (civil remedies). They evaluated public enforcement by assessing whether Mr. James and the approving parties could be fined and/or imprisoned as a result of what had occurred.[78] Though we have investigated how scoring under the public enforcement index developed over time we do not report the results here.[79] This is because this index has attracted considerably less interest than the private enforcement index, largely due to the fact that DLLS found that only the latter correlated in a meaningful way with measures of stock market development.[80]

The ASDI private enforcement index is made up of two sub-indices, one addressing *ex ante* private control of self-dealing and the other *ex post*.[81] The *ex ante* index, which focuses on regulation of the process by which the sale of the trucks could be validated, deals with requirements for advance disclosure of the proposed transaction by Mr. James and Buyer Co. and for an independent review of the transaction by a financial expert or an auditor. The *ex post* index, which measures the ease with which minority shareholders of Buyer Co. could establish potential wrongdoing in the courts after the transaction had been

---

77 *Id.*

78 *Id.* at 435.

79 For discussion of trends with the public enforcement index, see Cheffins, Bank, and Wells, *Law by Numbers*, *supra* note 26, at 1754.

80 DLLS, *Law and Economics*, *supra* note 35, at 451.

81 *Id.* at 434-35.

Electronic copy available at: https://ssrn.com/abstract=2595693

entered into, deals with requirements Buyer Co. would face to disclose the transaction, standing to sue, burden of proof and access to evidence.[82]

As with the ADRI variables, the variables in the ASDI private enforcement index are scored between "0" and "1." In some instances, such as with a requirement for an independent review, "0" and "1" were the only possible scores. More often allowance was made for the possibility of intermediate scores, with the range usually being "0", "0.5" and "1."[83] For instance, with disclosures Mr. James had to make in advance for validation of the hypothetical transaction to be possible, a country would score "0" if no disclosure was required, "0.5" if only the conflict of interest had to be disclosed and "1" if all material facts had to be divulged.

3. CBR SPI

Our last index is the CBR SPI, a 10 variable index initially constructed by Siems/CBR to score corporate law in 20 countries from 1995 to 2005[84] and subsequently deployed to score corporate law in 30 countries from 1990 to 2013.[85] The index addresses five basic categories, each associated with two of the ten variables:[86]

Table 3: CBR SPI Elements

CBR SPI Category	**Variables**
Shareholder power at shareholder meetings	Rights of shareholders to vote collectively on sale of the company's assets

82 *Id.* at 435.

83 With the *ex post* private index, the range for the "access to evidence" variable was 0, ¼, ½, ¾ and 1.

84 Siems, *Shareholder Protection II*, *supra* note 28, at 116; Armour *et al.*, *Shareholder, supra* note 47, 353.

85 Dionysia Katelouzou and Mathias Siems, *Disappearing Paradigms in Shareholder Protection: Leximetric Evidence for 30 Countries, 1990-2013*, J. CORP. L. STUD. (forthcoming), working paper version available at http://ssrn.com/abstract=2579832, 2; Mathias M. Siems, *The Leximetric Research on Shareholder Protection*, in RESEARCH HANDBOOK ON SHAREHOLDER POWER (Jennifer Hill and Randall Thomas, eds.) (forthcoming), working paper version available at http://ssrn.com/abstract=2578508, 7.

86 Siems, *Shareholder Protection II*, *supra* note 28, at 116. The ten variables are specified *id.* at 116-19.

Electronic copy available at: https://ssrn.com/abstract=2595693

	Rights of minority shareholders to require that that an item be put on a shareholder meeting agenda
Shareholder voting	Fostering effective voting by shareholders by making it possible for proxies to be sent by mail and by requiring the use of "two way" proxies that give the shareholder the possibility of voting "yes" or "no" Regulation of shares with multiple voting rights
Encouraging directors to take shareholder interests into account.	Regulation of board composition in the form of independent director requirements Rules dictating the feasibility of shareholder dismissal of directors before expiration of their term
Legal actions minority shareholders can file	Scope for minority shareholders to enforce breaches of duty by way of derivative suits Ability of shareholder to challenge shareholder resolutions
Change of corporate control protection	Imposing on a shareholder who acquires a large stake in a corporation an obligation to offer to buy the remaining shares Disclosure requirements for acquirers of large share ownership stakes

Consistent with the other indices, each CBR SPI variable is scored on a range between "0" and "1." Like the revised ADRI and the ASDI, the CBR SPI forsakes strict binary "0" and "1" coding. The CBR SPI indeed goes further to accommodate intermediate scoring so as to provide an accurate picture of the law.[87] Although the revised ADRI and the ASDI permitted non-binary options only when explicitly identified (such as "0", "0.5" and "1"), those coding the CBR SPI were prepared to give a wide range of intermediate scores for every variable.[88] For instance, while the description of the CBR SPI variable dealing with independent directors indicated that the scoring options were "1" if at least half of the board had to be independent directors, "0.5" if 25% of the board had to be independent and "0" otherwise,[89] Siems/CBR awarded China 0.4 for 2002 and 0.6 for 2003 to 2005.[90]

E. Which Types of Rules Qualify?

87 *Id.*, 120.

88 Mathias Siems et al., *CBR Extended Shareholder Protection Index*, (2009), 4, available at http://www.cbr.cam.ac.uk/fileadmin/user_upload/centre-for-business-research/downloads/research-projects-output/Shareholder%20protection%20index%20references%2025%20countries.pdf (accessed April 9, 2015) [hereinafter Siems et al., *CBR Extended* (2009)].

89 Siems, *Shareholder Protection II*, *supra* note 28, at 117.

90 Siems et al., *CBR Extended* (2009), *supra* note 90, at 34.

Electronic copy available at: https://ssrn.com/abstract=2595693

When deciding how to score legal rules going back through time, we had to take into account the form those rules took. Corporate law rules fall into three basic categories: mandatory, default/presumptive (applicable unless there has been a waiver or other form of "opting out"), and enabling/permissive (inapplicable unless there has been "opting in" by specific election).[91] When LLSV coded the original ADRI they failed to distinguish explicitly between these.[92] In contrast, when DLLS recoded the ADRI in 2008 they ignored enabling rules,[93] meaning a country would only be awarded a "1" when its corporate law had a default or mandatory rule providing the relevant protection to shareholders. The creators of the CBR SPI similarly awarded points only for mandatory and default rules.[94] DLLS did not indicate specifically which rules they focused on with the ASDI, but because they were seeking to measure "hurdles" that had to be jumped,[95] enabling rules, due to their permissive nature, should not have been taken into account.

Changing the types of rules that count can significantly alter scores awarded. LLSV, in their 1998 article, gave the United States "5" overall for the ADRI, with the only "0" occurring because shareholders lack pre-emptive rights under Delaware law, which LLSV again focused on to code the U.S.[96] In Delaware, a corporation is authorized to "opt in" to give shareholders cumulative voting rights and the right to call an extraordinary meeting.[97]

---

91 BRIAN R. CHEFFINS, COMPANY LAW: THEORY, STRUCTURE AND OPERATION 217-20 (1997).

92 DLLS, *Law and Economics*, *supra* note 35, at 454.

93 *Id.*

94 Siems et al., *CBR Extended* (2009), *supra* note 90, at 3-4 (indicating as well that only mandatory laws were counted with respect to rules precluding shares with multiple voting rights and requiring a shareholder to make a takeover bid for all shares upon acquiring a specified percentage of shares). Katelouzou and Siems, working with CBR SPI data, subsequently categorized legal rules that were elements of the CBR SPI as "enabling" and "paternalistic". In so doing, they were not attempting to revamp the basic typology of corporate law rules set out here, but rather were distinguishing between those CBR SPI rules that automatically imposed the rights in question on shareholders ("paternalistic") and those where shareholders had to be proactive to exercise the rights they had been given ("enabling"). See Katelouzou and Siems, *supra* note 85, 5.

95 DLLS, *Law and Economics*, *supra* note 35, at 432.

96 *Supra* note 67 and related discussion.

97 Cheffins, Bank and Wells, *Law by Numbers*, *supra* note 26, at 1746-47.

Electronic copy available at: https://ssrn.com/abstract=2595693

LLSV gave the United States a "1" for both variables, but when DLLS recoded the ADRI in 2008, they coded both as "0" because the rules governing these areas of the law were enabling rather than presumptive or mandatory.[98] This meant the aggregate score for the United States dropped from a "5" for LLSV to a "3 for DLLS.[99] Since DLLS themselves treated the revised ADRI as superior to the original, we decided to adopt the same approach to enabling rules as they did and excluded laws of this type from consideration when coding the ADRI going back through time.

Given how DLLS scored the ADRI for the United States, it might seem that "3" would be the obvious present-day baseline for historical research on Delaware. Holger Spamann's recoding of the ADRI, however, provides an additional wrinkle. Like DLLS, he discounted enabling rules and so awarded the United States "0"s for cumulative voting and for the calling of shareholder meetings. Spamann, however, awarded the United States a "2" rather than a "3" overall because he adopted a tougher standard than DLLS for awarding a "1" for proxy voting, a standard that Delaware failed to meet.[100] Spamann's coding of Delaware law provides as credible a departure point for our analysis as does DLLS's so we correspondingly decided to rely on both.

F. Who Made the Rules?

As part of our exercise of determining present-day coding before working backwards, we needed to determine not only the form of the relevant rules but also their source. The ADRI was scored purely by reference to company and bankruptcy/organization law and

98 Cheffins, Bank and Wells, *Questioning*, *supra* note 32, at 606.

99 *Id.*

100 On the differing approaches to proxy voting, see *infra* notes 143-44 and related discussion. Spamann, *Antidirector*, *supra* note 39, does not provide for the United States or any other country an element-by-element breakdown of ADRI scores. For this data, see http://rfs.oxfordjournals.org/content/23/2/467/suppl/DC1 [hereinafter Spamann, *Data*], (last visited April 10, 2015), link to Supplementary Data #2.

Electronic copy available at: https://ssrn.com/abstract=2595693

excluded securities law and stock exchange listing rules.[101] LLSV were prepared, however, to factor in judicial rulings when scoring jurisdictions.[102] For instance, they explicitly drew attention to the American derivative suit as an example of a legal mechanism that afforded shareholders protection against perceived oppression and its contours are defined primarily by case law.[103]

At first glance, it would seem that there is no need to go any further than LLSV did in identifying the laws that offer shareholder protection in the United States. Corporate law constitutes the most obvious source of shareholder rights and the relevant statutes are promulgated at state level.[104] While proposals to provide for federal incorporation pre-date adoption of the U.S. Constitution,[105] Congress has consistently resisted calls to provide for federal incorporation, leaving the matter instead to the states.[106] Each state has in turn promulgated a general corporate statute establishing the procedure for incorporating businesses and providing the ground rules governing the internal affairs of already incorporated companies.[107] When a corporation is incorporated under the laws of a particular state, that state's corporate law will be applicable notwithstanding where the principal place of business might be. The laws of the state of incorporation will be determinative due to a

---

101 LLSV, *supra* note 34, at 1120.

102 *Id*. at 1126.

103 Armour, Black and Cheffins, *supra* note 8, at 1349 (describing the prerequisites for bringing a derivative suit in Delaware as a "judicial construct").

104 Jill E. Fisch, *Leave it to Delaware: Why Congress Should Stay Out of Corporate Governance*, 37 DEL. J. CORP. L. 731, 732 (2013); Stephen M. Bainbridge, *The Creeping Federalization of Corporate Law*, 26 REGULATION 26, 26 (2003) ("For over 200 years, corporate governance has been a matter for state law.")

105 William W. Bratton and Joseph A. McCahery, *The Equilibrium Content of Federalism*, 41 WAKE FOREST L. REV. 619, 653 (2006) [hereinafter Bratton & McCahery, *Equilibrium*].

106 Robert B. Thompson, *Delaware, the Feds, and the Stock Exchange: Challenges to the First State as First in Corporate Law*, 29 DEL. J. CORP. L. 779, 784 (2004) [hereinafter Thompson, *Delaware*]; Robert B. Thompson, *Delaware's Disclosure: Moving the Line of Federal-State Corporate Regulation*, [2009] U. ILL. L. REV. 167, 177.

107 Wells, *Modernization*, *supra* note 65, at 573.

Electronic copy available at: https://ssrn.com/abstract=2595693

choice of law rule known as "the internal affairs doctrine" which does much to sustain Delaware's status as the leading supplier of corporate charters.[108]

The internal affairs doctrine, in addition to operating as a choice of law rule affecting states, has formed the basis of an understanding among federal and state lawmakers that has done much to shape U.S. corporate law. The key precept is that the internal affairs of corporations fall within the purview of state law and are not a proper subject for federal regulation.[109] Some judicial rulings imply that due to the nature of the federal system in the U.S. the internal affairs doctrine is constitutionally mandated.[110] This in fact is not the case. The better view is that federal corporate law-making authority is very broad, and that Congress could if it wished federalize corporate law largely without limit.[111]

Constitutional potentialities aside, over most of U.S. history Congress steered clear of enacting federal corporate law. There was no meaningful federal contribution on the corporate law front until the enactment of the Securities Act of 1933[112] and the Securities Exchange Act of 1934,[113] which established the federal Securities and Exchange Commission (SEC). Even these important pieces of legislation ultimately constituted only a tentative foray by Congress into the corporate law realm. The SEC would subsequently argue that key aspects of the 1934 Act authorized the SEC to create rules that directly affected the

---

108 Fredrick Tung, *Before Competition: Origins of the Internal Affairs Doctrine*, 32 J. CORP. L. 33, 39, 42-43 (2006).

109 Renee M. Jones, *Does Federalism Matter? Its Perplexing Role in the Corporate Governance Debate*, 41 WAKE FOREST L. REV. 879, 882 (2006).

110 COX & HAZEN, *supra* note 7, at 172; Greenwood, *supra* note 9, at 413; Roe, *Delaware's Competition*, *supra* note 17, 596.

111 Roe, *Delaware's Competition*, *supra* note 17, at 597; Kahan and Rock, *Symbiotic Federalism*, *supra* note 20, 1585-86; Fisch, *supra* note 104, at 737-38.

112 48 Stat. 74.

113 48 Stat. 881.

Electronic copy available at: https://ssrn.com/abstract=2595693

governance of corporations, such as regulation of shareholder voting conducted by proxy.[114] This, however, was not the consensus view at the time the federal securities law reform was undertaken. The post-1934 regulatory pattern was generally assumed to be one where federal law targeted trading markets by way of disclosure and anti-fraud rules ("securities law"), thereby leaving "corporate law" relating to the internal affairs of companies to the states.[115] The legislative history relating to the enactment of the 1933 and 1934 Acts indeed indicates that Congress did not intend to authorize federal securities regulators to interfere in the management of companies.[116]

This pattern began to change in the late twentieth century. Between the 1968 enactment of the Williams Act, which amended section 14 of the Securities and Exchange Act of 1934 to impose a range of obligations on parties making a tender offer to acquire shares,[117] and the close of the 20th century, there were various federal incursions in the corporate law realm. Laws and regulations were adopted fostering disclosure in relation to transactions pursuant to which publicly traded companies were taken private, discouraging the listing of dual-class shares, deregulating proxy requirements to facilitate institutional shareholder voice, and limiting the tax deductibility of executive compensation.[118] These incursions would soon be overshadowed, however, by the most ambitious federal corporate law-related initiative to date.

---

114 Arthur Fleisher, *'Federal Corporation Law': An Assessment*, 78 HARV. L. REV. 1146, 1151, 1158-59 (1965); Patrick Moyer, *The Regulation of Corporate Law by Securities Regulators: A Comparison of Ontario and the United States*, 55 U. TOR. FAC. L. 43, 49 (1997).

115 Bratton and McCahery, *Equilibrium*, *supra* note 105, at 624-25. A variety of tax provisions were enacted during this period that appeared to be motivated at least in part by the desire to affect corporate governance, but these were usually defended on tax policy grounds as well. *See* Steven A. Bank, *Tax, Corporate Governance, and Norms*, 61 WASH. & LEE L. REV. 1159, 1163-64 (2004).

116 Moyer, *supra* note 114, at 49-50.

117 Pub. L. No. 90-439, 82 Stat. 454.

118 Roe, *Delaware's Competition*, *supra* note 17, at 616-22; Bank, *supra* note 115, at 1161.

Electronic copy available at: https://ssrn.com/abstract=2595693

The game-changer was the Sarbanes-Oxley Act of 2002 (SOX),[119] which Congress enacted in response to high-profile corporate scandals involving companies such as WorldCom and Enron. As Mark Roe observed in a 2003 article where he emphasized the federal government's impact on competitive federalism,

> "With Sarbanes-Oxley in 2002, Congress did not even pretend to stay on the disclosure-and-trading side of the rhetorically traditional federal-state division of power, not even offering perfunctory respect for state rules governing the corporation's internal affairs."[120]

The nature and depth of SOX's corporate law content was something of a shock to those who had assumed that the states were pre-eminent.[121] Key changes SOX made included creating the possibility of executive pay "clawbacks" where there had been problematic restatements of earnings, prohibiting corporate loans to senior executives, requiring CEO certification of financial reports filed with the SEC, granting the SEC formal authority to regulate the structure and duties of board committees dealing with the audit function and giving the SEC explicit powers to formulate accounting standards.[122]

The Dodd-Frank Act of 2010 constituted another substantial federal incursion into the corporate law realm.[123] While this post-financial crisis legislation focused primarily on the regulation of banks, it contained a sub-title entitled "Strengthening Corporate Governance"

---

119 Pub.L. 107-204, 116 Stat. 745.

120 Roe, *Delaware's Competition*, *supra* note 17, at 633.

121 Bratton and McCahery, *Equilibrium*, *supra* note 105, at 668 (the "off-handed but emphatic revision of the internal affairs line drawn after 1934…upset settled expectations").

122 Brown, *supra* note 11, at 358-71; Robert B. Ahdieh, *From "Federalization" to "Mixed Governance" in Corporate Law: A Defense of Sarbanes Oxley*, 53 BUFFALO L. REV. 721, 724-25 (2005); Brian R. Cheffins, *Introduction*, THE HISTORY OF MODERN U.S. CORPORATE GOVERNANCE, vol. I, ix, xxvi (Brian R. Cheffins, ed., 2011).

123 Dodd–Frank Wall Street Reform and Consumer Protection Act of 2010 (hereinafter Dodd-Frank Act), Pub. L. 111-203.

Electronic copy available at: https://ssrn.com/abstract=2595693

applicable to all issuers falling under the SEC's jurisdiction, not just financial companies.[124] This sub-title amended federal securities law to instruct the SEC to introduce rules requiring companies that had failed to split the chief executive officer and chairman of the board roles to explain why and to authorize the SEC to develop a "proxy access" rule permitting shareholders with significant stakes to nominate under prescribed circumstances directors on a company's own proxy card. Another sub-title of the Act, dealing with executive compensation,[125] amended federal securities laws to mandate an advisory "say on pay" shareholder vote and additional compensation disclosures for all publicly traded companies subject to SEC jurisdiction.[126]

The ADRI, due to its exclusive focus on state corporate law,[127] does not take account of securities law-based federal initiatives that might bolster shareholder protection. The situation is different with the ASDI and the CBR SPI, which factor in a wider range of laws and correspondingly can reflect rules promulgated outside the state context. With the ADSI, DLLS coded by reference to "stock market act(s) and regulations" (i.e. securities law) and stock exchange listing rules as well as corporate legislation and judicial precedent.[128] With the CBR SPI, Siems and his colleagues similarly took into account securities law and stock exchange listing rules in addition to corporate law statutes and case law.[129]

To simplify rule categorization, we treat all laws not promulgated at state level as "federal," in the sense that they apply nationwide. Who are the relevant federal rule-makers?

---

124 Title IX, Sub-title G., encompassing §§ 971-72.

125 Title IX, Sub-title E., encompassing §§ 951-57.

126 Dodd-Frank Act, § 951 (shareholder voting on executive compensation); § 953 (disclosure). Of the provisions in Title IX, Sub-title E all govern all publicly traded companies subject to SEC jurisdiction save for § 956. This provision, which requires disclosure of executive pay arrangements to regulators, only applies to "covered financial institutions."

127 *Supra* note 101 and accompanying text.

128 DLLS, *Law and Economics*, *supra* note 35, at 433.

129 Siems, *Shareholder Protection II*, *supra* note 28, at 120.

Electronic copy available at: https://ssrn.com/abstract=2595693

Congress obviously is one. Though there is no federal incorporation legislation, Congress has periodically since the early 1930s enacted statutory measures as part of federal securities law that operate as *de facto* corporate law.[130] The SEC is another. As the administrative agency charged with administering federal securities law, it promulgates regulations and issues rulings pursuant to the statutory mandate under which it operates. Federal courts are a third, as they interpret federal securities law and SEC regulations and rulings.[131]

Beyond the official governmental realm, there are private actors – leading national stock exchanges – whose rules are taken into account with ADRI and CBR/SPI coding and which we treat as generating "federal" rules. The New York Stock Exchange (NYSE), for instance, is a private body, not an agency of the federal government. Nevertheless, the Securities Exchange Act of 1934 requires the NYSE, operating as a national securities exchange and self-regulatory organization under the Act, to submit listing rules governing companies traded on the Exchange to the SEC for approval.[132] Also, the SEC can amend the NYSE's listing rules to further the purposes of the 1934 Act.[133] The SEC correspondingly has substantial power to ask – even direct – the NYSE to make rules that affect shareholder protections.[134] Indeed, Robert Thompson has said of NYSE listing rule amendments promulgated from the late 1970s onwards dealing with governance-related topics such as shareholder voting rights, board composition and shareholder approval of executive pay, "Without the SEC's leadership, the exchanges would not likely have entered into the arena of corporate governance."[135]

---

130 *Supra* notes 112-26 and related discussion.

131 Roe, *Delaware and Washington*, *supra* note 18, at 11.

132 Securities and Exchange Act of 1934, § 19(b); 15 U.S.C. § 78(b).

133 Securities and Exchange Act of 1934, § 19(c); 15 U.S.C. § 78(c).

134 Roe, *Delaware and Washington*, *supra* note 18, at 11.

135 Thompson, *Delaware*, *supra* note 106, at 797.

Electronic copy available at: https://ssrn.com/abstract=2595693

III. HYPOTHESES AND FINDINGS

Our historically-oriented leximetric investigation of U.S. corporate law allows us to analyze numerous aspects of shareholder protection under corporate and securities law. To ensure our empirical research directly addresses the key issues, we have generated a series of specific, testable hypotheses. We identify these here before turning to our findings.

A. Hypotheses

Among the hypotheses that can be tested by using the ADRI, ASDI and CBR SPI to measure historically shareholder protection, perhaps the most obvious is that scores should decline over time, at least when measuring state corporate law. The corporate law "race" rhetoric used to characterize the evolution of the law, whether to the top or bottom, connotes movement.[136] Moreover, given the general consensus that the competition among states for incorporation business occurring in the 20th century served to erode shareholder rights while enhancing managerial flexibility,[137] shareholder protection scores should have fallen.

Hypothesis 1: Shareholder protection index scores, to the extent they reflect state law, should decline over time.

While the standard narrative has been that shareholder rights have been eroded over time, various observers have cited reform at the federal level to argue that shareholder protection in fact was bolstered from the 1930s onwards.[138] Assuming these observers are correct, one would expect that:

Hypothesis 2: Shareholder protection index scores, to the extent they reflect federal law, should increase over time.

---

136 Roe, *Delaware's Competition, supra* note 17, at 606.

137 *Supra* notes 4-6, *infra* notes 264 to 268 and related discussion.

138 *Supra* notes 14-16 and accompanying text.

Electronic copy available at: https://ssrn.com/abstract=2595693

Due to growing recognition of the role the federal government has played going back through time the conventional wisdom concerning state dominance of the United States' system of corporate law federalism has been shifting over the past decade.[139] The extent of federal influence is, however, open to debate.[140] If this influence was substantial then federal intervention fortifying the rights of shareholders may have been enough to more than offset any erosion of shareholder rights at the state level, meaning the overall level of shareholder protection would have increased. It follows that:

> *Hypothesis 3: If changes to federal law heavily influenced the scoring of individual components of shareholder protection indices, these indices' aggregate scores should have increased over time.*

All three of these hypotheses can be tested by way of the ASDI and the CBR SPI. This is because, as Part II.F described, these indices are scored not only by reference by state corporate law but also take into account securities law and rules developed by key players at the federal level, namely the SEC and national stock exchanges. With the ADRI, the fact that coding occurs purely by reference to state corporate law means that scoring over time can only be used to test hypothesis 1.

B. Present-Day Scores

Given our methodology, which involves determining present-day coding before working backwards,[141] with each of the three indices we begin by considering the current scoring for each of our three jurisdictions. This not only constitutes the foundation for our historical analysis but also provides insights concerning the level of shareholder protection the U.S. currently offers as compared to other countries. With the ADRI, which is governed

---

139 *Supra* notes 17-18 and accompanying text.

140 *Supra* note 19 and related discussion.

141 See text following note 65.

Electronic copy available at: https://ssrn.com/abstract=2595693

solely by state corporate law, the U.S. scores poorly by global standards. In contrast, with the ASDI and the CBR SPI, both of which factor in federally oriented securities regulation and stock market listing rules, the level of shareholder protection is high in global terms.

1. ADRI

With the ADRI, as mentioned, we score it using approaches developed by both DLLS and by Spamann.[142] DLLS gave the United States (i.e. Delaware) a "3" out of 6 overall while Spamann gave Delaware an aggregate score of "2" (Tbl. 4). The discrepancy arises from the proxy voting element of the ADRI. DLLS gave Delaware a "1" for proxy voting because the Delaware General Corporation Law ("DGCL") explicitly authorizes voting by proxy.[143] Spamann only gave countries a "1" with this variable if the law required that proxies provide for "yes or no" "two way" voting.[144] Delaware corporate law does not do this, so he scored this element "0."

Table 4: Delaware's Present-Day ADRI Scores

ADRI element	DLLS	Spamann	Justification for present day score
Vote by Proxy Allowed	1	0	DGCL § 212(b) (gives shareholders the right to vote by proxy but does not provide for, as Spamann requires, two way voting).
No Block	1	1	Spamann (2008) (at 183): "Under the default regime, firms cannot require deposit of shares…"
Cumulative Voting	0	0	DGCL § 214 (providing for an enabling rule, not a default rule)
Oppressed Minority	1	1	Spamann (2008, p. 184): Minority shareholders can enforce breaches of duty by directors by way of a derivative suit and can challenge

142 *Supra* notes 66, 100 and related discussion.

143 DLLS, *Law and Economics*, *supra* note 35, at 454 (indicating it would suffice if "shareholders can vote by mail on each of the items on the agenda through a ballot or proxy form"), 455 (Table 9, describing elements in their revised ADRI).

144 Holger Spamann, *On the Insignificance and/or Endogeneity of La Porta et al.'s "Anti-Director Rights Index" Under Consistent Coding*, HARVARD OLIN CENTER FOR LAW, ECONOMICS AND BUSINESS FELLOWS' DISCUSSION PAPER NO. 7, 27 (2006). "Yes or no" or "two way" voting refers to a proxy form that explicitly gives shareholders the ability to instruct the proxy to vote for or against a resolution.

Electronic copy available at: https://ssrn.com/abstract=2595693

			shareholder amendments to the corporate charter on grounds of "unfairness."
Pre-emptive Rights	0	0	Spamann (2008, p. 184): "Preemptive rights exist only to the extent expressly granted in the (certificate of incorporation) (DGCL §102(3))."
Ability to Call General Meeting	0	0	Spamann (2008, p. 184): "shareholders can call a special meeting only if allowed by, and under the conditions specified in, the (certificate of incorporation), (DGCL §211(d)....)."
Total	**3**	**2**	

Source: Spamann (2008)[145]

Given that in recent years Delaware law has not been amended in a way that would affect the scoring of any ADRI variables, DLLS's and Spamann's codings for U.S. corporate law should determine Delaware's present-day score for our purposes. These imply that Delaware corporate law is not "shareholder friendly," at least in comparison with other countries scored using the ADRI. DLLS's U.S. score of "3" was substantially below the average score of 4.29 DLLS awarded to common law countries and was similar to the average for civil law countries (2.88).[146] According to Spamann's coding, Delaware's aggregate ADRI score of "2" trailed well behind the overall average for common law countries (4.06) and civil law countries (3.93).[147] Indeed, no country had a lower overall score.[148]

For both Illinois and the Model Act, using DLLS's approach to the ADRI, "4" appears to be the appropriate present-day aggregate score (Tbl. 5, Tbl. 6). This aligns these

---

145 Spamann, *Data*, *supra* note 100.

146 On the common law average, see DLLS, *Law and Economics*, *supra* note 35, at 456. The civil law average is not discussed in this article but was set out in Table XII of a working paper version cited *supra* note 35. Spamann, in his 2010 article, provides different averages for the DLLS ADRI, namely 4.22 for common law countries and 3.11 for civil law countries: Spamann, *Antidirector*, *supra* note 39, at 475. DLLS and Spaman provided aggregate data for civil law and common law countries because an important feature of the "law and finance" literature has been determining whether legal protection relevant to investors differs among different legal families, such as civil or common law.

147 Cheffins, Bank and Wells, *Questioning*, *supra* note 32, at 608.

148 Spamann, *Antidirector*, *supra* note 39, at 475.

Electronic copy available at: https://ssrn.com/abstract=2595693

jurisdictions more closely with the DLLS average for common law countries and means they have significantly higher aggregate scores than the typical civil law country. The situation is somewhat different if Spamann's methodology is used. Given that neither the Model Act nor Illinois mandate the use of two way proxies, under Spamann's methodology their aggregate present-day scores become "3" rather than "4" respectively. This is below the overall average for common law countries and civil law countries but the discrepancy is not as dramatic as is the case with Delaware.

Table 5: Illinois Present-Day ADRI Scores

ADRI element	DLLS	Spamann	Justification for present day score
Vote by Proxy Allowed	1	0	Illinois Business Corporation Act (IBCA) § 7.50; reasoning for scoring is the same as Delaware.
No Block	1	1	IBCA §7.25 (provides for the concept of record ownership of shares, which means companies can identify who is entitled to vote without blocking share transfers prior to shareholder meetings).
Cumulative Voting	1	1	IBCA §7.40 (requires cumulative voting unless the articles of incorporation say otherwise).
Oppressed Minority	1	1	Brown v. Tenney, 532 N.E.2d 230, 232-33 (Ill. 1988); Kalabogias v. Georgou, 254 Ill. App. 3d 740, 747 (1993); IBCA §7.80 (governing the procedure for derivative litigation).
Pre-emptive Rights	0	0	IBCA §6.50; which merely permits pre-emptive rights to be created in the certificate of incorporation.
Ability to Call General Meeting	0	0	IBCA §7.05 (shareholders owning 20% of the shares can call a meeting, which exceeds 10% maximum required for a "1").
Total	**4**	**3**	

Table 6: Model Act Present-Day ADRI Scores

ADRI element	DLLS	Spamann	Justification for present day score
Vote by Proxy Allowed	1	0	Model Act § 7.22; reasoning for scoring is the same as Delaware.
No Block	1	1	Spamann (2008) (p. 184), citing

Electronic copy available at: https://ssrn.com/abstract=2595693

			Model Act §7.07.
Cumulative Voting	0	0	Model Act §7.28(b) (providing for an enabling rule, not a default rule)
Oppressed Minority	1	1	Spamann (2008, p. 184), citing Model Act §§8.31, 8.61, 13.02, and Chapter 7 Subchapter D.
Pre-emptive Rights	0	0	Model Act §6.30; reasoning similar to that for Illinois; see also Spamann (2008, p. 184).
Ability to Call General Meeting	1	1	Model Act §7.02(a) (10% threshold).
Total	**4**	**3**	

2. ASDI

Recall that our second index, the ASDI, measures the law applicable to a hypothetical self-dealing transaction by way of a public and private enforcement index.[149] The ASDI private enforcement index is comprised of two sub-indices relating respectively to ex-ante and ex-post control.[150] For the most part, for each of these sub-indices the present-day scores for Delaware, Illinois and the Model Act are identical. With the Model Act, this is partly due to us drawing upon Delaware and Illinois scoring with one ASDI element where coding was problematic because the Model Act is a model statute not anchored to the law of a particular state.

The ASDI element where we drew on Delaware and Illinois law to code the ASDI for the Model Act involved a component of the ex-post control of self-dealing index dealing with "access to evidence." With "access to evidence," the possible overall score ranges from "0" to "1." A jurisdiction is awarded one-quarter point each when a plaintiff shareholder challenging the hypothetical transaction who owns 10% or more of the shares (i) can request the court to investigate the self-dealing transaction; (ii) can request documents relevant to the case from the defendant; (iii) can ask the defendant questions prior to trial without prior

149 *Supra* note 78 and related discussion.

150 *Supra* note 81 and accompanying text.

Electronic copy available at: https://ssrn.com/abstract=2595693

judicial approval of the questions and (iv) can do the same with non-parties.[151] For U.S. companies these are issues that are governed by civil procedure rules of the state in which the litigation would occur, rather than by corporation law itself. Given that Djankov *et al.* awarded the United States (i.e. Delaware) 0.75 for access to evidence and given that this in all likelihood is the appropriate score for Illinois[152] we have given the same score to the Model Act.

Although ASDI scores are much the same for Delaware, the Model Act and Illinois, the situation is different with disclosure requirements in the ex-ante private control of self-dealing index applicable to Buyer Co. and Mr. James. DLLS awarded the U.S. (i.e. Delaware) "1" for these variables.[153] They did not do so because an explicit statutory duty is imposed; there are no provisions mandating such disclosure in the Delaware General Corporation Law.[154] Instead, it appears that Delaware was awarded "1"s for disclosure by Buyer Co. and by Mr. James because the relevant disclosures would have to occur in order for the parties to the hypothetical transaction to be able to rely on a statutory "safe harbor" provision in Delaware's corporate statute designed to help shield a related party transaction from challenge and protect the directors involved from liability.[155]

The Model Act's related party transaction "safe harbor" provision is worded similarly to Delaware's,[156] meaning the Model Act similarly should be given "1"s for the rules

---

151 DLLS, *Law and Economics*, *supra* note 35, at 432 (Tbl. 1).

152 On Delaware, see Shleifer, *Data*, *supra* note 72, Ex-Ante Control tab, columns D and E. Illinois should be given one-quarter point each because under the hypothetical the plaintiff shareholder could request documents, could ask the defendant questions prior to trial and could do the same with non-parties. See ILCS Supreme Court Rules, R. 206 (right to conduct oral depositions of parties and non-parties), R. 210 (right to conduct written depositions of parties and non-parties), R. 213 (right to conduct interrogatories), R. 214 (right to demand document production). The overall score should not be 1.00 because Illinois, like Delaware, lacks procedural or corporate law rules permitting a shareholder to request a court investigation.

153 Shleifer, *Data*, *supra* note 72, Ex-Post Control tab, column H.

154 Cheffins, Bank, and Wells, *Law by Numbers*, *supra* note 26, at 1758.

155 *Id.* at 1758-59.

156 Model Business Corporations Act, §8.61.

Electronic copy available at: https://ssrn.com/abstract=2595693

governing disclosure by the Buyer Co. and Mr. James (Tbl. 7). In contrast, Illinois's "safe harbor" provision is drafted explicitly to ensure that a transaction can be insulated from challenge if it was "fair" regardless of whether ex ante disclosure occurred or not. The relevant measure provides that the absence of full disclosure merely shifts the burden of proof on to those asserting the related party transaction should be treated as valid on the grounds of its fairness.[157] Correspondingly, Illinois should be given a "0" both for rules governing disclosure by the Buyer Co. and by Mr. James. With Illinois scoring "0s" for other elements of the ASDI's ex-ante private control of self-dealing sub-index, Delaware and the Model Act necessarily have higher overall scores (Tbl. 7).

Table 7: Present-Day ASDI Ex-ante Private Control of Self-Dealing Sub-Index -- Delaware, Illinois and the Model Act

ASDI Element	Delaware	Illinois	Model Act	Justification for present day score
Approval by disinterested shareholders	0	0	0	None of the jurisdictions have rules in place requiring that related party transactions be voted on by shareholders. The UK is an example of a jurisdiction where such approval is required (Companies Act 2006, c. 46, §§ 190-96).
Disclosure by Buyer Co.	1	0	1	See *supra* notes 153-57 and related text.
Disclosure by Mr. James	1	0	1	*Id.*
Independent Review	0	0	0	None of the jurisdictions require that a related party transaction be scrutinized by an independent auditor or financial expert.
Ex ante disclosure	0.67	0	0.67	Average of previous three variables.
Ex-ante Private Control of Self-Dealing	**0.33**	**0**	**0.33**	Average of approval by disinterested shareholders and ex ante disclosure.

[157] 805 ILCS 5/8.60; *see* Janice M. Church, Note, *Director Conflict of Interest Under the 1983 B.C.A.; A Standard of Fairness*, [1985] U. ILL. L. REV. 741 [hereinafter Church, *Director Conflict of Interest*] ("Section 8.60 supports such an approach because it relegates factors relevant to procedural fairness --disclosure and approval -- to the issue of shifting the burden of proof.").

Electronic copy available at: https://ssrn.com/abstract=2595693

As compared with countries elsewhere the ex ante private control of self-dealing scores for the jurisdictions we focus on are mediocre at best. The Delaware and Model Act scores of 0.33 were below the average of 0.36 for the 72 countries DLLS focused on.[158] Only three of the countries – Austria, Hungary and Tunisia – scored as poorly as Illinois with its 0.00.[159]

With ex post private control of self-dealing the story is much different. The overall Delaware, Illinois and Model Act scores of 0.98 (Tbl. 8) are inferior to only one jurisdiction, this being Singapore with 1.00.[160] Unlike with ex ante private control of self-dealing, with the ex post index there was no variation with any of the elements between Delaware, Illinois and the Model Act.

Table 8: Present-Day ASDI Ex-post Private Control of Self-Dealing Sub-Index/Overall ASDI Scores -- Delaware, Illinois and the Model Act

ASDI Element	Delaware	Illinois	Model Act	Justification for present day score
Disclosure in periodic filings	1	1	1	Federal regulation: 17 CFR §229.404, Form 10-K, 17 CFR §240.15D-1, 17 CFR §240.14A
Standing to sue (equals 1 if a derivative suit can be brought against Mr. James and bodies approving the transaction)	1	1	1	See discussion of derivative action in relation to the oppressed minority variable in Tables 4-6.
Rescission (equals 1 if rescission is available if the transaction is unfair or involves a	1	1	1	At common law, a related party transaction was void or at least voidable.[161] Delaware, Illinois and the Model Act each have statutory safe harbor provisions that can shelter transactions from challenge[162] but they

158 Cheffins, Bank, and Wells, *Law by Numbers*, *supra* note 26, at 1756.

159 Shleifer, *Data*, *supra* note 72, Ex-Ante Control tab, column H.

160 Cheffins, Bank, and Wells, *Law by Numbers*, *supra* note 26, at 1756.

161 Model Business Corporations Act, Subchapter F. Directors' Conflicting Interest Transactions, Introductory Comment, Part 1.

162 *Supra* notes 155-57 and accompanying text.

Electronic copy available at: https://ssrn.com/abstract=2595693

conflict of interest)				would not operate if a transaction was unfair or had not been approved by the board or the shareholders.
Ease of holding Mr. James liable (equals 1 if the interested director is liable if the transaction is unfair, oppressive, or prejudicial).	1	1	1	The Model Act specifically recognizes that damages will be recoverable when a related party transaction cannot be saved under a statutory safe harbor.[163] The remedy should also be available at common law.[164]
Ease of holding approving body liable (equals 1 if the members of the approving body are liable if the transaction is unfair, oppressive, or prejudicial).	1	1	1	Unclear. Relevant Delaware case law[165] indicates that, in a related party transaction context, directors who approve a one-sided transactions will be held liable only if they have breached duties of loyalty and care (i.e. gross negligence). Under DLLS' coding scheme, this means the United States should have been given "0". Consistent, however, with our policy of deferring to original coding,[166] we will assume that all three jurisdictions should be scored "1".
Access to evidence	0.75	0.75	0.75	*Supra* notes 151-52 and related discussion.
Ease of proving wrongdoing	0.95	0.95	0.95	Average of previous five variables
Ex-post Private Control of Self-dealing	**0.98**	**0.98**	**0.98**	Average of disclosure and ease of private wrongdoing
Anti-self-dealing index (private enforcement)	**0.65**	**0.49**	**0.65**	Average of Ex-ante Private Control of Self-Dealing and Ex-post Private Control of Self-dealing

As Table 8 indicates, with the ASDI the ex ante and ex post sub-indices are averaged to produce an overall ASDI private enforcement score. For Delaware and the Model Act, the combination of the very high ex post private control of self-dealing score with the mediocre

163 Model Business Corporations Act, §8.61(a).

164 *Id*., §8.61, Selected Cases, 2.G Conflicts of Interest/Damages.

165 See, e.g., *In re Loral Space and Communications, Inc*., 2008 WL 4293781, *33 (Sept. 19, 2008) ("[B]eing a non-independent director who approved a conflict transaction found unfair does not make one, without more, personally liable for harm caused. Rather, the court must examine that director's behavior in order to assess whether the director breached her fiduciary duties…"); *ATR-Kim Eng Financial Corp. v. Araneta*, 2006 WL 3783520 (Del. Ch. 2006).

166 *Supra* note 68 and related discussion.

Electronic copy available at: https://ssrn.com/abstract=2595693

score of 0.33 for ex ante private control yields an overall present-day score of 0.65. This score of 0.65 placed Delaware (i.e. the United States) 10th highest among the 72 countries DLLS coded and well above the global average of 0.44.[167] Illinois' overall private control of self-dealing score of 0.49 – despite being driven downwards by the score of 0 with ex ante private control – would have still placed Illinois 24th out of the 72 countries.[168]

3. CBR SPI

With our final index, the CBR SPI, when Mathias Siems and his CBR co-authors scored the United States (again, meaning Delaware) for 2005 they gave the U.S. a score of 7.25 out of a possible score of 10.[169] When they brought the CBR SPI up-to-date as of 2013 the score for the U.S. became 7.5, with the increase occurring because the Dodd-Frank Act of 2010 introduced an advisory say-on-pay vote for executive pay.[170] There have been no relevant changes to the law in the years since. Given our methodological choice not to depart from scores generated by those initially constructing an index for our purposes Delaware's present day score correspondingly is 7.5 (Tbl. 9).

Table 9: Delaware Present-Day CBR SPI Scores

CBR SPI Element	**Delaware score (2013/present day)**	**Justification for present day score**[171]
Powers of the general meeting for de facto changes. (The score is governed by the level of shareholder approval required for a sale of the company's assets).	0.75	DGCL § 271 requires shareholder approval for "sale, lease, or exchange" of "substantially all" of the assets. The relevant case law indicates that 50% does not automatically constitute "substantially all," which was the threshold specified for awarding a "1".

167 Cheffins, Bank, and Wells, *Law by Numbers*, *supra* note 26, at 1757.

168 Derived from analysis of Shleifer, *Data*, *supra* note 72, Ex-Post Control tab, column K.

169 Armour *et al*., *Shareholder*, *supra* note 47, 357, Table 2.

170 Mathias Siems et al., *CBR Extended Shareholder Protection Index* (2nd ed., 2013), 106 (hereinafter Siems *et al*., *CBR Extended* (2013) (copy on file with the authors).

171 Siems et al., *CBR Extended* (2009), *supra* note 90, at 103-5; Siems et al., *CBR Extended* (2013), *supra* note 170, at 105-7.

Electronic copy available at: https://ssrn.com/abstract=2595693

Agenda setting power. (The score is based on the ability of shareholders owning specified percentages of shares to put a matter to a shareholder vote).	1	SEC Rule 14a-7 (requiring a public company to provide a shareholder list to shareholders who ask); SEC Rule 14a-8 (allows shareholders meeting modest share ownership requirements to circulate resolutions in proxy material their company circulates).
Anticipation of shareholder decision facilitated. (Score = 0.5 if postal voting possible and 1 if postal voting possible and companies soliciting proxies must use "two-way"-- "yes" and "no" -- proxy forms.)	1	NYSE Manual, § 402.04 (requiring listed companies to solicit proxies to facilitate shareholder voting); SEC Rule 14a-4(b)(1) (mandating use of two way proxies).
Prohibition of multiple voting rights.	0.5	NYSE Manual, §§ 313.00 (Voting rights cannot be disparately reduced or restricted but companies with non-voting shares are permitted to continue to list and issue such shares).
Independent board members. (Score = 1 if at least half of the board members must be independent; 0.5 if 25% of them must be independent.)	1	NYSE Manual, § 303A.01 (half of the board members must be independent).
Feasibility of director's dismissal. (Score = 0.75 if a dismissed director can only claim for contractual compensation if dismissed without good reason if compensation is specifically contractually agreed.)	0.75	There can be compensation agreements with dismissed directors (*cf.* DGCL § 141(k)) and shareholders have by virtue of the Dodd-Frank Act of 2010 (see *supra* note 126 and accompanying text) the right to an advisory "say on pay" vote. [172]
Private enforcement of director duties. (The score is based on the ease with which a minority shareholder can bring a derivative suit.)	0.75	Siems et al. acknowledged that derivative actions are feasible in the United States but did not award a "1" because various restrictions apply, such as a contemporaneous ownership requirement (the plaintiff must have owned shares at the time the alleged breach of duty occurred), a requirement that a plaintiff typically make "demand" (ask the board to sue) and judicial deference to screening by special litigation committees.
Shareholder action against resolutions of the general meeting. (Score = 1 if every	1	Siems et al relied upon Delaware case law to justify awarding "1". The cases cited

[172] Those constructing the CBR SPI apparently inaccurately conflated dismissal as a director with dismissal as an executive. The analysis of the 0.75 scoring for the United States cited MBCA §8.08(a), which specifically permits a corporation's shareholders to dismiss a director without cause, meaning the dismissed director will not be entitled to compensation, as well as the provision in the Dodd-Frank Act that provided for an advisory "say on pay" vote: Siems et al., *CBR Extended* (2013), *supra* note 170, 106. Despite §8.08(a), an individual who is an executive in addition to being a director who is fired as an executive without cause will be able to sue for damages for wrongful termination from the executive position. It seems the possibility of this occurring was sufficient for Siems and the CBR team to refrain from giving the U.S. (i.e. Delaware) a score of 1 even though this scenario has nothing directly to do with director dismissal. The citing of the "say on pay" rule introduced by Dodd-Frank is also confusing in that the ability of shareholders to vote on executive compensation policy on an advisory basis has no obvious connection with the feasibility of director dismissal.

Electronic copy available at: https://ssrn.com/abstract=2595693

shareholder is eligible to challenge a shareholder resolution.)		indicate the powers of the majority are "always subject to the historical processes of a court of equity to gauge whether there has been an oppressive exercise of the power granted."[173]
Mandatory bid. The score is determined by the presence of rules requiring a shareholder who buys a designated percentage of shares to make an offer to buy the shares of all remaining shareholders.	0	Neither Delaware nor federal law requires an investor who acquires a large stake in a company to make a bid for all of the shares of the company.
Disclosure of major shareholder ownership. (Score = 0.75 if shareholders who acquire at least 5% of a company's shares have to disclose their stake.)	0.75	Securities Exchange Act 1934, § 13(d) and Schedule 13D of the Act combine to require those acquiring a stake of 5% or more to disclose their interest.
Total	**7.5**	

Sources: Siems et al., (2009), *supra* note 90; Siems et al., (2013), *supra* note 170.

In comparative terms, shareholders in Delaware corporations are well-protected. Among the 20 countries in the Siems/CBR dataset for 2005, the United States, with its score of 7.25, tied for second best with France, trailing slightly behind the UK at 7.375 and substantially exceeding the average score of 5.2.[174] Due to improved shareholder protection elsewhere, while the aggregate score for the U.S. increased to 7.5 for 2013 it did not rank quite as highly as in 2005. Three countries – China, Russia and France – each had scores exceeding the U.S. aggregate and Britain, Japan and Slovenia had equivalent overall scores.[175]

While with the ADRI the Illinois and Model Act present-day aggregate scores diverge from Delaware's (Tbls. 4-6) and the same occurs with Illinois with the ASDI (Tbls. 7, 8), with the CBR SPI all three sources of law have present-day scores which are identical element-by-element (Tbl. 10). The fact that federal law (including stock exchange listing

---

173 Siems et al., *CBR Extended* (2009), *supra* note 90, at 105 (citing Barrett v. Denver Tramway Corp., 53 F. Supp. 198, 202 (D. Del. 1943), aff'd, 146 F.2d 701 (3d Cir.1944), citing Goldman v. Postal Tel., Inc., 52 F. Supp. 763 (D. Del. 1943)).

174 Armour *et al.*, *Shareholder*, *supra* note 47, 357, Table 2. (average calculated from figures provided in the table).

175 Katelouzou and Siems, *supra* note 85, 7.

Electronic copy available at: https://ssrn.com/abstract=2595693

rules) determined the relevant score with five variables and influenced the scoring for a sixth contributed substantially to this uniformity.

Table 10: Illinois/Model Act Present-Day CBR SPI Scores

CBR SPI Element	Illinois/Model Act score (2013/present day)	Justification for present day score
Powers of the general meeting for de facto changes.	0.75/0.75	Illinois -- IBCA, §11.60 (same standard as Delaware). Model Act §12.02(a) (in effect requiring a shareholder vote if less than 25% of assets will remain after a disposition.)
Agenda setting power.	1/1	Federal securities law (see Table 9).
Anticipation of shareholder decision facilitated.	1/1	NYSE listing rules/federal securities law (see Table 9).
Prohibition of multiple voting rights.	0.5/0.5	NYSE listing rules (see Table 9).
Independent board members.	1/1	NYSE listing rules (see Table 9).
Feasibility of director's dismissal.	0.75/0.75	IBCA (§ 8.35) and Model Act (§ 8.08) both permit shareholders to dismiss directors without cause but executives dismissed without cause could still sue for compensation (see *supra* note 172, *infra* notes 206-7 and accompanying text). The Dodd-Frank provisions concerning "say on pay" amend federal securities law.
Private enforcement of director duties.	0.75/0.75	As is the case with Delaware (see Table 9) derivative actions are feasible under the IBCA and the Model Act but the requirements that mean that a "1" is not justified also apply. On the necessity of demand, see IBCA § 7.80(b), Model Act § 7.42(1). On special litigation committees, see Weiland v. Illinois Power Co. 1990 WL 267364 (accepting the use of a special litigation committee) ; Model Act §§ 1.43, 7.44 (indicating that a derivative suit can be dismissed by "qualified" directors, these being directors lacking a material interest in the challenged transaction). On contemporaneous ownership see IBCA § 7.80(a), Model Act § 7.41(1).
Shareholder action against resolutions of the general meeting.	1/1	Cases cited to justify a "1" for Delaware are consistent with general common law trends.[176]

[176] See Rutherford B. Campbell, *Corporate Fiduciary Principles for the Post-Contractarian Era*, 23 FLA. ST. UNIV. L. REV. 561, 573 (1996) (treating the cases cited as authoritative jurisprudence concerning recapitalizations involving preferred shareholders).

Electronic copy available at: https://ssrn.com/abstract=2595693

Mandatory bid.	0/0	See Table 9; the position is the same under Illinois law and the Model Act.
Disclosure of major shareholder ownership.	0.75/0.75	Federal securities law (see Table 9).
Total	**7.5/7.5**	

C. Historical Trends

1. ADRI

Turning from the present day to historical trends, with four of the six ADRI variables it appears that going back through time – to 1899 in the case of Delaware and Illinois and to 1950 for the Model Act -- the scores remained unchanged. First, with voting by proxy, just as is the case today, Delaware and Illinois corporate legislation authorized shareholders to vote in this manner in 1899 without requiring that proxies provide for "two-way" voting.[177] The Model Act has done likewise since 1950.[178]

Second, our searches failed to reveal any historical evidence of statutory provisions in Delaware or Illinois corporate legislation or the Model Act designed to block the transfer of shares prior to shareholder meetings.[179] Third, with the oppressed minority variable even though the right of shareholders to file derivative suits against directors was only first confirmed specifically by Delaware courts in the early 1920s, it was clearly available in Illinois as the nineteenth century drew to a close.[180] More generally the derivative suit's

---

[177] Delaware General Corporation Law (1899), § 20; Illinois General Corporation Law of 1874, §3.

[178] Model Business Corporation Act, 1950, §31.

[179] There were at various points in time statutory provisions that gave a corporation's directors the power to close the stock transfer books prior to a shareholder meeting to fix who was permitted to vote. See, for example, Delaware General Corporation Law 1925 § 17; Model Business Corporations Act 1950, §28. These measures, however, did not authorize the directors to preclude dealing in the shares.

[180] Allied Chemical & Dye Corp. v. Steel & Tube Corp. of America, 120 A. 486, 491 (Del. 1923); Fleer v. Frank H. Fleer Corp., 125 A. 411, 415 (Del. Ch. 1924); Wheeler v Pullman Iron & Steel Co., 32 N.E. 420, 422-23 (Ill. 1892); City of Chicago v. Cameron, 11 N.E. 899, 903 (Ill. 1887).

Electronic copy available at: https://ssrn.com/abstract=2595693

origins can be traced back in the U.S. at least as far as 1831,[181] and it was widely understood to be a general feature of U.S. corporate law by the late nineteenth century.[182] Correspondingly, a "1" is the appropriate score for Delaware as well as Illinois from the present day back to 1899 and for the Model Act back to 1950.

Finally, with rights shareholders have to call a shareholder meeting, Delaware has only regulated this topic by statute since 1967 and has never specifically authorized shareholders owning a designated percentage of shares to take this step.[183] While Illinois has empowered shareholders to call shareholder meetings since 1872 and the ownership threshold was reduced from two-thirds to 20% in 1919, the relevant figure has always exceeded the 10% threshold required to receive a "1" under the ADRI.[184] The Model Act, in contrast, has since 1950 authorized shareholders owning 10% or more of a corporation's shares to call a meeting, thus meriting a "1."[185]

Cumulative voting and pre-emptive rights are the two ADRI variables where change has occurred, with the moves being from "1" to "0" in each case. With cumulative voting, the Model Act is the only legal regime affected, with the score falling from "1" to "0" in 1969.[186] Delaware specifically authorized companies to "opt in" to this method of director selection in 1919 but never established cumulative voting as a default rule, meaning its cumulative voting score was "0" from 1899 to the present day.[187] While Illinois displaced a

---

181 Taylor v. Miami Exporting Co., 5 Ohio 162 (1831). The U.S. Supreme Court recognized the derivative suit in Dodge v Woolsey, 59 U.S. 331 (1855), which subsequently became the leading case. See Cheffins, Bank, and Wells, *Law by Numbers*, *supra* note 26, at 1749.

182 *See, e.g.*, VICTOR MORAWETZ, A TREATISE ON THE LAW OF PRIVATE CORPORATIONS 236 (1886).

183 Delaware General Corporation Law 1967, §211(d); Cheffins, Bank and Wells, *Questioning*, *supra* note 32, at 609.

184 Illinois Revised Statutes, 32 § 22, 702 (Harvey Hurd and B. Bradwell Helmer eds., 1917); Illinois General Corporation Act 1919, §40.

185 Model Business Corporation Act, 1950, §26.

186 On the chronology, see Cheffins, Bank, and Wells, *Law by Numbers*, *supra* note 26, at 1750-51.

187 29 Del. Laws c. 113, § 9; Cheffins, Bank and Wells, *Questioning*, *supra* note 32, at 609.

Electronic copy available at: https://ssrn.com/abstract=2595693

long-standing mandatory cumulative voting rule in favor of a presumptive rule in 1984,[188] "1" remains the appropriate score throughout because default rules are taken into account when scoring with the ADRI.

With pre-emptive rights all three jurisdictions experienced a change, with the score dropping from "1" to "0" in each instance. At common law, shareholders had pre-emptive rights,[189] meaning that as of 1899 Delaware and Illinois both scored "1"with this variable and the Model Act did likewise on its inception in 1950. The inaugural version of the Model Act expressly permitted shareholders to waive their pre-emptive rights,[190] as Delaware and Illinois had done since 1927 and 1933 respectively.[191] These enabling measures were insufficient to change a score of "1" to "0". This occurred with Delaware, Illinois and the Model Act in 1967, 1982 and 1984 respectively when pre-emptive rights were eliminated unless the articles of incorporation provided otherwise.[192]

Since all changes affecting the ADRI over time were from "1" to "0", it was inevitable that the time trend with the ADRI would be downwards. Moreover, with changes only affecting two of the ADRI variables, it was likely that changes to aggregate scores would be modest. This indeed was the case with Delaware, where the only change was from "4" to "3" ("3" to "2" using Spamann's methodology) due to the 1967 displacement of pre-emptive rights (Tbl. 11). Illinois was the same, with the aggregate score falling from "5" to "4" ("4" to "3" using Spamann's methodology) in 1982 due to the same change (Tbl. 11). These findings lend support to conjectures that meaningful competition between states in the

188 Illinois General Corporation Law of 1874, §3; Illinois Business Corporations Act 1984, §7.40.

189 Wells, *Modernization*, *supra* note 65, at 610-11; ADOLF BERLE AND GARDINER C. MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY 133-34 (1932).

190 Model Business Corporation Act, 1950, §24.

191 Delaware General Corporation Law 1927 § 5, para. 10; Illinois Business Corporations Act 1933, § 24.

192 Delaware General Corporation Law 1967, §102(b)(3); Business Corporations Act – Shareholder Rights, Pub. Act 82-650 (Ill.), § 1; Model Business Corporations Act, §6.30, Annotation, Historical Background, 2. Model Act (indicating as well that a provision was added to the MBCA in 1961 providing for abolition of pre-emptive rights that was set out as an alternative to the 1950 "opt out" approach).

Electronic copy available at: https://ssrn.com/abstract=2595693

corporate law realm "has now long since ended"[193] and amounts not to a race but a "leisurely walk."[194]

Table 11: Aggregate ADRI Scores, Delaware, Illinois and Model Act, 1899-Present

	1899	**1950**	**1967**	**1969**	**1982**	**1984**	**Present day**
Delaware (DLLS/Spamann)	4/3	4/3	**3/2**	3/2	3/2	3/2	3/2
Illinois (DLLS/Spamann)	5/4	5/4	5/4	5/4	**4/3**	4/3	4/3
Model Act (DLLS/Spamann)	X	6/5	6/5	**5/4**	5/4	**4/3**	4/3

Note: Scoring changes are identified in **bold**.

With the Model Act, because the 1984 displacement of pre-emptive rights was preceded by the 1969 side-lining of cumulative voting, the downwards trend was more pronounced. However, the drop occurred from a very high initial starting point. The Model Act's ADRI aggregate score of "6" for 1950 to 1969, following DLLS's coding, exceeded the score of each country DLLS considered when revising the ADRI.[195] With Spamann's recoding, among the countries he coded only South Korea and Spain, with scores of "6", exceeded the Model Act's 1950 to 1969 score of "5".[196]

2. ASDI

With Delaware, Illinois and the Model Act there has been little change over time with the ASDI private control of self-dealing index. With the ex ante sub-index, statutory provisions mandating shareholder approval or independent review of related party

193 Marcel Kahan and Ehud Kamar, *The Myth of State Competition in Corporate Law*, 55 STAN. L. REV. 679, 724 (2002).

194 Bebchuk and Hamdani, *Vigorous Race*, *supra* note 8.

195 *Supra* note 70 and related discussion.

196 Spamann, *Antidirector*, *supra* note 39, at 475.

Electronic copy available at: https://ssrn.com/abstract=2595693

transactions have never been a feature of state corporate law in the United States. Correspondingly, scores with these variables are "0" going back through time (Tbl. 12).

Table 12: ASDI Ex-ante Private Control of Self-Dealing -- Delaware, Illinois and the Model Act, 1899-Present

ASDI Element	1899 -- Delaware/Illinois/Model Act	1950 – Delaware/ Illinois/Model Act	1984 – Delaware/ Illinois/Model Act	Present day – Delaware/Illinois/Model Act (see Tables 7)
Approval by disinterested shareholders	0/0/x	0/0/0	0/0/0	0/0/0
Disclosure by Buyer Co.	1/1/x	1/1/1	1/**0**[197]/1	1/0/1
Disclosure by Mr. James	1/1/x	1/1/1	1/**0**/1	1/0/1
Independent Review	0/0/x	0/0/0	0/0/0	0/0/0
Ex ante disclosure	0.67/0.67/x	0.67/0.67/0.67	0.67/**0**/0.67	0.67/0/0.67
Ex-ante Private Control of Self-Dealing	0.33/0.33/x	0.33/0.33/0.33	0.33/**0**/0.33	0.33/0/0.33

Note: Scoring changes are identified in **bold**.

Where change did occur was with respect to required disclosure by Mr. James and Buyer Co. The Delaware and the Model Act were unaffected. With Illinois, however, the "safe harbor" provision with wording that ensures ex ante disclosure was not even implicitly required began to govern in 1984 when the Illinois Business Corporation Act of 1983 (IBCA)

[197] Illinois initially had a statutory provision specifically governing related party transactions in 1981 – Illinois Business Corporations Act 1933, §40a. The enactment of this provision would not have reduced Illinois' Disclosure by Buyer Co. and Disclosure by Mr. James scores in the same way as the 1984 provision because the 1981 provision specifically required disclosure of the transaction to the board before a court could save the transaction. On the nature of the 1981 provision, see Church, *Director Conflict of Interest*, *supra* note 157, at 746-47.

Electronic copy available at: https://ssrn.com/abstract=2595693

came into force.[198] Prior to this, the common law would have applied and full disclosure likely would have been required for a court to exercise the discretion it would have had to relieve parties of the adverse consequences potentially associated with related party transactions.[199] Hence, the only change to the ex ante private control of self-dealing index going back to 1899 was that Illinois' ex ante disclosure score fell from 0.67 to 0 in 1984, which in turn reduced Illinois' overall ex ante private control of self-dealing index score from 0.33 to 0.

As with the ex ante private control of self-dealing sub-index, with the ex post sub-index the scoring only changed for one variable going back through time, though the change was not restricted to one jurisdiction. The variable affected was disclosure in public filings, with the relevant change occurring in 1935 when disclosure of material contracts between the company and any of its directors or officers became compulsory under federal securities law.[200] The change more than doubled Delaware and Illinois' ex-post private control of self-dealing score and increased the overall anti-self-dealing index score for both jurisdictions from 0.41 to 0.65 (Tbl. 13).

Table 13: ASDI Ex-post Private Control of Self-Dealing -- Delaware, Illinois and the Model Act, 1899-Present

ASDI Element	1899 -- Delaware/Ill./	1935 -- Delaware/Ill./	1950 – Delaware/	1984 – Delaware/	Present Day – Delaware/ Ill./Model Act

198 805 ILCS 5/8.60 (safe harbor provision); Ill. Rev. Stat. ch. 32 ¶¶ 1.01-16.10 (IBCA). On when the Illinois Business Corporation Act of 1983 came into force, see James M. Van Vliet, *The New Illinois Business Corporation Act Needs More Work*, 61 CHI. KENT. L. REV. 1, 2 (1985).

199 On the necessity for disclosure under the common law, *see Corporations – Directors – Transactions Involving Conflicts of Interest*, 42 ORE. L. REV. 61, 64 (1962) ("A finding of nondisclosure will make a consideration of other facets of a transaction unnecessary in most cases. Nondisclosure of an interest by a director may constitute unfairness per se under the fairness test and thus make the transactions voidable."); Note, *The Fairness Test of Corporate Contracts with Interested Directors*, 61 HARV. L. REV. 335, 338 (1948) ("The courts usually require of the interested director full disclosure of his interest and of those facts, such as his own purchase price, which would affect the board's decision to buy.") With respect to Illinois, pre-1984 there was conflicting case law concerning related party transactions but in Shlensky v. South Parkway Bldg. Corp., 19 Ill. 2d 268, 283 (1960) full disclosure was identified as a factor that would determine the outcome of a fairness test. *See* Church, *Director Conflict of Interest*, *supra* note 157, at 746, 749-50.

200 Cheffins, Bank, and Wells, *Law by Numbers*, *supra* note 26, at 1759.

Electronic copy available at: https://ssrn.com/abstract=2595693

	Model Act	Model Act	Ill./Model Act	Ill./Model Act	(see Table 8)
Disclosure in periodic filings	0/0/x	**1/1**/x	1/1/1	1/1/1	1/1/1
Standing to sue	1/1/x	1/1/x	1/1/1	1/1/1	1/1/1
Rescission	1/1/x	1/1/x	1/1/1	1/1/1	1/1/1
Ease of holding Mr. James liable	1/1/x	1/1/x	1/1/1	1/1/1	1/1/1
Ease of holding approving body liable	1/1/x	1/1/x	1/1/1	1/1/1	1/1/1
Access to evidence	0.75/0.75/x	0.75/0.75/x	0.75/0.75/0.75	0.75/0.75/0.75	0.75/0.75/0.75
Ease of proving wrongdoing	0.95/0.95/x	0.95/0.95/x	0.95/0.95/0.95	0.95/0.95/0.95	0.95/0.95/0.95
Ex-post Private Control of Self-dealing	0.48/0.48/x	**0.98**/**0.98**/x	0.98/0.98/0.98	0.98/0.98/0.98	0.98/0.98/0.98
Anti-self-dealing index	0.41/0.41/x	**0.65**/**0.65**/x	0.65/0.65/0.65	0.65/**0.49**/0.65	0.65/0.49/0.65

Note: Scoring changes are identified in **bold**.

With other variables in the ASDI ex-post private control of self-dealing index, scores for "Access to evidence" have remained unchanged over time because Delaware and Illinois civil procedure rules provided as far back as 1899 for the same core litigant rights that justify the present-day score of 0.75.[201] With the variables measuring standing to sue, rescission and the ease of holding Mr. James and the approving body (i.e. the board) liable, at present common law principles provide the justification for the "1"s awarded to Delaware, Illinois and the Model Act (Tbl. 8). The same common law principles should have been applicable

[201] On the right to request documents relevant to the case from the defendant, see Rules of the Revised Statutes of the State of Delaware (1893), Ch. 30, vol. 13, § 13; Ill. Rev. Stat., ch. 51 §9 (1874). On the right to examine the defendant without a court approving the questions, see Rules of Equity Practice in the Court of Chancery (1868), R. 40, §§24-28 (setting out rules for witnesses), §1 (indicating parties were not excluded from being witnesses). On the right to examine non-parties without a court approving the questions, see Rules of Equity Practice in the Court of Chancery (1868), R. 48; Ill. Rev. Stat., ch. 51 §§24-28 (1874).

Electronic copy available at: https://ssrn.com/abstract=2595693

back to 1899. Verifying this point definitively admittedly is not feasible. For instance, Delaware lacked any case law directly focusing related party transactions until the early 1920s.[202] Still, the trend of authority from other states should, in the absence of Delaware jurisprudence, provide a reasonably accurate characterization of what the law would have been in Delaware prior to that point.[203]

3. CBR SPI

With both the ADRI and the ASDI there were relatively few changes to scores over time and, other than the 1935 introduction of the requirement of ex post disclosure of related party transactions, what changes there were all moved scores downwards. The situation was much different with the CBR SPI. With the CBR SPI, the aggregate score changed reasonably often and there was a marked upward trend with aggregate scores (Fig. 1). There were changes at the state level as far back as 1903, with the pace of change increasing starting in 1950. Each change at the state level, with two exceptions, moved scores upward (Tbl. 14). This trend was strongly reinforced by changes made to federal securities law and NYSE listing rules (Tbl. 15), the content of which the SEC strongly influences.[204]

Figure 1: CBR SPI Aggregate Scores for Delaware, Illinois and the Model Act, 1899-Present

202 Cheffins, Bank, and Wells, *Law by Numbers*, *supra* note 26, 1762.

203 There was pre-1920s case law from New York which indicated that individual shareholders might lack standing to challenge related party transactions. Even if this was in fact the law, the doctrine was subject to sufficiently wide exceptions to suggest a "1" was the appropriate score for standing to sue. See Cheffins, Bank, and Wells, *Law by Numbers*, *supra* note 26, at 1761-62.

204 *Supra* notes 134-35 and related discussion.

Electronic copy available at: https://ssrn.com/abstract=2595693

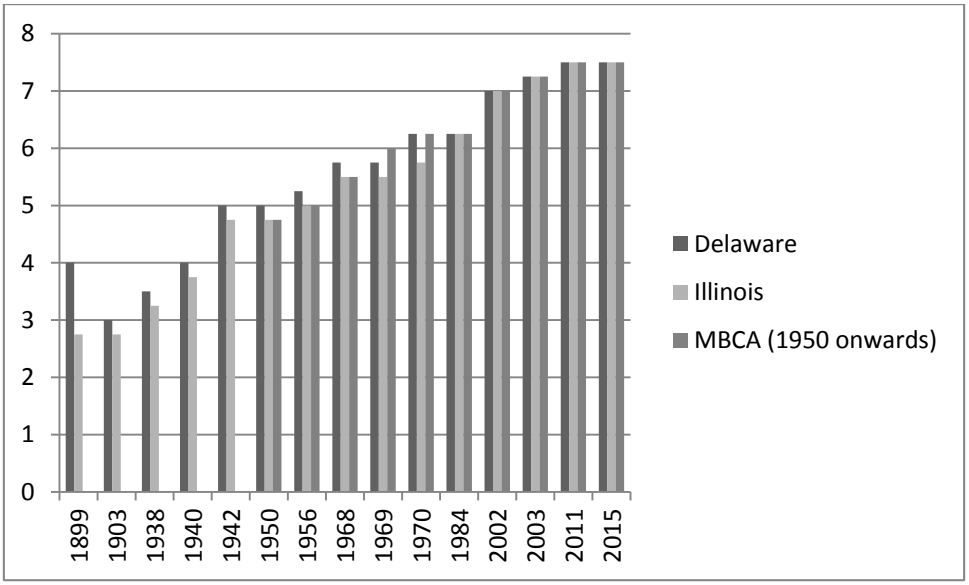


Table 14: Changes to CBR SPI Scores for Individual Variables Generated by State Law -- Delaware, Illinois and the Model Act, 1899-Present

Year	CBR SPI Variable	Jurisdiction(s) Affected	Score Change	Explanation
1903	Prohibition of multiple voting rights	Delaware	1 to 0	The Delaware General Corporation Law of 1899 authorized the issuance of share classes with different voting rights but it only took full effect with the 1903 repeal of a provision in the Delaware Constitution of 1897 which stated that "in all elections for directors or managers of stock corporations, each shareholder shall be entitled to one vote for each share of stock he may hold."[205]
1950	X	Model Act	X	Model Act first introduced.
1969	Feasibility of director's dismissal.	Model Act	0 to 0.5	In 1960, the forerunner to the current Model Act § 8.08 was introduced as an "optional" provision and in 1969 the optional designation was removed.[206] This displaced the common law rule, which was that shareholders could only remove directors for cause, reflecting the fact that the directors had a statutory entitlement to their office.[207] The common law rule would

205 *Brooks v. State ex rel. Richards*, 79 A. 790, 800 (Del. 1910).

206 Model Business Corporations Act, §8.08(a), Annotation, History – Historical Background, 2. The Model Act.

207 COX & HAZEN, *supra* note 7, §9.14; MBCA, §8.08, Official Comment.

Electronic copy available at: https://ssrn.com/abstract=2595693

				score a "0" under the CBR SPI coding protocol.[208]
1970	Feasibility of director's dismissal.	Delaware	0.25 to 0.5	DGCL § 141(k) enacted,[209] which the CBR SPI coders rely upon to give Delaware/U.S. a 0.5.[210]
1982	Prohibition of multiple voting rights	Illinois	1 to 0.5	IBCA § 28 amended to allow corporations formed after December 31, 1981 to eliminate voting rights attached to shares, including those relating to cumulative voting .[211]
1984	Feasibility of director's dismissal.	Illinois	0 to 0.5	IBCA § 8.35 enacted, displacing the common law rules which offered shareholders little, if any, scope to dismiss directors.[212]
2003	Private enforcement of director duties.	Delaware, Illinois, Model Act[213]	0.5 to 0.75	The private enforcement of directors' duties score increased due to case law developments "evidenc(ing) a heightening of judicial scrutiny on directors in the wake of the corporate governance scandals."[214]

208 Under the "feasibility of director's dismissal" the CBR coders gave jurisdictions a "0" if "good reason (was) required for the dismissal of directors": Armour *et al.*, *Shareholder*, *supra* note 47, 354, Table 1.

209 Laws of 1970, ch. 437, http://delcode.delaware.gov/sessionlaws/ga127/chp437.shtml.

210 Siems et al., *CBR Extended* (2009), *supra* note 90, at 104. Prior to the enactment of § 141(k), the Delaware General Corporation Law contained a provision indicating that directors could be removed but it was unclear whether this had to be for cause. *See* Charles H. Nida, *Note: The New Delaware Corporation Law*, 5 HARV. J. LEGISL. 413, 427-28 (1968). Delaware had a provision of this sort going back to 1899. *See* Katharina Pistor et al., *The Evolution of Corporate Law: A Cross-Country Comparison*, 23 U. PA. J. INT'L. ECON. L. 791, 815 (2002). A pre-1970 score of 0.25 appears to be appropriate, which the CBR SPI coders award when it is clear that a director can be dismissed but would always be compensated: Armour *et al.*, *Shareholder*, *supra* note 47, at 354, Tbl 1.

211 *See* Roanoke Agency v Edgar, 461 N.E.2d 1365, 1368 (Ill. 1984)

212 *See*, for example, Van Vliet, *supra* note 198, 34 ("New BCA section 8.35 reflects a basic public policy change, granting statutory authority for the removal of directors with or without cause, by shareholder action. There was no counterpart to this in the old BCA so that, prior to the New BCA, only the common law right to remove a director for cause existed".) The common law rule generally applicable in U.S. states was that directors could only be removed before the end of their terms "for cause," but this rule was gradually displaced by statute beginning in the 1930s. *See* HENRY W. BALLANTINE, BALLANTINE ON CORPORATIONS (2d ed. 1946) 433-34. The law may have remained restrictive in Illinois because, prior to the adoption of the 1983 Illinois Business Corporation Act, "there was no statutory provision for removal of directors" (Voss Engineering Inc. v Voss Industries Inc., 481 N.E.2d 63, 66 (Ill. App. 1985)). At least one Illinois court had earlier suggested that allowing shareholders to remove a director even for cause would be inappropriate because this would permit an end-run around cumulative voting requirements of the Illinois constitution. *See* Laughlin v Geer, 121 Ill. App. 534, 538-39 (1905) as well as more generally CHARLES MURDOCK, 7 ILL. PRAC. BUS. REORGANIZATIONS § 11.18 (2nd ed. 2010).

213 With this case law driven change in scoring, each case cited was from Delaware: Siems et al., *CBR Extended* (2009), *supra* note 90, at 105. Given, however, our policy of deferring to coding by those who constructed the original indices (*see supra* note 68 and related discussion) and given the influential nature of Delaware case law, we have assumed the private enforcement of director duties score would increase with Illinois and the MBCA as well as with Delaware.

214 Siems et al., *CBR Extended* (2009), *supra* note 90, at 105.

Electronic copy available at: https://ssrn.com/abstract=2595693

Table 15: Changes to CBR SPI Scores for Individual Variables Generated by Changes to Federal Law-- Delaware, Illinois and the Model Act, 1899-Present

Year	CBR SPI Variable	Jurisdiction(s) Affected	Score Change	Explanation
1938	Anticipation of shareholder decision facilitated.	Delaware, Illinois	0.5 to 1	SEC Rule X-14A-2, forerunner to SEC Rule 14a-4(b)(1), adopted.[215]
1940	Prohibition of multiple voting rights.	Delaware[216]	0 to 0.5	The NYSE introduced a rule precluding the listing of non-voting common stock.[217]
1942	Agenda setting power.	Delaware, Illinois	0 to 1	Shareholder proposal mechanism that is now SEC Rule 14A-8 introduced as rule X-14A-7.[218]
1956	Independent board members.	Delaware, Illinois, Model Act	0 to 0.25	Companies listed on the NYSE were required to have at least two independent directors.[219]

[215] On the chronology with the SEC rule *see* Sheldon E. Bernstein and Henry G. Fischer, *The Regulation of the Solicitation of Proxies: Some Reflections on Corporate Democracy*, 7 U. CHI. L. REV. 226, 229 (1940). On the pre-1938 scoring, according to the CBR SPI protocol a "0.5" is justified if postal/proxy voting is merely authorized. State laws that justify a coding of "1" for Delaware and Illinois for the ADRI proxy voting variable date back to 1899 (*supra* note 177 and related discussion) should meet this threshold. The CBR SPI coders cite a 1959 NYSE listing rule compelling companies to solicit proxies to justify the "1" they give the United States with the "Anticipation of shareholder decision facilitated" – *see supra* Tbl. 9. On the fact that the relevant listing rule was not introduced until 1959, see Douglas C. Michael, *The Untenable Status of Corporate Governance Listing Standards Under the Securities Exchange Act*, 47 BUS. LAW. 1461, 1469 (1992); Thompson, *Delaware, supra* note 106, at 795.

[216] Illinois' score for this variable did not increase in 1940 because it was already "1" due to a provision in the Illinois constitution prohibiting the use of share classes with different voting rights for directors' elections. *See* ILL. CONST. art XI, § 3 (1870) (replaced 1970) ("in all elections for directors or managers of incorporated companies, every stockholder shall have the right to vote . . . for the number of shares owned by him . . . or to cumulate said shares, and give one candidate as many votes as the number of directors multiplied by the number of his stock shall equal"). *See also* H. W. Ballantine, *A Critical Survey of the Illinois Business Corporation Act*, 1 U. CHI. L. REV. 357, 386 (1934).

[217] Stephen M. Bainbridge, *The Short Life and Resurrection of SEC Rule 19C-4*, 69 WASH. U.L.Q. 565, 569 (1991). The NYSE had refused to list corporations with dual-class capitalizations beginning in 1926, but did not adopt a formal rule forbidding such listings until 1940. *See* JOEL SELIGMAN, THE TRANSFORMATION OF WALL STREET: A HISTORY OF THE SECURITIES AND EXCHANGE COMMISSION AND MODERN FINANCE 585-86 (3d ed. 2003).

[218] George W. Dent, *SEC Rule 14a-8: A Study in Regulatory Failure*, 30 N.Y.L. SCHOOL REV. 1, 3-4 (1985). *See also* Susan W. Liebeler, *A Proposal to Rescind the Shareholder Proposal Rule*, 18 GEO. L. REV. 425, 427-28 (1984); Mortimer M. Caplin, *Proxies, Annual Meetings and Corporate Democracy: The Lawyer's Role*, 37 VA. L. REV. 653, 669 (1951) (indicating that prior to 1942 the SEC had said companies should set shareholder proposals forth in proxy soliciting materials but only specifically permitted a shareholder to submit a proposal at that point).

[219] Thompson, *Delaware, supra* note 106, 795; Michael, *supra* note 215, 1469.

Electronic copy available at: https://ssrn.com/abstract=2595693

1968	Disclosure of major shareholder ownership.	Delaware, Illinois, Model Act	0 to 0.5	The Williams Act[220] introduced Securities Exchange Act 1934, § 13(d) and Schedule 13D of the Act, which required shareholders owning 10% or more of the shares of an issuer governed by the Act to disclose its stake.
1970	Disclosure of major shareholder ownership.	Delaware, Illinois, Model Act	0.5 to 0.75	Ownership disclosure threshold applicable to Securities Exchange Act 1934, § 13(d) and Schedule 13D reduced to 5%.[221]
2002	Independent board members.	Delaware, Illinois, Model Act	0.25 to 1	NYSE Manual, § 303A.01 (2002) adopted.
2011	Dismissal of directors.	Delaware, Illinois, Model Act	0.5 to 0.75	The Dodd-Frank Act of 2010 provided shareholders with the right to an advisory "say on pay" vote.[222]

D. Our Hypotheses Revisited

To distil our findings we return to the three hypotheses we sought to test with our historical analysis of the ADRI, ASDI and CBR SPI.[223] Our first hypothesis (H1) presupposes a state-driven race to the bottom and would be verified if scores fell in relation to those elements of shareholder protection indices determined by state law. Our findings on balance confirm H1, but the trend was not robust. With the ADRI, the aggregate scores for Delaware and Illinois did drop, but only did so by one point out of six when those jurisdictions displaced pre-emptive rights. The Model Act's ADRI score fell by one point in 1969 and again by one in 1984 but the decline was from a very high starting point.[224]

With the ASDI there again was, with its state law elements, a downwards trend but continuity was the main theme. Between 1899 and the present day on only one occasion was there state law-driven change to the index, this being the 1984 amendment to Illinois law that

220 Pub. L. 90-439, 82 Stat. 454 (1968).

221 Pub. L. No. 91-567, 84 Stat. 1497 (1970).

222 *Supra* note 126 and related discussion.

223 See Part III.A.

224 *Supra* notes 195-96 and related discussion.

Electronic copy available at: https://ssrn.com/abstract=2595693

meant that advance disclosure of related party transactions was no longer even implicitly required.[225] Finally, while with the ADRI and the ASDI changes to state law reduced aggregate scores, with the CBR SPI, the trend was mixed. State-law driven changes to this index affecting the use of share classes with multiple voting rights caused the scores of Delaware and Illinois to decline while those relating to director dismissal and enforcement of directors' duties pushed the scores of Delaware, Illinois and the Model Act up (Tbl. 14). The upshot is that H1 is confirmed, but the trend was neither robust nor entirely uniform.

Our second and third hypotheses (H2 and H3) relate to the impact of federal law on shareholder protection over time. H2 presupposes that changes to federal law should bolster shareholder rights. The assumption underlying H3 is that changes to federal law were significant, and significant enough to outweigh whatever downward pressure a state-driven "race to the bottom" had.

H2 and H3 are strongly confirmed. Federal law was not taken into account with the coding of the ADRI and each of the changes to this index that decreased Delaware, Illinois and the Model Act's aggregate score correspondingly occurred at state, not federal, level. While federal law was taken into account with the ASDI, scoring for private control of self-dealing was dictated primarily by state law (Tbls. 7, 8). Still, with the one element determined by federal law -- disclosure in periodic filings – federal reform drove scores upwards in what was otherwise a very stable environment over time.[226]

The impact of federal law was considerably more pronounced with the CBR SPI. Unlike with the ADRI and the ASDI, federal law (defined to include national stock exchange listing rules)[227] had a major impact on the CBR SPI's scoring for Delaware, Illinois and the

---

225 *Supra* note 157 and accompanying text.

226 *Supra* notes 198-201 and related discussion.

227 On why, see *supra* notes 129, 132-33 and accompanying text.

Electronic copy available at: https://ssrn.com/abstract=2595693

Model Act, with federal rules accounting for the scoring of five of its ten elements and influencing a sixth.[228] Overall, the aggregate CBR SPI scores for each jurisdiction increased markedly between 1938 and 2003 (Fig. 1), with changes to federal law accounting for most of the upward movement (Tbl. 15). CBR SPI trends correspondingly indicate that federal developments substantially bolstered shareholder protection (H2) and more than cancelled out whatever movement downwards was associated with changes to state law (H3).

IV. "PRESENT-DAY" BIAS?

The fact that our second and third hypotheses were strongly confirmed affirms the significance of a theme that has moved to the forefront quite recently in the literature on corporate law federalism, namely that the federal government is an important player.[229] The weak confirmation of H1 combined with the strong confirmation of H2 and H3 runs contrary to a much better established element of the received wisdom, this being that competition between states served to erode shareholder protection substantially over time. Our results indicate federal intervention more than outweighed a relatively weak trend in favor of diminution of shareholder protection at the state level, meaning that on a net basis shareholder rights became more robust over time.

While our historical findings cast doubt on the received wisdom that jurisdictional competition resulted in a net erosion of shareholder rights and confirm the accuracy of the more recent theory that federal intervention has done much to shape shareholder protection, this presupposes that our indices measure what was really occurring. This cannot be taken for granted. Given the historical orientation of our leximetric investigation a source of particular concern is that the indices are afflicted by a "present-day" bias.

---

228 The five variables were Agenda setting power, Anticipation of shareholder decision facilitated, Prohibition of multiple voting rights, Independent board members and Disclosure of major shareholder ownership and the sixth was dismissal of directors. See Tables 9 and 10. With anticipation of shareholder decision facilitated, state law was potentially relevant as well. See *supra* note 215.

229 *Supra* notes 17-18, 20 and related discussion.

Electronic copy available at: https://ssrn.com/abstract=2595693

This Part elaborates initially on why present-day bias is potentially a source of concern. We then carry out cross-checks which indicate that whatever bias exists with the indices we use is insufficient to compromise our findings materially. We ultimately show that our historical analysis of corporate law indices provides reliable evidence that whatever erosion of shareholder protection has occurred under state law since 1900 has been modest and that a federally-oriented surge in shareholder rights has been a significant countervailing influence.

A. Reasons for Concern

Mathias Siems, often together with co-authors, has on various occasions suggested that when LLSV constructed the ADRI they fell into a trap that comparative lawyers seek to avoid, namely imposing one's own pre-conceptions on foreign legal systems.[230] Siems maintains that the fact that cumulative voting was included in the ADRI -- a topic historically widely debated in the United States but not elsewhere – and the law on removal of directors was not -- legal rules in the United States that can entrench boards have been heavily criticized as being shareholder-unfriendly – betray a pro-U.S. bias in the ADRI.[231] Though plausible, Siems' conjectures do not fit the facts comfortably. If the ADRI was, as Siems alleges, affected by a pro-U.S. bias, one might have expected that this would translate into high scores for the supposedly favored country. It is true that under LLSV's original ADRI the United States did score "5" out of "6."[232] However, with DLLS' and Spamann's ADRI

---

230 Lele and Siems, *Shareholder Protection I*, *supra* note 27, at 20-21; Armour *et al.*, *Shareholder*, *supra* note 47, at 349; Mathias M. Siems, *What Does Not Work in Comparing Securities Law: A Critique on La Porta et al.'s Methodology*, [2005] INT. COMPANY COMM. L. REV. 300, 301.

231 Lele and Siems, *supra* note 27, at 20-21.

232 *Supra* note 96 and related discussion.

Electronic copy available at: https://ssrn.com/abstract=2595693

recoding, the U.S. aggregate score ("3" and "2" respectively) was substantially below the average for the countries taken into account.[233]

Given that our leximetric analysis of corporate law focuses exclusively on the United States throughout it is largely immaterial to us if the indices we deploy betray an implicit partiality for U.S. corporate law. There is, however, another type of bias that potentially affects the indices we rely upon that could compromise our results, namely a tilt in favor of scores increasing as time progressed. Bias of this sort is a source of concern partly because there are some variables in the indices we use where for substantial periods of time contemporaries would have been unaware that regulating the topic in question might have been beneficial for investors. Under such circumstances, the law governing U.S. corporations could not realistically generate positive scores for the variables in question. This could only begin to change when the value of the rules in question was recognized, which in turn would tend to bias upwards scores from recent decades, with scores rising as the new rules were introduced.

The CBR SPI variable concerning the mandating of a designated proportion of independent directors on the board is an example of an index element where a present-day bias exists. It appears that William Douglas in a 1934 *Harvard Law Review* article was the first to advocate that a majority of board seats be occupied by individuals not affiliated with management.[234] Under such circumstances, it would be unrealistic to expect that the law governing U.S. corporations would have scored positively with the independent director component of the CBR SPI prior to that point in time

---

233 Cheffins, Bank and Wells, *Questioning*, *supra* note 32, at 606, 608.

234 William O. Douglas, *Directors Who Do Not Direct*, 47 HARV. L. REV. 1305, 1314-15 (1934) (advocating the introduction of legislation mandating that stockholders independent of management should make up half of the board). On Douglas' pioneer status, see Bratton and McCahery, *Equilibrium*, *supra* note 105 at 661 (2006) ("Douglas' article set out the basic terms of the governance agenda that has guided corporate law reforms ever since"). Robert Gordon was another early advocate of mandating the appointment of independent directors: ROBERT A. GORDON, BUSINESS LEADERSHIP IN THE LARGE CORPORATION 347-50 (1945).

Electronic copy available at: https://ssrn.com/abstract=2595693

Even setting to one side the independent director variable the CBR SPI seems particularly susceptible to present-day bias. Those constructing the CBR SPI selected topics thought to form the core of international corporate governance "best practice" between 1995 and 2005.[235] In so doing, as they explicitly acknowledged, they intentionally focused on a period when change was on the policy agenda in numerous countries.[236] Given this, it should not be surprising that, consistent with the 1995-2005 trend for most of the 20 countries Siems and his CBR associates coded,[237] the CBR SPI scores for Delaware, Illinois and the Model Act increased by a full point out of ten between 2001 and 2003 (Fig. 1). For the period between 2006 and 2013, the CBR SPI scores for these jurisdictions increased again but only by a modest 0.25, opening the way for a number of countries to draw level with or pass the U.S.[238]

Present-day bias, in the form of index components with a strongly modern orientation, is, however, by no means an endemic feature with variables in the indices on which we focus. With many of the variables in the indices we draw upon it was theoretically possible for scores to be positive back to 1900. The "5" that Illinois had as early as 1899 using DLLS's ADRI scoring method and the very high scores the Model Act had when it was introduced in 1950 (Tbl. 11) indicate that at least for the ADRI "1"s have been for decades more than a theoretical possibility.

An additional potential source of an upwards present-day bias with the indices we deploy is that shareholders may have in the past had protections available to them that are no longer part of shareholder rights discourse. Due to their outdated nature, legal protections of this nature would be unlikely candidates for inclusion in the ADRI, ASDI and CBR SPI.

---

235 Armour *et al.*, *Shareholder*, *supra* note 47, at 355, 374.

236 *Supra* note 50 and accompanying text.

237 Siems, *Shareholder Protection*, *supra* note 28, at 122-23.

238 *Supra* notes 174-75 and related discussion.

Electronic copy available at: https://ssrn.com/abstract=2595693

Shareholders therefore may have had in 1900, 1910 or 1920 significant protections largely unknown today the indices would not capture. Correspondingly, reforms that compromised, eroded or abolished such rights would have occurred and diminished shareholder protection without reducing historical scores for Delaware, Illinois or the Model Act. Our historical leximetric exercise could in turn fail to capture going back through time the abrogation or abolition of potentially significant shareholder rights. We account for this aspect of present-day bias next.

B. What Shareholder Rights Mattered in 1929?

A plausible cross-check against present-day bias in the indices we use to measure historical shareholder protection trends is to identify what shareholder rights were thought to matter in the past and ascertain whether these have been eroded over time. Conducting such an exercise is not straightforward because those writing about corporate law in the opening decades of the 20th century were not constructing indices in the same way as LLSV, DLLS and those responsible for the CBR SPI. However, a 1929 book by John Sears, *The New Place of the Stockholder*,[239] provides a helpful substitute.

Sears indicated that with his book "the aim and purpose [was] to consider methods and practices proposed to *protect the stockholder, use the stockholder, and help the stockholder*."[240] He identified as a departure point "an understanding of the deeply fundamental character of the stockholder's legal rights"[241] and composed a 14-point "list of strict legal rights, powers and remedies" so "[t]hat we may more clearly understand where we

239 JOHN SEARS, THE NEW PLACE OF THE STOCKHOLDER (1929).

240 *Id*. at 9. Emphasis in original.

241 *Id.* at 8.

Electronic copy available at: https://ssrn.com/abstract=2595693

stand."[242] This 14-point list can be used to capture a historically sensitive sense of trends concerning shareholder protection.

If it transpired that there had been in the decades following the 1929 publication of Sears' book a substantial erosion of the protections Sears identified, this would suggest that the indices we have relied upon are seriously compromised by present-day bias. Our findings correspondingly would have to be discounted considerably. As we will see, the legal rights on Sears' list remain largely intact today and to the extent they have been displaced the indices we use reflect the change. It follows that that the trends we have identified in fact are robust.

Sears' book, as with various others published during the same era dealing with shareholders and publicly traded corporations, would subsequently be overshadowed by Adolf Berle and Gardiner Means' landmark 1932 volume *The Modern Corporation and Private Property*.[243] Nevertheless, as Lawrence Mitchell has observed, Sears' views "were taken seriously" at the time of publication.[244] The *Wall Street Journal* referred to *The New Place of the Stockholder* as "One of the most timely books of recent date…."[245] and the *Boston Globe* described the book as "worthy" and "of "genuine interest and value" to "every stockholder."[246] At least one reviewer of *The Modern Corporation and Private Property* explicitly acknowledged Sears' book as a forerunner of Berle and Means' work[247] and Gardiner Means cited *The New Place of the Stockholder* in a 1930 *Quarterly Journal of*

---

242 *Id.* at 198.

243 BERLE & MEANS, *supra* note 189. For examples, of such books see Robert Hessen, *The Modern Corporation and Private Property: A Reappraisal*, 36 J.L. ECON. 273, 279-80 (1983) (citing THOMAS NIXON CARVER, THE PRESENT ECONOMIC REVOLUTION IN THE UNITED STATES (1925); WILLIAM Z. RIPLEY, MAIN STREET AND WALL STREET (1927); I. MAURICE WORMSER, FRANKENSTEIN INCORPORATED (1931)).

244 Lawrence E. Mitchell, *The "Innocent Shareholder": An Essay on Compensation and Deterrence in Securities Class-Action Lawsuits*, [2009] WISC. L. REV. 243, 273.

245 *New Publications: The New Place of the Stockholder*, WALL ST. J., Sept. 18, 1929, 20.

246 *Worthy Work Treats of Stockholders' Rights*, BOSTON GLOBE, Sept. 7, 1929, 4.

247 *Book Review: The Modern Corporation and Private Property*, 18 CORNELL L.Q. 634, 634 (1933).

Electronic copy available at: https://ssrn.com/abstract=2595693

Economics article Berle and Means drew upon heavily in *The Modern Corporation and Private Property*.[248] Sears' catalog of protections available to shareholders in 1929 thus can serve as a fair measure of the rights shareholders enjoyed at that moment.

With two items on Sears' 14-point list – cumulative voting and pre-emptive rights -- shareholder protections available in 1929 were eroded in subsequent decades. In both instances, however, we have already taken the topics in question into account for the purposes of this Article because they were ADRI components (Tbl. 16). With each item on Sears' list that was not dealt with by the ADRI, the rights Sears cited remain currently available to shareholders (Tbl. 17). This suggests that even if there is some element of present-day bias in the indices we use, our findings concerning shareholder protection trends remain valid.

Table 16: Elements of Sears' 14-Point List of Shareholder Rights That Were Also ADRI Components – ADRI Trends

Shareholder Right, Identified by Number of Sears' List	Sears' Description	ADRI Component	ADRI Trend
Right to vote (# 7) – proxy voting.	"The right to…vote by proxy…is provided by statute and court decisions (at p. 202)"	Vote by Proxy Allowed.	DLLS: Delaware "1" (1899-present); Illinois "1" (1899-present); Model Act "1" (1950-present) Spamann: DLLS: Delaware "0" (1899-present); Illinois "0" (1899-present); Model Act "0" (1950-present)[249]
Cumulative voting (# 8)	"To accumulate his votes in the election of directors, when statute or state constitution make this right compulsory, and to do so where such right is	Cumulative Voting	Delaware "0" (1899-present); Illinois "1" (1899-present); Model Act "1" (1950-69), "0" (1969-present)[250]

[248] Gardiner C. Means, The *Diffusion of Stock Ownership in the United States*, 44 Q.J. ECON. 561, 561 (1930). On Berle and Means' reliance on this research, see the preface to the 1932 edition of BERLE AND MEANS, *supra* note 189.

[249] *Supra* notes 143-44, 177-78 and related discussion.

[250] *Supra* notes 186-88 and accompanying text.

Electronic copy available at: https://ssrn.com/abstract=2595693

	permissive and the certificate of incorporation etc. provides therefor (at p. 202).		
Pre-emptive rights (#11)	"Preemptive right to participate in new issue upon increase of capital stock (at p. 202)"	Pre-emptive Rights	Delaware "1" (1899-1967), "0" (1967-present); Illinois "1" (1899-1982), "0" (1982-present); Model Act "1" (1950-84), "0" (1984-present).[251]
Derivative action (#12)	"To bring legal actions, in a representative capacity for all the stockholders, in the event the directors are acting fraudulently in withholding suit…(at p. 202).	Oppressed Minority	Delaware "1" (1899-present); Illinois "1" (1899-present); Model Act "1" (1950-present).[252]

Table 17: Additional Elements of Sears' 14-Point List of Shareholder Rights – Present-Day Situation

Shareholder Right, Identified by Number of Sears' List	Sears' Description	Present-Day Situation (Delaware, Illinois, Model Act)
Ultra vires (#1)	"Every stockholder, however small, has the right to insist that the purposes of the corporation be confined to those stated in the charter (at p. 198)."	Individual shareholders have standing to challenge *ultra vires* transactions if it would be equitable for this to occur.[253]
Shareholder voting on charter amendments (#2)	"To make amendments, to alter the charter, the statutes require the vote of holders of various proportions of stock (at p. 200)."[254]	Shareholder approval is generally required for corporations to amend their articles of incorporation – DGCL § 242(b)(1); 805 Ill. Comp. State. 5/10.20; Model Act § 10.03(b).
Calling stockholder meetings (#3)	"Power in the stockholders to call meetings, in the event the regularly constituted officers fail to do so, is usually provided by statute (at p.	Where corporate legislation requires that there be an annual shareholder meeting (e.g. DGCL § 211(b); 805 Ill. Comp. State. 5/7.05; Model Act § 7.01)

251 *Supra* notes 189-92 and related discussion.

252 *Supra* notes 179-82 and accompanying text.

253 See Delaware General Corporation Law §124(1); 805 Ill. Comp. State. 5/3.15; Model Business Corporations Act § 3.04(b)(1); COX & HAZEN, *supra* note 7, § 4.8. With the rise of general incorporation laws and broad corporate purpose clauses, ultra vires was largely a vestigial doctrine by the 1920s. *See* HERBERT HOVENKAMP, ENTERPRISE AND AMERICAN LAW 1836-1937, 60-62 (1991).

254 Procedurally amending the articles required the directors to submit a proposal to the shareholders. See SMITH-HURD, ILLINOIS REVISED STATUTES 1929, chapter 32, § 62; 1915 Revised Statutes of the State of Delaware, ch. 65 1940 §26.

Electronic copy available at: https://ssrn.com/abstract=2595693

	200)."	individual shareholders have the right to demand that an annual meeting be held.[255]
Power to dissolve (#4)	"Stockholders, usually by a two-thirds vote at a meeting…may dissolve the corporation….(at p. 200-1)."[256]	"Every state provides for the voluntary dissolution of a corporation when authorized by a vote of the shareholders."[257] See, for example, DGCL § 275; 805 Ill. Comp. State. 5/12.15; Model Act § 14.02.
Right to assets on dissolution (#5)	"After the payment of corporate debts, the stockholder becomes entitled to his proportionate share of the assets of the company (at p. 201)."	A key duty of directors during the winding up process for a corporation is "to distribute the remaining assets to the shareholders after provision has been made for creditors."[258]
Right to sell stock (#6)	"The right of alienation is an inseparable incident to the ownership of stock as it is of other property (at p. 201)."	"In publicly held corporations, free alienation of shares is a distinct advantage of the corporate form of doing business."[259]
Right to vote (#7)	"The stockholder is normally entitled to one vote for each share of stock….(at p. 201)."	"Generally…each outstanding share of stock is entitled to one vote…."[260]
Right to dividends (#9)	"A well-known law writer [I.M. Wormser, footnote omitted] believes that where it appears that dividends have erroneously and unfairly been detained from distribution to the stockholders for a long period of years, a point will be reached where a court of equity should unhesitatingly intervene….(at p. 134)."	With dividends, "[t]he shareholders are usually entitled to the amounts credited to them….In most cases where dividends have been compelled, it has been shown that the directors wilfully abused their discretion….."[261]
Defend suits on behalf of the corporation (#13)	If the board's power to defend suits that have been brought against the corporation is "fraudulently neglected, a stockholder might conceivably act on behalf of and in defense of the corporation (at p. 202)"	"…refusal to defend (by the board), where it partakes more of disregard of duty than of an error of judgment, or is a breach of trust although not involving intentional moral delinquency, warrants relief to complaining shareholders."[262]

255 COX & HAZEN, *supra* note 7, § 13.13.

256 At the time of publication of Sears' book the procedure for the dissolution of a corporation in both Illinois and Delaware called for the board to present a dissolution proposal to their shareholders. The proposal, however, could be made at the request of shareholders. See 1929 Illinois Revised Statutes 32 § 75; 1915 Revised Code of Delaware, 1953, § 39.

257 COX & HAZEN, *supra* note 7, § 26.2.

258 *Id*. § 26.13.

259 *Id*. § 1.5.

260 ROBERT C. CLARK, CORPORATE LAW 361 (1986).

261 COX & HAZEN, *supra* note 7, §§ 20.1, 20.2.

262 12B FLETCHER CYC. CORP. § 5853 (2013).

Electronic copy available at: https://ssrn.com/abstract=2595693

Remedy against misconduct by majority shareholders (#14)	"A *bona fide* minority stockholder who has not…ratified fraudulent acts of the majority…may sue and will be given appropriate remedies against an offending majority….(at p. 202)."	"In broad overview, transactions shown to produce disproportionate gains to the controlling stockholders are typically judged by a standard of fairness….(T)he burden of establishing the fairness of the transaction is placed upon the controlling stockholder…."[263]

C. What Shareholder Protections Were Displaced?

While the ADRI, ASDI and CBR SPI scores for Delaware, Illinois and the Model Act imply that there was only a modest erosion of protection afforded to shareholders under state corporate law from 1899 onwards, and while the shareholder rights identified as important by Sears in 1929 remain largely intact today, the literature across the decades abounds with claims that changes to state law did markedly compromise shareholder rights. Perhaps, then, neither our leximetric investigation nor our historical cross-check using Sears' 14-point list has captured fully what in fact was a prevalent trend in U.S. corporate law. Correspondingly, we identify now changes to the law emphasized by those saying shareholder protection afforded by state law diminished considerably and assess whether the changes in question were of sufficient importance to undermine our ADRI, ASDI and CBR SPI findings.

Throughout the 20th century there were numerous assertions that competition by states was placing shareholder rights in jeopardy. In 1929 Adolf Berle, subsequently co-author of *The Modern Corporation and Private Property*, said that unless managerial power was subject to equitable control by the courts "the interest of anyone who purchases or contracts in respect of shares of a Delaware corporation is so hazardous from a legal point of view that no well informed person would care to run the risk."[264] John Flynn, in a 1930 *Atlantic Monthly* article explaining "Why Corporations Leave Home" for Delaware, said the state's

263 COX & HAZEN, *supra* note 7, § 11.11.

264 A.A. Berle, *Investors and the Revised Delaware Corporation Act*, 29 COLUM. L. REV. 563, 581 (1929).

Electronic copy available at: https://ssrn.com/abstract=2595693

laws were liberal "to the point of glaring laxity."[265] Wiley Rutledge observed in 1937 that numerous states were following "the lead of Delaware," meaning

> "The individual shareholder now has largely a 'pig-in-a-poke.' His old vested rights are gone or are going. He is made more dependent with each new statute upon the desires of the management…."[266]

Ernest Folk, who played a leading role in the revision of Delaware corporate law that led to the enactment of the Delaware General Corporation Law of 1967, said in 1968 of the approach taken "We do not seek to protect shareholders, creditors or others; rather we limit their rights and remedies. We constantly enlarge the rights and freedom of management."[267] Finally, William Cary, in a landmark 1974 article on regulatory competition's impact on corporate law, indicated that the "race for the bottom" had "watered the rights of shareholders vis-à-vis management to a thin gruel."[268]

What forms of shareholder protection were abrogated or compromised to elicit such forceful rhetoric? There were throughout the 20th century various changes to the law both in Delaware and elsewhere that bolstered managerial freedom of action. Did these compromise shareholder rights in the profound manner implied by the "race" rhetoric used in relation to regulatory competition by states? An analysis of major changes in state corporation law across the century suggests not.

---

265 John T. Flynn, *Why Corporations Leave Home*, ATLANTIC MONTHLY, Sept., 1932, 268, 272.

266 Wiley B. Rutledge, *Significant Trends in Modern Corporation Statutes*, 22 WASH. U.LQ. 305, 337 (1937).

267 Ernest L. Folk, *Some Reflections of a Corporation Law Draftsman*, 42 CONN. B.J. 409, 415 (1968). On Folk's role in the lawmaking process, see Comment, *Law for Sale: A Study of the Delaware Corporation Law of 1967*, 117 U. PA. L. REV. 861, 865-68 (1969) [hereinafter Comment, *Law for Sale*].

268 Cary, *supra* note 11, at 666.

Electronic copy available at: https://ssrn.com/abstract=2595693

Within two years of Delaware's 1899 enactment of a new general incorporation statute designed to attract incorporation business,[269] Delaware was revising the legislation to enhance managerial flexibility, adding a new section permitting a corporation's certificate of incorporation to contain any provision not demonstrably in violation of the statute.[270] The process continued in 1917, when directors of a Delaware corporation were explicitly authorized to sell all or substantially all of the corporation's assets so long as such action had been approved on a majority vote by the shareholders.[271] Also, following a precedent set by New York in 1912,[272] in 1917 Delaware allowed corporations to issue shares with no par value.[273] Berle claimed in 1928 that the institution of no-par stock probably was "the greatest single step in transferring control of property rights from stockholders to corporate managements…."[274] This change to the law did theoretically make it easier for directors to benefit favored investors inappropriately by issuing new shares cheaply.[275] Still, the salutary flexibility of no par value shares quickly became apparent,[276] and by the time the 20th century drew to a close par value was an anachronism.[277]

---

269 *Supra* note 60 and related discussion.

270 S. Samuel Arsht, *A History of Delaware Corporation Law*, 1 DEL. J. CORP. L. 1, 9 (1976) (discussing Act of March 7, 1901, ch. 167, § 5).

271 *Id*. at 10 (discussing Act of April 9, 1917, ch. 114, § 20 and indicating the amendment was made in response to a court decision throwing doubt on whether a company could sell all of its assets with less than unanimous shareholder approval).

272 Wells, *Modernization*, *supra* note 65, at 606.

273 Del. Laws 1917, c. 113, § 3.

274 ADOLF A. BERLE, STUDIES IN THE LAW OF CORPORATION FINANCE 64 (1928).

275 For an overview of the perceived risks created by the creation on non-par stock, see Wells, *Modernization*, *supra* note 65, 607.

276 See, for example, BALLANTINE, *supra* note 212, at 473 ("The great feature of no-par shares is price flexibility….").

277 Venture Stores, Inc. v. Ryan 678 N.E. 2d 300, 303 (Ill. Ct. App., 1997); see also COX & HAZEN, *supra* note 7, § 16.15 ("'Par value' is a rapidly vanishing feature of corporate law.") *Cf*. BAYLESS MANNING AND JAMES J. HANKS, LEGAL CAPITAL 30 (3rd ed., 1990) (…par stock continues to be in majority use.")

Electronic copy available at: https://ssrn.com/abstract=2595693

Otherwise, few amendments were made to Delaware's corporation statute until the late 1920s, when major changes were made to provisions governing corporation finance.[278] Delaware corporations were at this point in time explicitly authorized to issue stock options and to create large blocks of authorized but unissued "blank stock" for which managers could tailor the rights and preferences to meet market conditions at the time of issuance.[279] Berle characterized these and related changes to the Delaware legislation as "dangerous" and "unworkable".[280] Stock options, however, were already popular by the time Delaware changed its rules and within a few decades blank stock provisions were commonplace in corporate laws.[281]

The 1933 Illinois Business Corporations Act, befitting a statutory measure that was supposed to protect shareholders from ongoing abuses,[282] did not bolster managerial discretion or erode shareholder rights dramatically as compared with other legislation of the time. For instance, the 1933 Illinois Act preserved pre-emptive rights even though the California General Corporation Law of 1931 had set a precedent for abolition of such rights.[283] The Illinois Act likewise retained mandatory cumulative voting even though Delaware never went further than authorizing companies to "opt in" to this method of director selection in 1919.[284] Similarly, while Delaware explicitly authorized the issuance of stock options in the 1920s, the 1933 Illinois Act did not do so and also provided directors

---

278 Arsht, *supra* note 270, at 11.

279 *Id*.; Berle, *supra* note 264, at 565-73 (discussing Act of March 2, 1927, ch. 85; Act of March 22, 1929, ch. 135, § 6).

280 Berle, *supra* note 264, at 579.

281 On stock options, see John C. Baker, *Stock Options for Executives*, HARV. BUS. REV., Sept. 1940, 106, 106 (indicating that stock options "became exceedingly popular in the 1920s"). On blank stock, see E.R. Latty, *Some General Observations on the New Business Corporation Law of New York*, 11 BUFFALO L. REV. 591, 597 (1962).

282 *Supra* note 65 and related discussion.

283 Ballantine, *supra* note 216, at 362-63.

284 *Supra* note 187 and related discussion; Illinois Business Corporations Act 1933, § 28.

Electronic copy available at: https://ssrn.com/abstract=2595693

with less scope to carry out share buy-backs and declare dividends than Delaware was offering.[285] Illinois then refrained from revising its incorporation statute substantially until the enactment of the Illinois Business Corporations Act of 1983.[286]

Delaware periodically tweaked its corporate law statute between 1929 and 1967 but did not disturb the basic structure of the legislation until concerns arose in the mid-1960s that its dominant position might be under threat from other states seeking to compete for incorporations by changing their laws to "out-Delaware Delaware."[287] Delaware enacted a revised statute in 1967 referred to by one critic as "a modern round of state charter-mongering" [288] and by another as "a prime exemplar of the trend away from shareholder control."[289] Whether such forceful rhetoric was justified is doubtful. We have already considered some changes made by the 1967 legislation, these being the displacement of the presumptive rule concerning the existence of pre-emptive rights and, in the related party transaction context, the deeming by statute of approval by informed, disinterested directors as having the same insulating effect as a good faith shareholder vote.[290] Other changes cited by commentators arguing the 1967 Act diluted shareholder rights substantially were hardly radical, as the amendments cited compromised in some respects the scope for appraisal rights

---

285 Ballantine, *supra* note 216, at 363, 365, 369.

286 Van Vliet, *supra* note 198, 2-3.

287 Arsht, *supra* note 270, at 11; Joel Seligman, *A Brief History of Delaware's General Corporation Law*, 1 DEL. J. CORP. L. 249, 279-82 (1976) (quoting "out Delaware Delaware" from Tom Downs, *Michigan to Have a New Corporation Code*, 18 WAYNE L. REV. 913, 914 (1972)).

288 Seligman, *supra* note 287, at 279.

289 Comment, *Vestiges of Shareholder Rights Under the New Delaware Corporation Law*, 57 GEO. L.J. 599, 599 (1969) [hereinafter Comment, *Vestiges*].

290 On pre-emptive rights, see *supra* note 192 and related discussion. On Delaware's safe harbor provision, see *supra* note 155 and related discussion; Cheffins, Bank, and Wells, *Law by Numbers*, *supra* note 26, at 1760.

Electronic copy available at: https://ssrn.com/abstract=2595693

in companies registered on a national stock exchange or having more than 2,000 shareholders[291] and empowered corporations to purchase directors' and officers' insurance.[292]

Delaware has not engaged in a wholesale revision of its corporation statute since 1967. In the ensuing decades, the 1986 enactment of § 102(b)(7) of the Delaware General Corporation Law has been the manager-friendly change to Delaware law that has attracted the most attention.[293] This provision, which authorizes Delaware corporations to include a provision in their certificates of incorporation that limits or eliminates for directors personal liability arising from breaches of the duty of care, was enacted in response to concerns that honest directors were exposed to a substantial and unjustified risk of having to pay damages out of their own pocket and that the cost of directors' and officers' insurance was escalating counterproductively.[294] Given that the substantive content of directors' duties is not addressed in a general way by the ADRI, the ASDI or the CBR SPI, this change to the law would not have been captured by these indices.

One other area where the ADRI, ASDI and CBR SPI might not capture significant changes in shareholder protection concerns states' antitakeover statutes. Following an unprecedented burst of hostile takeover activity in the 1980s, a majority of states adopted statutes that empowered boards to impede unwelcome takeover bids by, for instance, allowing boards to take into account "other constituents" beyond shareholders in making

---

[291] Comment, *Law for Sale*, *supra* note 267, at 872-73; Comment, *Vestiges*, *supra* note 289, at 608-9; see now Del. Code Ann., tit. 8, § 262(b)(1). These commentators used sweeping language to characterize the change ("effectively eliminate appraisal rights": Comment, *Law for Sale*, supra note 267, at 873; "abolition": Comment, *Vestiges*, *supra* note 289, at 609). In so doing they glossed over the fact that appraisal rights were preserved in a stock-for-stock merger: Del. Code Ann., tit. 8, § 262(b)(2).

[292] Comment, *Law for Sale*, *supra* note 267, at 884-85; Comment, *Vestiges*, *supra* note 289, at 603.

[293] Brown, *supra* note 11, at 331-32 (treating the provision as manager-friendly); Edward P. Welch and Robert S. Saunders, *Freedom and its Limits in the Delaware General Corporation Law*, 33 DEL. J. CORP. L. 845, 854 (2008) ("the most significant post-1967 amendment").

[294] James L. Griffith, *Director Oversight Liability: Twenty-First Century Standards and Legislative Controls on Liability*, 20 DEL. J. CORP. L. 653, 688 (1995); Stephen A. Radin, *"Smith v. Van Gorkom" on its 15th Anniversary*, DIRECTORS & BOARDS, Spring 2000, 24, 27.

Electronic copy available at: https://ssrn.com/abstract=2595693

business decisions and removing for a period of time would-be acquirors' voting rights.[295] Anti-takeover statutes seemingly reduced shareholder value.[296] The indices deployed here therefore may have missed an area where shareholder protection was significantly weakened over time. On the other hand, the anti-takeover measures adopted in the 1980s arguably did not mark a fundamental departure from historical trends but rather merely confirmed that boards had substantial discretion to thwart takeover attempts. In Delaware, for instance—admittedly a state which belatedly adopted a relatively weak antitakeover statute and one where takeover law was largely made by the courts—takeover doctrine developed during the 1980s may ultimately have circumscribed rather than enhanced board discretion.[297]

The foregoing synopsis indicates that while some significant shareholder protections were eroded from 1900 onwards, the changes were not dramatic compared to changes to the legal rules we have already taken into account by way of our historical analysis of the ADRI, the ASDI, the CBR SPI and Sears' 14-point list. Correspondingly, while amendments to state law may have diminished shareholder protection to some degree, at least from 1900 onwards the "race" terminology applied to trends concerning state corporate law is somewhat hyperbolic.

It is possible that focusing on changes to the law occurring in the 20th century may in fact not be the appropriate way to ascertain why there was a general consensus that

---

295 For summaries of these laws, see Subramanian, *supra* note 65, 1828; Michal Barzuza, *The State of State Antitakeover Law*, 95 VA. L. REV. 1973, 2040-42 (2009).

296 *See, e.g*., Subramanian, *supra* note 65, at 1800 ("Econometric analysis of these statutes consistently find that they reduce shareholder wealth"); Lucian Bebchuk, Alma Cohen, and Allan Ferrell, *Does the Evidence Favor State Competition in Corporate Law?* 90 CAL. L. REV. 1777, 1801 (2002) ("a typical antitakeover statute has a negative, albeit modest effect on shareholder value….").

297 Compare, e.g., *Cheff v. Mathes*, 199 A.2d 548, 556 (Del. 1964) (effectively applying the business judgment rule in the context of takeover defenses) with *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946, 955-56 (Del. 1985) (applying a more searching two-prong test for evaluating board use of defensive tactics to fend off an unwelcome takeover bid); *see also* COX & HAZEN, *supra* note 7, § 23.6. "First generation" takeover statutes states adopted prior to the 1980s may have provided protection against takeovers exceeding that available previously but these measures typically failed to pass constitutional muster. See Edgar v. MITE Corp. 457 U.S. 624 (1982); Ahdieh, *Trapped*, supra note 9, at 300 ("Enthusiasts of federalism . . . have pointed to reduction in the levels of resistance condoned by successive generations of state antitakeover statutes").

Electronic copy available at: https://ssrn.com/abstract=2595693

competition between states for incorporation business had caused a substantial erosion of shareholder rights. This is because affirmative statutory shareholder protection may never have been a prominent feature of 20th century state corporate law. The two pivotal themes in the New Jersey corporation law of 1896—from which Delaware's 1899 statute was derived—were to remove limits formerly imposed on corporations and to increase dramatically the scope that those incorporating and acting as directors of companies had, relative to shareholders, to dictate the internal structure and operation of corporations.[298] As far back as 1899, then, Delaware's general incorporation statute failed to specify in any systematic way the responsibilities of management to shareholders or afford substantial rights and remedies to dissident shareholders.[299] Correspondingly, the "race" that has ostensibly characterized the development of shareholder protections under state corporate law in the United States may well have been largely over just as it started.

This revised characterization of the chronology of state corporate law is not novel. Bill Bratton and Joe McCahery have said "Legislative innovation at the state level never again reached the intensity experienced in the wake of New Jersey's competitive initiative."[300] They have observed similarly that "the structure of state [corporate] law showed remarkable stability between 1896 and the takeover wars of the 1980s, and that structure was determined in a manifestly competitive environment," referring with respect to the 1980s to the introduction of anti-takeover legislation in that decade.[301] William Cary has similarly suggested that that Delaware had a "modern and 'liberal' act" by 1915.[302]

---

298 Wells, *Modernization*, *supra* note 65, at 584.

299 Kenneth K. Luce, *Trends in Modern Corporation Legislation*, 50 MICH. L. REV. 1291, 1298 (1952); Arsht, supra note 270, at 8 ("…the 1899 Act was largely silent with respect to the standards to be adhered to by officers and directors in the performance of their duties….)"

300 Bratton and McCahery, *Equilibrium*, *supra* note 105, at 631.

301 *Id.* at 646.

302 Cary, *supra* note 11, at 665.

Electronic copy available at: https://ssrn.com/abstract=2595693

These observations accord with our ADRI, ASDI and CBR SPI findings, at least with respect to state law – there was no dramatic erosion of shareholder rights during the period we focus on. Some statutory amendments occurring in the 20th century did elicit strong reactions. Nevertheless, Bratton and McCahery's characterization of 20th century rounds of innovation as "minor adjustments to a stable legal regime"[303] appears to be on the mark. As our shareholder protection indices indicate, changes to state law did not fundamentally compromise shareholder rights after 1899.

If a substantial erosion of shareholder protection in fact was not a hallmark of state corporate law in the United States from 1899 onwards, was there ever a robust race to the bottom? To the extent it did happen, the closing decades of the 19th century stand out as the crucial period. It has been said that "American corporate law lost a substantial part of its regulatory content from the 1880s"[304] and that "the position of minority shareholders if anything became weaker" as the 19th century drew to a close.[305] We leave it to others to verify by way of leximetrics and otherwise these claims. From 1899 onwards, however, general trends concerning state corporate law in the United States appear to accord with our empirical findings that a "race" did not compromise fundamentally shareholder rights under state corporate law.

V. CONCLUSION

The general consensus is that U.S. law does not offer shareholder protection that is as robust as it is in comparable countries. To the extent this is the case, the pattern can be attributed most obviously to a central and distinctive feature of U.S. corporate law, namely

303 Bratton and McCahery, *Equilibrium*, *supra* note 105, at 635.

304 P.M. Vasudev, *Corporate Law and Its Efficiency: A Review of History*, 50 AM. J. LEGAL HIST. 237, 260 (2008-10).

305 Naomi Lamoreaux, *Scylla or Charybdis? Historical Reflections on Two Basic Problems of Corporate Governance*, 83 BUS. HIST. REV. 9, 21 (2009).

Electronic copy available at: https://ssrn.com/abstract=2595693

competition between states for incorporation business stemming from the ability of corporations to be incorporated under the law of a state different from the one in which they are headquartered. While there has been acrimonious debate whether competition between states has produced a legal regime disproportionately disempowering shareholders to managers' benefit (and so been a "race to the bottom"), or instead has prodded states to develop corporate law that enhances shareholder wealth (and so been a "race to the top") there has been general agreement that shareholder rights have diminished over time. This Article has deployed empirical analysis to discern how shareholder protection has evolved over time and casts doubt on this received wisdom. In so doing, it has made three major contributions to the literature on corporate law and shareholder protection.

First, our Article presents a fresh way to track quantitatively the development of U.S. corporation law over time. Using indices originally developed to compare shareholder protections across nations, the Article charts the development of three vital bodies of U.S. corporate law, those of Delaware, Illinois and the Model Business Corporation Act, since the turn of the twentieth century. The nature of our findings suggests quantitative analysis of the development of corporate law over time could be deployed effectively to generate insights in other contexts.

Second, the Article has used quantitative analysis to cast new light on the nature of jurisdictional competition between states. Our deployment of leximetric analysis indicates, for instance, there has been erosion of shareholder protections offered by state law over the past century. This erosion was generally modest, however, suggesting that if there was a meaningful race to the bottom (or top), it did not occur from 1900 onwards.

The Article's third and final significant contribution has been to put into context the federal role in affording protection to shareholders. We demonstrate quantitatively that federally-oriented reform has bolstered considerably shareholder rights over time and indeed

Electronic copy available at: https://ssrn.com/abstract=2595693

has more than off-set whatever diminution occurred due to state law changes. Today's shareholders, at least those in public corporations, are better protected by the U.S.'s amalgam of state and federal "corporation law" (including stock exchange listing rules) than were shareholders of a century or even a half-century ago. Our study correspondingly shows that there has not been a steady erosion of shareholder rights in the period under scrutiny, at least once the significant effect of federal interventions is taken into account. Moreover, the level of protection shareholders currently enjoy is reasonably high by global standards.

We leave open for present purposes the normative implications of the trends we have identified. This is because assessing the desirability of shareholder protection is anything but straightforward. While this Article indicates that shareholders were offered greater protection overall over time, it is possible the costs of such additional protection may have outweighed the benefits. Views expressed by those in the "race to the top" camp illustrate the point. Given that the "race to the bottom" with state corporate law presupposes a sacrificing of shareholder rights to cater to managers desiring increased flexibility, it might seem to follow that a "race to the top" would imply fortification of shareholder rights. To the extent that this is correct, race to the top advocates seemingly should have welcomed the federal interventions that pushed upwards scores in our ASDI and CBR SPI. Their reaction in fact was largely the opposite.[306] What they admire about state corporate law, and dislike about federal corporate law, relates to choice rather than content. As Frank Easterbrook has observed "States can't harm investors...—if they make bad laws, capital migrates

[306] See, for example, Roberta Romano, *The Sarbanes-Oxley Act and the Making of Quack Corporate Governance*, 114 YALE L.J. 1521, 1529-43 (2005) (canvassing the empirical evidence relating to four key changes SOX made). Larry E. Ribstein, *Markets vs. Regulatory Responses to Corporate Fraud: A Critique of the Sarbanes-Oxley Act of 2002*, 28 J. CORP. L. 1, 11-18 (critiquing key SOX provisions), 57-61 (advocating state-led corporate law) (2002).

Electronic copy available at: https://ssrn.com/abstract=2595693

elsewhere…If Congress makes a mistake, it is not automatically undercut by market forces."[307]

The ADRI, ASDI and CBR SPI do not purport to measure regulatory style. Instead, the focus is on the presence or absence of rules that can offer protection to shareholders. Correspondingly, our historically-oriented leximetric analysis does not provide an appropriate basis for evaluating whether the sort of race that race to the top advocates favor has been a dominant feature of U.S. corporate law over time. More broadly, we leave it to others to assess the normative implications of our findings. What we have done is provide a richer understanding of trends relating to shareholder protection that should provide an improved foundation for policy analysis.

[307] Frank H. Easterbrook, *The Race for the Bottom in Corporate Governance*, 95 VA. L. REV. 685, 698 (2009). See also Romano, *Regulatory Competition*, *supra* note 19, at 216; Daniel R. Fischel, *The "Race to the Bottom" Revisited: Reflections on Recent Developments in Delaware's Corporation Law*, 76 NW. U. L. REV. 913, 921-22 (1982).

Electronic copy available at: https://ssrn.com/abstract=2595693