Lost in Translation: From U.S. Corporate Charter Competition to Issuer Choice in International Securities Regulation

Frederick Tung
LOST IN TRANSLATION: FROM U.S. CORPORATE CHARTER COMPETITION TO ISSUER CHOICE IN INTERNATIONAL SECURITIES REGULATION

Frederick Tung*

I. INTRODUCTION ........................................527

II. THE DELAWARE STORY AND ISSUER CHOICE ............536
    A. THE DOMINANT PARADIGM ................................537
    B. FROM U.S. CHARTER COMPETITION TO INTERNATIONAL
       ISSUER CHOICE ........................................539

III. CHOICE OF LAW FOR U.S. CHARTER COMPETITION:
     ORIGINS OF THE INTERNAL AFFAIRS DOCTRINE ..........542
    A. OVERVIEW ...........................................543
    B. ORIGINS: LOCAL FIRMS AND THE IDEOLOGY OF
       TERRITORIAL SOVEREIGNTY ...............................545
    C. INDUSTRIALIZATION, INTERSTATE FIRMS, AND THE
       INTERNAL AFFAIRS DOCTRINE ............................549
    D. THE GREAT MERGER MOVEMENT AND CORPORATE LAW .552
    E. THE POLITICAL ECONOMY OF THE INTERNAL
       AFFAIRS DOCTRINE .......................................556

IV. CHOICE OF LAW IN INTERNATIONAL SECURITIES REGULATION:
    TERRITORIALITY AND ITS PERSISTENCE ..................561
    A. THERE'S NO PLACE LIKE HOME ..........................561

* Professor of Law and Dean's Fellow, Loyola Law School (Los Angeles). A.B. 1983, Cornell University; J.D. 1987, Harvard Law School. Web: http://www.lls.edu/academics/faculty/tung.html; e-mail: Fred.Tung@lls.edu. For helpful comments and conversation, thanks to Bernie Black, Steve Choi, Jim Cox, Jill Fisch, Katie Pratt, and workshop participants at the American Law and Economics Association 2003 Annual Meeting, the Law and Society Association 2004 Annual Meeting, and Loyola Law School.
526 GEORGIA LAW REVIEW [Vol. 39:525

B. INTEREST GROUPS AND THE PERSISTENCE OF TERRITORIAL MONOPOLY .......................... 566
   1. Regulators and Regulatory Price Discrimination ........................................ 567
   2. Other Interest Groups: Path Dependence and Increasing Returns ..................... 573
      a. Learning Effects ......................................................................................... 575
      b. Coordination Effects .................................................................................. 578

V. THE GLOBAL MARKET FOR SECURITIES LAW .............................................. 581
   A. THE DEARTH OF COMPETITORS ................................................................. 582
   B. THE IMPORTANCE OF COMMITMENT ......................................................... 584
   C. ESTABLISHED CAPITAL MARKET COUNTRIES .......................................... 587
      1. Regulators' Constraints ............................................................................. 588
      2. Victims of Prosperity .................................................................................. 589
      3. Private Interests and Political Equilibrium ............................................... 592
   D. CAPACITY VS. COMMITMENT: PROBLEMS FOR SMALLER NATIONS ............ 598
      1. Regulatory Infrastructure Investments ....................................................... 600
      2. Credible Commitment and World Market Share ........................................... 603
      3. Size Does Matter ......................................................................................... 608
      4. Rivals' Strategic Behavior .......................................................................... 613

VI. ENFORCEMENT ............................................................................................. 616
   A. MIX AND MATCH TRANSNATIONAL ENFORCEMENT ........................................ 616
   B. ENFORCEMENT OF CORPORATE LAW IN THE U.S. BY CONTRAST ............ 618

VII. STAYING HOME .......................................................................................... 620
   A. INSTITUTIONAL COMPLEMENTARITIES AND MISMATCHES .......................... 621
   B. AGENCY ISSUES ............................................................................................ 624

VIII. CONCLUSION .............................................................................................. 625
I. INTRODUCTION

Corporate charter competition among U.S. states has been held out as a model of welfare-enhancing regulatory competition. Proponents of this story also rely on it as a basis for promoting regulatory competition in international securities regulation. These "issuer choice" proponents argue that an issuer of securities should be permitted to choose the securities regulation of any nation to govern its securities offerings and trading worldwide. This Article challenges the notion that the claimed success of corporate charter competition among U.S. states argues in favor of international issuer choice.

Corporate law is obsessed with Delaware. Delaware, Delaware, Delaware. Most commentators hold Delaware out as the model competitor in a successful, admirable, welfare-enhancing system of regulatory competition. Yet others decry Delaware as a rogue state, leading a race to laxity in corporate law. And finally, a third strand of commentary doubts that much if any competition over corporate law occurs at all. Across all three perspectives, despite their differences, a central task is to explain Delaware—how it came to be the leading incorporation state for public companies by a wide margin.

Make no mistake, the "good" competition story dominates corporate law scholarship, as successive bursts of insight have refined the model both theoretically and empirically. Like all successful models, this model shows a healthy presumption to

---

2 Id. at 390.
3 See infra note 6 and accompanying text.
4 See infra note 46 and accompanying text.
5 See infra note 47 and accompanying text.
imperialism: What was once merely a small state has become an act, a verb, a process. "Delawarization"—regulatory competition based on the U.S. corporate charter competition paradigm—has been observed, recommended, predicted, and sometimes distinguished in many areas—corporate law in Europe, U.S. and international bankruptcy law, international financial regulation, and environmental law, to name a few. The debate over corporate

---


charter competition has even influenced debate in areas as seemingly far removed as campaign finance and legal ethics. It is not surprising that this imperialism has reached the neighboring turf of securities law. Roberta Romano, long an ardent and articulate Delaware booster, has called for regulatory competition in securities law both within the U.S. and internationally. Domestically, she has proposed that states be allowed to offer competing securities regulatory regimes that firms may choose in lieu of federal law when engaging in securities activities in the United States. Internationally, she has argued that firms should be able to choose any nation’s securities law to govern their securities activities on a global basis. In the name of efficiency, she and other scholars have called for nations to forswear their traditional prescriptive jurisdiction over securities activity within their borders. Instead, each issuer should be free to select any government’s regulatory regime to govern the offering and trading of the issuer’s securities worldwide.

Among many U.S. corporate law scholars, this call for issuer choice seems in the natural order of things. Modeled as it is on the dominant U.S. corporate charter competition paradigm, issuer

12 See H. Geoffrey Moulton, Jr., Federalism and Choice of Law in the Regulation of Legal Ethics, 82 MINN. L. REV. 73, 139 (1997) (suggesting usefulness of federal intervention for legal ethics, in order to avoid race to the bottom as seen in corporate and environmental law).
14 Romano, supra note 1, at 392.
15 Choi & Guzman were perhaps the first to suggest regulatory competition in international securities regulation. In a 1996 Article, they sketched their “portable reciprocity” idea. Stephen J. Choi & Andrew T. Guzman, The Dangerous Extraterritoriality of American Securities Law, 17 NW. J. INT’L L. & BUS. 207, 231 (1996) [hereinafter Choi & Guzman, Dangerous Extraterritoriality]. Later, they elaborated their idea the same year that Romano made her domestic proposal. Stephen J. Choi & Andrew T. Guzman, Portable Reciprocity: Rethinking the International Reach of Securities Regulation, 71 S. CAL. L. REV. 903, 903 (1998) [hereinafter Choi & Guzman, Portable Reciprocity] (proposing that international issuers be allowed to choose their securities law). Choi and Guzman, however, do not embrace the U.S. corporate charter competition model as a basis for their international proposal the way Romano does. Rather than promise a race to the top, Choi and Guzman posit the heterogeneity of issuers, whose diverse needs may best be met by a diversity of regulatory regimes from which to choose. Id. at 923.
16 See generally THOMAS KUHN, THE STRUCTURE OF SCIENTIFIC REVOLUTIONS (1962)
choice seems a logical extension. The debate for the last thirty years over corporate law's race-to-the-top versus race-to-the-bottom is a familiar one, and it is fitting that Romano, a leading race-to-the-top exponent, has called for extension of the perceived benefits of regulatory competition to international securities regulation. Romano expressly relies on the claimed success of U.S. charter competition as an exemplar:

[T]he interests and incentives in the two settings are similar: the object of protection of both regimes is the financial interest of investors, and under competition, investors' preferences will dictate the choice of regulator because insiders who require investment capital will bear the higher capital cost of an investor-unfriendly regime choice.

On this view, the same dynamics that have driven the presumed race to the top in U.S. corporate law can be harnessed to produce optimal securities regulation internationally.

I challenge the notion that the U.S. corporate charter competition model lends support for issuer choice in international securities regulation. Even granting the assumptions of race-to-the-top advocates and accepting the best story for corporate charter competition, that story translates poorly into the context of

(17) See infra note 46 and accompanying text.
(18) Romano, supra note 1, at 493. Romano's international proposal includes a lengthy defense of state charter competition in a section entitled, "The Market for Corporate Law in the United States as a Paradigm for International Securities Regulation." Id.
(19) The charter competition story is in large measure a political economy story. It characterizes the incentives and motivations of political actors as well as private actors and the operation of political markets in describing the signature regulatory competition success story. Similarly for issuer choice, proponents adopt standard public choice assumptions in making their case, positing that regulatory bureaucracies thrive by expanding their reach. In the case of securities regulation, the number and size of firms being regulated and the volume of regulated securities offerings and trading are regulators' maximands. In a world of private choice of securities law, regulators would be forced to supply optimal regulation to meet the demands of issuers and investors. Otherwise, regulators risk becoming irrelevant. See infra notes 49-63 and accompanying text.

For purposes of my analysis, I am willing to accept these assumptions. This economic approach to theorizing about bureaucracy is hardly without controversy. See James Q.
international securities regulation. Reliance on that story glosses over important differences in political economy as between U.S. states in a federal system and independent nations in an anarchic global environment. These differences make the charter competition model inapposite. I pursue this argument along two major lines. The first involves choice of law coordination. While U.S. states have been able to coordinate around the internal affairs doctrine for choice of corporate law, no similar rule exists in international securities regulation, where the basic rule is territoriality. The internal affairs doctrine among U.S. states emerged from historical conditions and political dynamics that do not exist among nations. I argue that international choice of law coordination for issuer choice is unlikely.

Second, even setting aside the choice of law problem, and assuming that such international coordination were possible, there is another problem with relying on the Delaware model. On the basis of the Delaware success story, few if any nations would seem to have both sufficient incentive and sufficient capacity to compete over securities law. Corporate charter competition among states is said to be driven by legislators' pursuit of revenues from the sale of corporate charters, and Delaware's peculiar success is said to derive from its fiscal dependence on its corporate chartering revenues. This dependence makes Delaware a "hostage" to its success, enabling it to demonstrate a credible commitment to maintaining efficient and responsive corporate law. For established capital market countries in an issuer choice world, regulatory revenues

Wilson, The Politics of Regulation, in The Politics of Regulation 357, 358 (James Q. Wilson ed., 1980) (assessing explanatory power of economic theory of regulation). However, I allow these basic premises for purposes of discussion. In addition, I leave unchallenged the demand-side story of regulatory competition advocates—that firm managers are adequately constrained by market forces such that they will choose law that maximizes firm value and investor returns. See infra notes 41-48 and accompanying text.

The internal affairs doctrine selects the law of the firm's state of incorporation for disputes over corporate internal affairs. See infra note 64 and accompanying text.

Frederick Tung, From Monopolists to Markets: A Political Economy of Issuer Choice in International Securities Regulation, 2002 Wis. L. Rev. 1363, 1371 (explaining nations' territorial application of securities laws).

Throughout this Article, I refer to the Delaware model as shorthand for the race-to-the-top story, the story of good regulatory competition for corporate charters among U.S. states.

See infra note 43 and accompanying text.
would likely be too small to attract legislators' interest. In addition, the small stakes would make it very difficult for such countries to demonstrate the fiscal dependence on regulatory revenues that is critical for credible commitment. All but the smallest nations would have difficulty showing fiscal dependence. The smallest nations, on the other hand, would not likely possess sufficient legal and regulatory infrastructure to be able to offer sophisticated, internationally competitive securities law. Given this dearth of competitors and lack of competition, as well as enforcement problems that may generate indeterminacy for issuer-selected foreign law, issuers might just stay home. Even given the choice, few if any issuers might be willing to opt out of their home country rules.

Part II of the Article provides background. In it, I describe the dominant race-to-the-top story for U.S. corporate charter competition. I then recount the adaptation of the race-to-the-top story to proposals for international issuer choice.

In Parts III and IV, I address the choice of law problem, contrasting the historical conditions leading to the emergence of the internal affairs doctrine with the current political economy of securities regulation among nations. No less than substantive rules, choice of law rules are likewise a product of interest group influences and historical contingency. A plausible case for issuer choice based on the claimed success of U.S. corporate charter competition would have to explain the emergence of consensus over choice of law rules among competing jurisdictions. It would have to explain why and how nations would switch from the current choice of law rule—territoriality—to a rule respecting private choice. I argue that the requisite choice of law coordination will not emerge.

24 See infra notes 41-63 and accompanying text.
25 See infra notes 41-63 and accompanying text.
26 See infra notes 64-188 and accompanying text.
27 See infra notes 85-115 and accompanying text.
28 See infra notes 49-63 and accompanying text. I use the term "coordination" in a nontechnical sense. The emergence of the internal affairs doctrine among U.S. states may have involved no true coordination or cooperation in the game theoretic sense. Instead, adoption of the rule may have been a strictly dominant strategy for each state. Before the existence of interstate firms, state courts would generally have had difficulty enforcing decrees concerning the internal affairs of foreign corporations. See infra note 90. Concerns for institutional integrity and respect for courts may therefore have driven state courts to refrain from meddling in foreign corporations' internal affairs. By contrast, adoption of an
In Part III, I explain the ideological, political, and economic origins of the internal affairs doctrine and its historical contingency. Corporate law race-to-the-top advocates recognize the significance of the internal affairs doctrine in enabling jurisdictional competition. Ironically, however, that rule emerged at a time when U.S. states enjoyed territorial monopolies over corporate law. All business firms were local firms. Those that incorporated had no choice but to incorporate locally. In that context, the internal affairs doctrine merely confirmed the local regulatory monopoly enjoyed by each state's legislature. Far from enabling competition over corporate law, the internal affairs doctrine—applying the law of the state of incorporation—promoted market sharing among states.

Only later with improved transportation and communication did firms become more mobile with the emergence of interstate markets. This put some pressure on states’ territorial monopolies. However, it was not until the end of the nineteenth century during the great merger movement that New Jersey began to offer corporate charters to firms with no substantive economic ties to the state. Economic pressures caused other states to follow suit, breaking the territorial ties between firms and their incorporating states. State legislatures forsook attempts to restrict the out-of-state activity of local corporations or to impose their own local corporate law on foreign corporations operating locally. Instead, states respected foreign corporations’ chosen corporate law. The internal affairs doctrine, already part of the existing custom among states, came under no pressure for revision. It now facilitated charter competition, though it was never designed for this task.

The political economy of international securities regulation is different, an issue I take up in Part IV. For jurisdictional competition over securities law to develop, national policymakers would have to be willing to forswear their own territorial jurisdiction to prescribe securities laws. They would have to agree that foreign law might govern local activity, and they would have to agree on a choice analogous rule among nations with respect to securities law would seem to require cooperation. See generally JAMES D. MORROW, GAME THEORY FOR POLITICAL SCIENTISTS (1994) (using game theory to discuss cooperation and decisionmaking among nations).

See infra notes 64-115 and accompanying text.

See infra notes 116-88 and accompanying text.
of law rule respecting private choice. Romano and other issuer choice proponents fail to explain how nations might achieve such a choice of law convention. They merely assume that a global rule analogous to the internal affairs doctrine could emerge.

But issuers generally have no exit option in terms of where they issue securities; they cannot avoid issuing securities in their home markets. Home country investors are generally the most receptive investors for their local issuers' securities. National regulators are therefore not forced to compete with one another over securities law with respect to their domestic issuers. Especially in the most important national capital markets, securities regulators enjoy territorial monopolies with respect to securities law, and they play a dominant role in setting domestic policy concerning cross-border securities activity. Following the public choice assumptions of issuer choice proponents, these regulators will oppose competition and choice of law rules enabling firms' easy exit from existing territorial monopolies. Instead, regulators in the most important capital markets maximize private benefits under their existing monopolies through a strategy I call regulatory price discrimination. They augment their regulatory purview by maintaining their existing monopolies over local issuers while at the same time offering lower regulatory burdens to attract foreign issuers. Other important interest groups in major capital markets—lawyers, accountants, underwriters, stock exchanges, and securities firms, among others—also have strong and longstanding stakes in preserving the status quo of territorial monopoly and regulatory price discrimination. Without international choice of law consen-

31 It makes sense to focus on the most important capital markets since regulators, issuers, and investors in those markets are likely to have the most significant influence over the shape of international securities regulation.

32 In other work, I identify important capital markets as regulatory price setting jurisdictions, whose regulators enjoy market power and pursue this regulatory price discrimination strategy. Tung, supra note 21, at 1397. At the opposite extreme is the regulatory price taking jurisdiction, in which regulators may be forced to grant unilateral recognition to the regulatory regimes of particular price setting jurisdictions that might otherwise offer attractive alternative markets for the price taker's indigenous issuers. Id. at 1405-06.

33 See infra notes 135-66 and accompanying text.
sus—that each nation should honor private choice of securities regulation—jurisdictional competition is not possible.

Setting aside the choice of law issue, Part V addresses the other important problem with the Delaware model in promoting issuer choice. Even assuming the choice of law issue could be resolved, vigorous competitors over securities law might be hard to find. For important capital market countries, the revenue incentives that are assumed to motivate U.S. state legislators would be too weak to draw attention from policymakers in those countries.\textsuperscript{34} Relative to the size of their national budgets, the likely amount of regulatory revenues available in a global market for securities law would be minuscule.\textsuperscript{35} By the same token, it would be difficult for these prosperous countries to demonstrate the fiscal dependence on regulatory revenues necessary to show a credible commitment to a program of responsive regulation.

Under plausible assumptions about the size of the international market for securities law, only nations with very small budgets would be able to demonstrate the requisite fiscal dependence. However, these nations would not likely possess the legal or financial expertise or administrative capacity to offer desirable securities law.\textsuperscript{36} In any case, potential upstarts would have to worry about strategic behavior of the dominant capital markets in terms of deterring entry or new investment in regulatory capacity.\textsuperscript{37}

In Part VI, I briefly discuss enforcement problems that would plague issuer choice. The transnational mix and match of legal institutions required to enforce issuer-selected foreign law would be unlikely to generate predictable rules responsive to the needs of issuers and investors.\textsuperscript{38}

In the end, impediments to competition might cause issuers to simply stay home. Even given the choice, they might not be willing to opt out of home country regulation, a question I discuss in Part

\textsuperscript{34} See infra notes 212-16 and accompanying text.

\textsuperscript{35} Perhaps regulators in those nations—seeking to augment the prestige and power of their bureaucracies—might be motivated to compete. But any ostensible commitment to maintain responsive regulation would be subject to legislative fiat and changing political equilibria. See infra notes 209-10 and accompanying text.

\textsuperscript{36} See infra notes 260-61 and accompanying text.

\textsuperscript{37} See infra notes 312-17 and accompanying text.

\textsuperscript{38} See infra notes 318-29 and accompanying text.
Established capital market countries account for the overwhelming majority of the world's issuers and investors by market capitalization.\textsuperscript{39} Especially for these issuers, opting out of home country law would mean transplanting foreign law into a complex and sophisticated set of home country institutional arrangements and organizations that have developed in complementary fashion with home country securities law. Opting out of home country law would forsake significant learning and coordination benefits that have accrued with territorial regulation. Investors might react negatively. Unpredictability from this institutional mixing and matching might cause investors to apply a heavy discount to the securities of issuers who abandon home country regulation. With U.S. corporate charter competition, by contrast, a fairly homogeneous legal and business culture in the United States and the relative similarity of state court systems obviate any similar problems.

Corporate charter competition among U.S. states emerged in a wholly different context from that envisioned in an issuer choice world. In the United States, a federal system with a unique history, the dismantling of trade barriers among states, and shared legal and business cultures all contributed to making corporate law portable across states and to pressuring states to accept this portability. These features do not exist for securities regulation among nations.

\section*{II. The Delaware Story and Issuer Choice}

It is fitting that scholarly discussion of regulatory competition begins with the story of corporate charter competition among U.S. states, the most prominent example of arguably successful—i.e., welfare enhancing—regulatory competition. Corporate charter competition has been actively debated among scholars for several decades. I first describe the dominant race-to-the-top view, which holds that this jurisdictional competition has produced efficient

\textsuperscript{39} See infra notes 330-44 and accompanying text.

\textsuperscript{40} See infra note 208 and accompanying text.
corporate law. I then recount the adaptation of the dominant paradigm for issuer choice.

A. THE DOMINANT PARADIGM

According to the charter competition success story, firm managers' freedom to choose from among the corporation laws of the fifty states and the District of Columbia enables a well-functioning market in corporate law. On the demand side, firm managers are constrained by market forces to seek out corporate law that is best for investors.41 They are constrained by efficient capital and product markets to faithfully pursue investors' interests in choosing corporate law. Investors, who price differences in corporate law, will pay less for shares of firms with inefficient corporate law, so managers will choose efficient rules—those that investors prefer—in order to minimize their firms' costs of capital. Managers might be tempted to benefit themselves at the expense of investors by choosing lax law, but the resulting higher capital costs would place such firms at a competitive disadvantage in product, labor, and capital markets. This might ultimately lead to the demise of such firms and the ouster of their self-seeking managers.42

On the supply side, according to this story, state legislatures compete to offer corporate law that managers and investors desire. Legislatures participate in this competition in order to garner revenues in the form of chartering fees and other fees paid to the state of incorporation. Lawyers in each state also participate in the making of attractive law in the hope that their state's corporation code will garner widespread adoptions, which inures to the lawyers' financial and professional benefit.43

Delaware has dominated the competition, the story goes, because of its relatively heavy investment in and dependence on its chartering business. Because of its small size and relative lack of indigenous industry, Delaware depends significantly on chartering revenues for its state budget. In addition, Delaware offers a

41 See Winter, supra note 6, at 257 (discussing various market influences on managers).
42 Id. at 254-73.
specialized chancery court to hear corporate cases. Not only does this expert court produce better corporate law decisions than other states' generalist courts, but this specialized court has no ready alternative use. Delaware's significant investment in maintaining the court therefore offers firms some comfort that Delaware is in the corporate law business for the long term. This function-specific investment, together with Delaware's budgetary dependence on chartering revenues, serves as a commitment to firms that Delaware will always be responsive to firms' corporate law needs. It will continually update its corporate law as firms' needs may change. It will not behave opportunistically by altering corporate law to extract rents from consumers—those firms that have already incorporated under Delaware law.44

This dominant story has not gone unchallenged. For thirty-odd years, corporate scholars have debated whether corporate charter competition benefits investors45 or only self-serving firm managers.46 The latest challenges to the dominant story argue that competitive pressures on Delaware are very weak or nonexistent and therefore,

---

44 Id. Whether these features of Delaware truly function as commitment devices depends a great deal on one's perception of the costs of reincorporation and the length of the shadow of the future. Romano generally believes that reincorporation is expensive and cumbersome, such that Delaware needs these commitment devices in order to demonstrate to firms that it will not renege—that it will not be tempted to change its laws opportunistically to the detriment of firms that have chosen to incorporate in Delaware. Id. at 44.

Others have suggested that the commitment analysis is not convincing, for two reasons. First, if reincorporation is in fact relatively inexpensive, then Delaware cannot behave opportunistically because firms will simply leave. So the ostensible commitment devices are not necessary and therefore cannot explain Delaware's dominance in the market for corporate charters. See Bernard S. Black, Is Corporate Law Trivial?: A Political and Economic Analysis, 84 NW. U. L. REV. 542, 586-89 (1990) (arguing transaction costs of reincorporation are low). And even if reincorporation were expensive, a state that hoped to remain attractive to firms in the future would still not be able to behave opportunistically toward firms already incorporated there.

45 Classic race-to-the-top works include Frank H. Easterbrook & Daniel R. Fischel, THE ECONOMIC STRUCTURE OF CORPORATE LAW (1991); Fischel, supra note 6; Romano, supra note 6; Winter, supra note 6.

that Delaware has little incentive to offer optimal law to maximize firm value.\textsuperscript{47} Despite the various challenges, race-to-the-top continues to be the dominant view among corporate scholars.\textsuperscript{48}

B. FROM U.S. CHARTER COMPETITION TO INTERNATIONAL ISSUER CHOICE

The basic rationale for issuer choice parallels the rationale behind the corporate law race-to-the-top story. Law is a product; competition among suppliers results in products that better satisfy consumer preferences.\textsuperscript{49} The consumers in the case of corporate and securities laws, of course, are investors and firm managers.

Roberta Romano\textsuperscript{50} and Stephen Choi and Andrew Guzman\textsuperscript{51} have called for a competitive, market-based approach to securities regulation. While distinctive in the details, the central argument in both proposals is that issuers should be allowed to choose the regime of securities regulation under which they will be governed. Under the current territorial approach to securities regulation, issuers and investors wishing to transact in a given market are unavoidably bound by the national securities laws of the jurisdiction in which the market is located.\textsuperscript{52} Within each jurisdiction, the national regula-

\begin{footnotesize}

\textsuperscript{48} "According to the view that appears to dominate the current thinking of corporate law academics, state competition produces a 'race to the top' that benefits shareholders." Bebchuk \& Cohen, \textit{supra} note 47, at 384.

\textsuperscript{49} Romano, \textit{supra} note 6, at 225 (describing rationale behind race-to-the-top theory).

\textsuperscript{50} Romano, \textit{supra} note 13, at 2361; Romano, \textit{supra} note 1, at 388.

\textsuperscript{51} Choi \& Guzman, \textit{Dangerous Extraterritoriality, supra} note 15, at 231; Choi \& Guzman, \textit{Portable Reciprocity, supra} note 15, at 903.

\textsuperscript{52} Cf. Romano, \textit{supra} note 13, at 2149 ("The SEC's territorial approach to jurisdiction prevents foreign issuers who are in compliance with their home states' disclosure require-
tory authority enjoys a monopoly in terms of the regulation it chooses to supply. But that regulatory regime may not be optimal for parties transacting in the particular market.

In addition, regulatory monopolists have insufficient incentive and insufficient information to offer optimal regulation. Unbundling capital markets from the national laws of the jurisdictions in which the markets are located breaks the regulatory monopolies. Issuers and investors left to their own private choices will force regulators to supply optimal regulation upon peril of extinction. Bureaucracies thrive by expanding their reach, the argument goes, and securities regulators will respond to consumer demand in order to expand their regulatory purview. Regulators will wish to maximize the number of firms and the volume of securities offerings and trading they regulate. Individual decisions of issuers in choosing their regulatory regimes also provide market information to regulators, who can respond to consumers by altering regulatory products to maximize adoptions.

Issuer choice proponents are confident that investors will not be disadvantaged by firm managers' regulatory choices, since efficient capital markets can price the regulatory regimes selected. Managers choosing regimes that provide insufficient investor protections—for example, a regime may allow managerial opportunism or require slim or no disclosure—will cause their firms to suffer in the capital markets. Investors will pay less for the securities of those issuers than if a more investor-protective regime had been selected, disadvantaging those issuers relative to their competitors. Because of firm managers' desire to minimize the firm's costs of capital and maximize offering proceeds and postoffer

ments . . . from listing on U.S. stock exchanges.

53 Id. at 2361.
54 See Choi & Guzman, Portable Reciprocity, supra note 15, at 922-24 (detailing advantages of market-based issuer choice approach).
55 Id.
56 Id.
57 Id. This assumption that regulators will attempt to maximize the number of firms and transactions under their regulatory purview is crucial to the issuer choice proposal. It explains why regulators in an issuer choice world would compete to offer popular law. If firms are free to choose their regulation, then the only avenue for regulators to augment the volume of transactions they regulate is by offering regulation that firms and investors prefer.
58 Choi & Guzman, Portable Reciprocity, supra note 15, at 922-24.
trading values, they will, given the choice, select the regulatory regime that is optimal for the firm’s investors. According to Romano, this competition produces corporate law that maximizes firm values and investor returns. Additionally, the same dynamics that have driven this race to the top can be harnessed to produce optimal securities regulation. In Romano’s view, competition over securities regulation will similarly cause regulatory regimes to converge around the rules that issuers and investors want.

The remainder of this Article considers the significant features of the dominant race-to-the-top story for U.S. charter competition and their applicability to international securities regulation and issuer choice. I first consider choice of law. I then turn to other impediments to competition in international securities regulation that are absent from or glossed over in the translation from the U.S. corporate charter competition story.

---

59 Id.
60 Romano, supra note 13, at 2388-95. Romano offers empirical evidence of plausibly market-driven optimal voluntary disclosure that exceeds the level of mandatory disclosure in (a) private debt markets; (b) European listings in the United Kingdom, which comply with U.K. requirements though they could use lower home country standards; and (c) European international-style private institutional offerings, for which disclosure exceeds even the U.K. standard, but is in fact closer to U.S. standards. Id. at 2373-80.
61 Id. at 2388-95; Romano, supra note 1, at 390.
62 Romano, supra note 13, at 2362, 2367.
63 Id. at 2395. Choi and Guzman are less convinced about convergence and are agnostic as to its direction. Instead, they posit the heterogeneity of issuers and investors. Not all issuers are alike, so a regulatory regime that is suitable for one may not be desirable to another. In their view, the beauty of competition is that it generates regulatory diversity, allowing firms to choose from an array of regulatory options and allowing investors a choice as to the regulatory regimes under which they will invest. In this way, heterogeneous issuers and investors are more likely to be matched, thereby eliminating the deadweight losses associated with territorially imposed regulation. Choi & Guzman, Portable Reciprocity, supra note 15, at 914-18.
Under U.S. corporate charter competition, the internal affairs doctrine enables the competition that exists. While each state offers its own corporation law, states generally accept and apply the so-called internal affairs doctrine for their choice of law regarding a corporation's internal affairs—the relations among a firm's shareholders and managers. Under this doctrine, the firm's chosen corporation law will govern its internal affairs, regardless of the location of the firm's headquarters, assets, or personnel, and regardless of where particular transactions occur or particular persons reside. Therefore, a firm may incorporate under the corporation law of any state, and its choice will be respected in other states. According to the dominant paradigm, this common respect for firm choice effectively creates a common market for corporate law.

Moving to the international context, it is understandable that issuer choice proposals might overlook choice of law issues, or simply assume that nations could coordinate around a rule recognizing private choice of securities law. After all, the internal affairs doctrine has generally been the dominant rule in the United States. But no mechanism like the internal affairs doctrine exists for international securities regulation. That consensus on the doctrine could emerge among U.S. states does not imply that a similar choice of law rule and competitive framework could spontaneously develop internationally for securities regulation. The background conditions are dissimilar. The dynamics behind emergence of the internal affairs doctrine are not likely to be replicated in the international context.

64 A handful of states—California and New York most notably—impose their own local requirements on certain foreign corporations as to certain issues. CAL. CORP. CODE § 2115 (West 2001); N.Y. BUS. CORP. LAW §§ 1317-1320 (McKinney 2002).
65 See ROMANO, supra note 43, at 14-51 (arguing that competition for corporate charters among U.S. states has resulted in more efficient corporate law overall).
66 See Deborah A. DeMott, Perspectives on Choice of Law for Corporate Internal Affairs, 48 LAW & CONTEMP. PROBS. 161, 161 (1985) (examining outreach statutes as alternatives to traditional internal affairs doctrine); Elvin R. Latty, Pseudo-Foreign Corporations, 65 YALE L.J. 137, 137 (1955) (cataloguing deviations from internal affairs doctrine).
Unlike corporate law among U.S. states as it currently operates, securities law has always been territorial among nations. Each nation asserts jurisdiction to prescribe rules regarding securities offering and trading within its borders, and no nation allows firms unfettered choice over the law that will govern their securities activities. History matters, and it should hardly be surprising that the different histories for corporate law among U.S. states and for securities law among nations would produce different choice of law rules in the two areas, as well as interest groups with differing stakes in those rules. In nations with important securities markets, the choice of law rule for securities law will preserve existing regulatory monopolies. It will not enable competition.

In this Part, I explain the emergence and persistence of the internal affairs doctrine among U.S. states. In the next Part, I explain why a similar rule is unlikely to emerge for international securities regulation.\(^6\)

A. OVERVIEW

Courts first enunciated the internal affairs doctrine in the 1860s. Courts outside a firm’s state of incorporation refused to entertain disputes over the corporation’s internal affairs, instead deferring jurisdiction in favor of the incorporating state’s courts.\(^6\) This was decades before modern law-as-a-product charter competition emerged at the end of the nineteenth century, however.\(^6\) The context in which the doctrine first emerged was quite different from the environment in which charter competition later developed.

Courts’ early articulation of the internal affairs doctrine recognized that a corporation’s internal disputes implicated the territorial sovereignty of the incorporating state. This state sovereignty notion reflected the historically intimate legal, economic, and geographical ties between the corporation and its incorporating state. Historically, the corporation was literally—not just figuratively—a creation of the legislature of the incorporating state. Each corporation was

\(^{67}\) See infra notes 116-88 and accompanying text.

\(^{68}\) See infra note 79.

\(^{69}\) See infra notes 92-103 and accompanying text.
created by a special act of the legislature, and through the early part of the nineteenth century, corporations were chartered only for public purposes and were viewed as agencies of the incorporating state. As a creature of the sovereign, the corporation was thought to exist only within the territorial borders of the incorporating state. Economically as well, corporations were closely tied to their incorporating states. Before the mid-nineteenth century, all businesses were local businesses. Firms generally had little choice about where to incorporate. A firm that incorporated did so in its home state—where its organizers lived and where its operations were located. Before the mid-nineteenth century, as a practical matter, each state enjoyed a territorial regulatory monopoly over its local corporations.

With advances in transportation and communication around the mid-nineteenth century, interstate firms arose, putting pressure on states' regulatory monopolies. The Commerce Clause assured that states could not erect trade barriers to impede the interstate movement of goods, and with the emerging common market and technological advances, firms enjoyed some geographical mobility. They could move. Given firms' mobility, states were forced to compete to attract businesses to locate in-state. However, they generally maintained requirements concerning corporations' ties to their incorporating states. During this period, courts first enunciated the internal affairs doctrine, deferring to the territorial sovereignty of the incorporating state regarding the internal matters of its corporations.

Only at the end of the nineteenth century did modern law-as-a-product corporate charter competition emerge, at the time of the great merger movement. The century's end saw enormous economic dislocation, as well as corporate law innovations by the New Jersey legislature that led to the demise of mandatory territorial ties between corporations and their incorporating states. Economic

---

70 See infra notes 73-84 and accompanying text.
71 See Welton v. Missouri, 91 U.S. 275, 276 (1876) (striking down discriminatory tax burdens on out-of-state goods); Robbins v. Shelby County Taxing Dist., 120 U.S. 489, 498 (1887) (striking down Tennessee license tax on drummers for out-of-state manufacturers and holding explicitly that "interstate commerce cannot be taxed at all").
72 See infra notes 85-91 and accompanying text.
pressures on state legislatures caused them to forsake attempts to impose their own local corporate law on foreign corporations operating locally. Instead, states respected foreign corporations' chosen corporate law. The internal affairs doctrine, already part of the existing custom among states, came under no pressure for revision, despite the fact that this new context of nonterritorial corporate law differed radically from the context in which the doctrine had first emerged.

That the internal affairs doctrine persisted to play its modern role in facilitating charter competition can largely be explained by reference to institutional inertia and interest group pressures. The doctrine, assuring deference to the incorporating state, carried over from an earlier period of territorial corporate law. Opportunistic adaptation by private interests during the merger movement led New Jersey to offer liberal, nonterritorial corporate law. Economic conditions caused other states' legislatures to value the participation of foreign corporations in their local economies, regardless of these corporations' lack of territorial ties to their incorporating states. Modern corporate charter competition began, and with it, the internal affairs doctrine took on a facilitative role. That the earlier emergence of the internal affairs doctrine later facilitated competition, however, was hardly by design. It was merely the result of fortuitous historical circumstance.

B. ORIGINS: LOCAL FIRMS AND THE IDEOLOGY OF TERRITORIAL SOVEREIGNTY

During the preindustrial period—from the American Revolution to the middle of the nineteenth century—the animating ideas for courts' later articulation of the internal affairs doctrine were formed. Corporations were thought of not only as creatures of their incorporating states, but—at least through the early part of the nineteenth century—they were conceived as agencies of the state. A state's exclusive authority over the internal affairs of its corporations was seen as a matter of state sovereignty.

Before industrialization, businesses were small and predominantly family-run. They transacted primarily in local product, labor, and capital markets and rarely had operations out-of-state.
Most were run as partnerships, and those that incorporated did so in their home states. Foreign corporation questions rarely arose because firms' activities were typically confined to their home states. States were generally assumed to enjoy territorial sovereignty over their domestic corporations.

The conception of the corporation was also very different from its current conception. Incorporation was not generally available to all who applied; instead, corporate charters were granted only sparingly, one-by-one, through special acts of state legislatures. Corporate size and powers were limited, and privileges were sparingly granted. Each act was specifically tailored to the particular project proposed, with powers and privileges specifically defined. Like the other more popular types of corporations of the day—municipal, charitable, ecclesiastical, educational—business corporations were formed to pursue public purposes and were thought of as auxiliary organs of state government. This view of the corporation occasioned practices and associations between the corporation and state government that would be unthinkable today, when the business corporation is viewed primarily as a private organization. Business corporations were typically granted special privileges or delegated government powers thought necessary to the accomplishment of the particular projects undertaken. For example, canal companies typically enjoyed eminent domain powers. States were also often actively involved in the financing or managerial oversight of their corporations, investing state funds and taking board seats.

Given the close relations between state governments and the corporations they created, sovereignty considerations necessitated

73 JOSEPH STANCLIFFE DAVIS, ESSAYS IN THE EARLIER HISTORY OF AMERICAN CORPORATIONS v.2 16-20 (1917).
74 EDWIN MERRICK DODD, AMERICAN BUSINESS CORPORATIONS UNTIL 1860 196-98 (1954).
75 Id.
76 As late as 1892, one treatise writer on statutory law categorized the law of business and private corporations as public law. Id. at 15 (citing 2 FREDERICK J. STIMSON, AMERICAN STATUTE LAW 1 (1892)).
77 See LAWRENCE M. FRIEDMAN, A HISTORY OF AMERICAN LAW 169 (1973) (describing state investments in banks, turnpike companies, and other firms with quasi-public projects); LOUIS HARTZ, ECONOMIC POLICY AND DEMOCRATIC THOUGHT: PENNSYLVANIA 1776-1860 82-104 (1948) (recounting history of Pennsylvania's investment in its turnpike companies).
that each state should enjoy exclusive authority over the internal affairs of its corporations. In the aftermath of the Revolution, each new state jealously guarded its sovereign prerogatives, and the later deference to the incorporating state embodied in the internal affairs doctrine—assuring each state singular control over the internal governance of its business corporations—followed naturally from these sovereignty concerns. Writing in 1933, one commentator noted:

The early corporations trailed the clouds of glory of their sovereign origin. Thus the East India Company wore the ermine: late in the eighteenth century English courts dismissed a dispute over its breach of contract as a "political question." . . . It is not surprising to find indications, where "internal affairs" were involved, that a matter of some diplomatic nicety was at stake and even today, when general incorporation laws and nationwide corporations are of course, courts hasten to add, in taking jurisdiction, that they are not exercising "visitorial powers." 78

Indeed, well into the twentieth century, the internal affairs doctrine was viewed as a jurisdictional bar—precluding courts from even adjudicating disputes involving foreign corporations' internal affairs—and not merely a choice of law rule. 79 Resting

78 Note, Forum Non Conveniens and the "Internal Affairs" of a Foreign Corporation, 33 COLUM. L. REV. 492, 494-95 (1933) (citations omitted). "Visitorial powers" were those powers "exercised by the founder of a corporation to make and enforce by-laws and to command faithful performance of duties by officers." Id. at 495 n.14.

79 WILLIAM MEADE FLETCHER, 17 CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS § 8425 (perm. ed. 1933); RESTATEMENT OF CONFLICT OF LAWS §§ 196, 197, 199 (1934); Stanley A. Kaplan, Foreign Corporations and Local Corporate Policy, 21 VAND. L. REV. 433, 443 (1969). See generally N. State Copper & Gold Mining Co. v. Field, 20 A. 1039 (Md. 1885); Wilkins v. Thorne, 60 Md. 253 (1883); Smith v. Mutual Life Ins. Co., 96 Mass. 336 (1867); Williston v. Michigan So. & No. Indiana R.R. Co., 95 Mass. 400 (1866); Erickson v. Nesmith, 86 Mass. 233 (1862); Redmond v. Enfield Mfg. Co., 13 Abb. Pr. (N.S.) 332 (Sup. Ct. NY 1872); Howell v. Chicago & Nw. Rwy. Co., 51 Barb. 378 (Sup. Ct. NY 1868). This jurisdictional bar also had certain practical underpinnings. A common rationale for viewing the internal affairs doctrine as a jurisdictional bar was the recognition that a local court would have difficulty enforcing a judgment against a foreign corporation. As one court noted, "it is a little difficult to imagine how a court in [the District of Columbia] could restrain and direct the action of the
jurisdiction exclusively with the courts of the incorporating state invariably resulted in application of that state's laws to the internal affairs dispute, so the choice of law outcome would be consistent with the modern doctrine.

As a creature of the sovereign, each business corporation was thought to exist only within the territorial borders of the sovereign. Since most businesses were local in character, this territorial notion was unremarkable and caused little controversy before the mid-1800s. This ideology of territorial sovereignty helps explain how the internal affairs doctrine could later emerge. Only the incorporating state was deemed to possess authority to decide its corporation's internal affairs disputes. The courts of other states were unwilling to interfere.

This ideology of sovereignty was also conveniently consistent with legislators' rent seeking interests. Because each grant of corporate privileges was effected by special act, legislators were able to exact tribute from the corporate promoters seeking these special privileges. The ideology of state sovereignty assured that legislative bargains would not be revisited by courts outside the incorporating state.

corporation at its home office in the city of New York." Clark v. Mutual Reserve Fund Life Ass'n, 14 App. D.C. 154, 178 (1899). See also Kansas E. Constr. Co. v. Topeka, S. & W. R.R., 135 Mass. 34, 41 (1883) (refusing to enjoin issuance of stock of foreign corporation where issuance would occur out of state and would be governed by other state's law). Corporate assets and corporate officers were not generally found outside the incorporation state.

When businesses eventually began to expand to engage in transactions across state lines, states commonly imposed territorial restrictions on their domestic corporations and forbade foreign corporations from certain businesses and from owning real property in-state. See infra note 86 and accompanying text.

It is not too surprising that jurisdictional disputes would not have arisen before the 1860s. Given the quasi-public conception of corporations, their close ties with state legislatures, and the fact that no distinctions were made among municipal, business, and other corporations, it would have been unthinkable during the preindustrial period for a state's legislature or court to attempt to interfere in the inner workings of the corporate creation of a sister state.

Judicial opinions articulating the doctrine regularly noted the sovereign interests of the incorporating state that were at stake. See infra note 89 and accompanying text.

The graft and logrolling involved with special charters eventually caused popular resentment of the practice. This was one factor that ultimately led to the demise of the practice.

In the early years of the Republic, most states' judges were appointed by the state legislature and so could be assumed to be sensitive to legislators' interests. See Symposium, The Case for Judicial Appointments, 33 U. TOLEDO L. REV. 353, 356-57 (2002) ("The idea of
C. INDUSTRIALIZATION, INTERSTATE FIRMS, AND THE INTERNAL AFFAIRS DOCTRINE

With industrialization, firms’ activities began to cross state lines, and states were forced to develop policies on treatment of foreign corporations. Changes in technology and industrial organization put some competitive pressures on states’ regulatory monopolies. Interstate markets emerged, following dramatic advances in transportation, communication, and energy. The Supreme Court’s Commerce Clause jurisprudence also facilitated market integration. Interstate markets led to the rise of interstate firms and the legal issues concerning states’ treatment of foreign corporations. The first general foreign corporation statutes appeared in 1852. The emergence of interstate firms led to disputes over corporate internal affairs that were brought in courts outside the incorporating state. These suits typically involved shareholders suing in their home states to enforce rights against foreign corporations in which they had invested. In response, courts first articulated the internal affairs doctrine, reflecting preindustrial notions of states’ territorial sovereignty over domestic corporations.

Corporate law was still largely territorial at mid-century. That is, firms ordinarily incorporated in their home states. Corporations and legislatures expected—and legislatures sometimes mandated—that corporations would have significant operations in the incorporating state, that officers and directors would be residents of that state, and that shareholders’ and directors’ meetings would be

direct election of judges was still a generation away.") Popul

1. See James Andrew Wynn, Jr., Judging the Judges, 86 MARQ. L. REV. 753, 764 (2002) (noting “the move away from appointing and to electing state judges coincided with the rapid growth of the American republic” in mid to late 1800s). With popular elections, of course, judges would feel the same local interest group pressures as legislators did.

Moreover, at least until the turn of the twentieth century, courts faced with internal affairs decisions consistently noted that jurisdiction could not exist absent statutory authority. N. State Copper & Gold Mining Co., 20 A. at 1040; Smith, 96 Mass. at 336; Halsey v. McLean, 94 Mass. 438, 438 (1866); Erickson, 86 Mass. at 237; Howell, 51 Barb. at 384-85; Stafford & Co. v. Am. Mills Co., 13 R.I. 310, 310 (1881).

held in the state. In other words, firms ordinarily maintained significant tangible identification with their states of incorporation. Corporate law would remain territorial until the 1890s when charter competition began in earnest.

Multistate markets, however, meant that firms became geographically more mobile at the margin. Firms therefore enjoyed some latitude to shop for favorable business conditions, including attractive corporate law, simply by moving operations to a neighboring state. States felt some pressure to liberalize their corporate laws, including the relaxation of territorial restrictions, in order to maintain local employment and the industrial tax base. What were initially conventional corporate law restrictions—on capitalization, on permissible business activities and their geographical scope—became a hindrance on growth and expansion that was necessary for firms to survive. States had always competed with one another for economic development. Now with the changing needs of business, states responded by loosening some of these corporate law constraints. However, they did not abolish all of them. Instead, they retained the basic idea of limiting corporate size and scope through corporate law. And they continued to demand that their corporations maintain economic ties to their incorporating states. Until the 1890s, the primary focus of these reforms in most states was on keeping and attracting capital and labor.


See Harry N. Scheiber, Federalism and the American Economic Order, 1789-1910, 10 LAW & SOC'Y REV. 57, 71-72 (1975) (describing state competition for economic development as sort of "rivalistic state mercantilism").

Raising revenues directly through the sale of corporate charters was an innovation that occurred only in the 1890s with New Jersey's implementation of its "chartermongering" strategy. Christopher Grandy, New Jersey Corporate Chartermongering, 1875-1929, 49 J. ECON. HIST. 677, 680-81 (1989). Before 1888-1890, even New Jersey's corporate law liberalization was done primarily with local firms in mind—firms with operations located primarily in-state. See supra note 86. A special Massachusetts legislative committee report in 1903 noted that "[u]ntil within the past ten years the practice of foreign incorporation was not general." MASSACHUSETTS REPORT OF THE COMMITTEE ON CORPORATION LAWS 18 (1903).
Early decisions articulating the internal affairs doctrine echoed preindustrial notions of states' sovereignty over their domestic corporations. Sovereignty considerations required deference to the incorporating state, and courts of other states did not have jurisdiction to address questions of corporate internal affairs. This jurisdictional bar "does not merely regard the powers of the court, but rather the extent of the state authority which underlies those powers. It is in the nature of a question of sovereignty." Internal affairs decisions before the merger movement were not many, and judging from that relative handful of decisions, courts seemed to find their jurisdictional limitations in this area fairly self-evident. They consistently noted the special role of the incorporating state, the state under whose laws the corporation was created and on which its existence depended. Though private business corporations were no longer viewed as public agencies, a strong sense continued to exist that they were territorially and conceptually bound to their incorporating states—that each corporation depended for its existence on its state of incorporation and had no legal existence outside that state except as the comity of other states.

---

89 *Smith*, 96 Mass. at 336.
90 *Id.* at 341; *Howell v. Chi & N.W. Rwy. Co.*, 51 Barb. 378 (N.Y. Sup. Ct. 1868). In addition to state sovereignty considerations, courts also noted the practical wisdom of the doctrine. Courts recognized the territorial limits of their own authority, and they wished to avoid adopting decisions that would require enforcement in other states. Taking jurisdiction "would be assuming a power which the court ought not to exercise, and rendering a judgment which could not be enforced against the company in the place of its existence." *Redmond v. Enfield Mfg. Co.*, 13 Abb. Pr. (n.s.) 332, 333 (N.Y. Sup. Ct. 1872); *see also N. State Copper & Gold Mining Co. v. Field*, 20 A. 1039, 1041 (Md. 1885) (stating that legislature did not give judiciary powers over internal affairs of foreign corporations). In addition, consistent with modern functionalist explanations for the doctrine, some courts recognized that the jurisdictional bar avoided subjecting corporations to conflicting decisions and inconsistent obligations. This was especially problematic for mutual insurance companies, whose policyholders were also its shareholders. "[N]o corporation could ever venture to conduct business beyond the limits of the State of its creation . . . . It might have a half dozen courts, in as many different States, requiring discovery, and demanding the production of books, and directing the statement of accounts, all at the same time." *Clark v. Mut. Reserve Fund Life Ass'n*, 14 App. D.C. 154, 179 (1899); *see also N. State Copper & Gold Mining Co.*, 20 A. at 1041 (noting prospect of "conflicting decisions," "interminable confusion," and "judgments and decrees that the courts of Maryland would be unable to enforce"); *Taylor v. Mut. Reserve Life Ass'n*, 33 S.E. 385, 389 (Va. 1899) (discussing problems of inability to enforce injunction).
might allow. With Paul v. Virginia, the Supreme Court in 1868 reaffirmed this territorial view of corporate existence.91

D. THE GREAT MERGER MOVEMENT AND CORPORATE LAW

Modern law-as-a-product charter competition began in earnest in the last decade of the nineteenth century. The story of corporate charter competition among the states—and the explanation for the persistence of the internal affairs doctrine—is inextricably bound with the story of the great merger movement at the end of the nineteenth century and New Jersey’s pioneering strategy of marketing its corporation law to firms with no economic ties to the state. Economic pressures forced other states to follow suit. They stopped insisting that corporations maintain substantive economic ties to their incorporating states, and they recognized the corporate status of corporations with no such ties. Now firms could choose their corporate law.

Toward the end of the nineteenth century, industrialization, urbanization, and the emergence of interstate markets and firms had led to industrial concentration across important industries. Driven in part by the new scale economies92 and in large measure by

91 75 U.S. 168, 181 (1868)

The corporation being the mere creation of local law, can have no legal existence beyond the limits of the sovereignty where created . . . . The recognition of its existence even by other States, and the enforcement of its contracts made therein, depend purely upon the comity of those States—a comity which is never extended where the existence of the corporation or the exercise of its powers are prejudicial to their interests or repugnant to their policy. Having no absolute right of recognition in other States, . . . it follows, as a matter of course, that such assent may be granted upon such terms and conditions as those States may think proper to impose. They may exclude the foreign corporation entirely; they may restrict its business to particular localities, or they may exact such security for the performance of its contracts with their citizens as in their judgment will best promote the public interest. The whole matter rests in their discretion.

Id. Even after the merger movement and the formation of the great trusts as holding companies with national reach, courts relied on these same state sovereignty ideas in articulating the internal affairs doctrine.

92 From 1850 to 1920, the average manufacturing plant for agricultural implements increased its capital by over 260 times, its number of wage earners by almost twenty-one times, and the gross value of its output by 114 times. JEREMIAH WHIPPLE JENKS & WALTER
anticompetitive impulses, entire industries consolidated into one or a handful of national producers. Numerous industries became monopolized. These monopolies were originally organized under private trust agreements, corporation laws being too restrictive to be useful in this regard. The trusts provoked public outrage. The vast majority of corporations were still “relatively small affairs, financed for the most part through local subscriptions rather than by resort . . . to nationwide systems of security distribution or to stock exchanges.”

Beginning in the 1880s, state officials in six states attacked the trusts in court in order to break them up.

E. CLARK, THE TRUST PROBLEM 17 (5th ed. 1929). For iron and steel manufacturing plants, the average capital increased almost 107 times, the average number of wage earners increased by more than eleven times, and the value of output increased 119 times. Id. Across all manufacturing plants, average capital increased by thirty-seven times, labor by almost five times, and the value of output by almost twenty-six times. Id.

Eastern railroad corporations formed the first significant national monopolies. Eight railroad corporations together used their control over transportation to acquire ninety-five percent of the anthracite coal industry by 1893. Railroads monopolized other industries as well: bituminous coal, kerosene, matches, stoves, furnaces, steam and hot water heaters, boilers, gas pipelines, and candles. RALPH NADER ET AL., TAMING THE GIANT CORPORATION 39 (1976). John D. Rockefeller’s Standard Oil Trust was the first great industrial monopoly. By 1880, he controlled ninety-five percent of all refined oil shipments in the United States. Id. at 42. Other industrial trusts followed in short order. The Cotton-seed Oil Trust was organized in 1884; the Linseed Trust in 1885. Three great trusts were created in 1887: the National Lead Trust, the Sugar Trust, and the Whiskey Trust. HENRY R. SEAGER & CHARLES A. GULICK, JR., TRUST AND CORPORATION PROBLEMS 51 (1929); Harold Underwood Faulkner, Consolidation of Business, in ROOSEVELT, WILSON, AND THE TRUSTS 7 (1950) (Edwin C. Rozwenc ed.). For specific discussion of the formation and operation of the Sugar Trust, see REPORT OF THE COMMITTEE ON GENERAL LAWS RESPECTING ALL MATTERS RELATING TO “TRUSTS,” AND ESPECIALLY “SUGAR TRUSTS,” N.Y. SEN. DOC. NO. 79 4-9 (1891). By 1890, twenty-four trusts had been formed, with total capital of $376 million. NADER ET AL., supra, at 42.

E. Merrick Dodd, Jr., STATUTORY DEVELOPMENTS IN BUSINESS CORPORATION LAW, 1886-1936, 50 HARV. L. REV. 27, 30 (1936); see also Thomas R. Navin & Marian V. Sears, The Rise of a Market for Industrial Securities, 1887-1902, 29 BUS. HIST. REV. 105, 107 (1955) (noting that industrial firms of late 1880s were “typified by small single-plant companies serving limited markets”).


The legal theory relied upon did not directly address questions of monopoly or restraint
At the same time the trusts came under attack by the states, New Jersey adopted a new tack in developing its corporation law. As earlier noted, before the merger movement, states generally liberalized their corporation laws, not to sell corporate charters for their own sake, but typically as part of a program to attract and retain capital and labor in the state.\footnote{See supra notes 87-88.} Offering attractive corporate law was merely part of a general effort to create a favorable climate for business. Beginning in 1888, New Jersey targeted firms without any necessary economic connection to the state. It hoped to raise revenue merely from the sale of corporate charters to firms with all or most of their operations elsewhere.\footnote{Christopher Grandy, New Jersey and the Fiscal Origins of Modern American Corporation Law 43 (1993).} Its new pricing strategy—taxing its corporations annually based on their authorized capital—created the potential for enormous revenues.\footnote{Somewhat fortuitously, New Jersey had modified its method of taxing corporations a few years earlier. In 1884, "[a]llmost as an afterthought" following passage of a new tax on railroads, the legislature enacted a corporate tax based on authorized capital. Grandy, supra note 88, at 680-81. Several years passed before anyone saw the revenue potential in this new method of taxation.} Corporate law became a product, not just a marketing device.

New Jersey’s timing was excellent. Critical amendments were enacted beginning in 1888 that facilitated holding company structures and consolidations, exactly the legal tools the great trusts needed that corporate law had not theretofore offered.\footnote{An 1888 act allowed New Jersey corporations to hold stock in other corporations, thereby enabling holding companies. Keasbey, supra note 86, at 207; Harold W. Stoke, Economic Influences upon the Corporations Laws of New Jersey, 38 J. Pol. Econ. 551, 571 (1930). An 1891 law permitted corporations to purchase stock or other property using their own stock in payment, with great deference given to the directors’ judgment. Stoke, supra, at 571. This deference was important in allowing acquiring corporations to pay handsomely for their acquisitions by issuing their own stock as consideration. In 1892, New Jersey repealed its antitrust statute. Keasbey, supra note 86, at 209. It also made explicit that corporations could be formed to do all their business outside the state. See Louis K. Liggett Co. v. Lee, 288 U.S. 517, 563 & n.44 (1933) (citing N.J. Laws 1892, p. 90). General authority for mergers was enacted in 1893, along with a broadening of authority for holding companies. See supra note 86 at 207.}
Corporations, especially the largest ones, flocked to New Jersey. By 1899, all the combinations that had been dissolved through the actions of the state attorneys general in the preceding decade had reemerged as New Jersey corporations.\(^\text{100}\)

Other states faced a crucial choice during this period of industry consolidation and New Jersey's stunning modifications of its corporation law. They could either fight New Jersey and its corporations, or they could succumb. While most other states condemned New Jersey's charter-selling strategy, and a few studiously mimicked it, most states reluctantly succumbed. The legal tools for resistance to New Jersey were available. States could readily have revoked the charters of domestic corporations that attempted to merge or consolidate into New Jersey holding company structures.\(^\text{101}\) And they could have excluded foreign corporations from conducting local business or admitted them with appropriate conditions.\(^\text{102}\) But most states followed New Jersey's lead on many aspects of corporation law. They modified their laws sufficiently to defend against the possibility of their domestic corporations seeking new charters from New Jersey. And they did not attempt to exclude foreign corporations or condition their entry in any meaningful way. Massive consolidation across important industries, along with the Panic of 1893, left state economies weak. Their economic condition made it too risky for most state legislatures to attempt to exclude foreign corporations or condition their entry. Imposing conditions might merely drive business to a neighboring state. A foreign

---

\(^{100}\) McCurdy, supra note 95, at 322-23 (citing XIX REPORTS OF THE INDUSTRIAL COMMISSION 598-99).

\(^{101}\) The same quo warranto actions that state attorneys general took against the trusts would have been viable after those same trusts found homes as holding companies under New Jersey's corporation law. Operating companies chartered in the various states had no more power to transfer control to New Jersey holding companies than they had power to transfer control to the trusts that preceded them.

\(^{102}\) See McCurdy, supra note 95, at 336 (noting states' power to forbid foreign corporations from doing business locally); Alton D. Adams, State Control of Trusts, 18 POL. SCI. Q. 462, 478 (1903) (discussing states' broad powers over foreign corporations). States could not exclude foreign corporations engaged in interstate commerce, however. HARRY G. HENN, HANDBOOK OF THE LAW OF CORPORATIONS AND OTHER BUSINESS ENTERPRISES 17 (1961); GERARD CARL HENDERSON, THE POSITION OF FOREIGN CORPORATIONS IN AMERICAN CONSTITUTIONAL LAW 114 (1918).
corporation's lack of significant economic ties to its state of incorporation now mattered little.

Despite the demise of territorial corporate law, the rhetoric of courts' internal affairs decisions during and after the merger movement remained consistent with the earlier justifications. The sovereignty of the incorporating state remained a concern. Courts recognized that their disability to interfere in a foreign corporation's internal affairs resulted from their state's general lack of authority in the area. 103

E. THE POLITICAL ECONOMY OF THE INTERNAL AFFAIRS DOCTRINE

While the basic notion remained consistent that the law of the state of incorporation should apply to the corporation's internal affairs, the doctrine's impact would be dramatically different depending on firms' practical ability to choose their state of incorporation. When all businesses were local businesses and all corporations incorporated locally, each state enjoyed something of

103 Courts continued to conceive of corporations in territorial terms, echoing state sovereignty considerations from the eighteenth century. Courts referenced the sovereign powers of the incorporating state in refusing jurisdiction over disputes involving the internal affairs of foreign corporations. For example, an 1894 Minnesota Supreme Court decision noted:

The doctrine is well settled that courts will not exercise visitatorial powers over foreign corporations, or interfere with the management of their internal affairs. Such matters must be settled by the courts of the state creating the corporation. This rule rests upon a broader and deeper foundation than the mere want of jurisdiction in the ordinary sense of that word. It involves the extent of the authority of the state (from which its courts derive all their powers) over foreign corporations.

Guilford v. W. Union Tel. Co., 61 N.W. 324, 325, 339-40 (Minn. 1894). Despite this acknowledged limitation on the court's jurisdiction, however, it proceeded to order the corporation's issuance of replacement stock certificates to an in-state shareholder, finding that this would not interfere with internal management of corporate affairs. Id.; see also Clark v. Mut. Reserve Fund Life Ass'n, 14 App. D.C. 154 (1899)

[A]crts [authorizing local business by foreign insurance companies] do not extend the jurisdiction of the courts of one State and authorize them to reach over their territorial limits into the jurisdiction of another State, and to bring into review and revision the corporate acts and internal affairs of the local corporations of the latter State. Such a power, if attempted to be exercised, would be futile and ridiculous. Indeed, neither the legislatures of the States, nor the Congress of the United States, could confer such power.

Id.
a territorial monopoly over its local firms. Legislatures could therefore extract rents from geographically captive businesses, both in terms of fees and other exactions and also by reinforcing firms' territorial limits through legal mandate. By requiring, for example, that domestic corporations maintain local headquarters and do only in-state business and that key managers reside in-state, a state legislature was able to cement its local corporations' dependence on its legislative grace.

In this context, the internal affairs doctrine merely augmented the existing legal monopoly by assuring that each state's local monopoly would not be interfered with by sister states. In effect, the doctrine promoted market sharing among states with respect to their legal monopolies over local businesses. Even with the rise of interstate firms, as long as states expected or required that firms maintain economic ties with their incorporating states, firms had little choice about where to incorporate.

However, the merger movement and New Jersey's charter-selling strategy broke the territorial ties between the firm and its incorporating state. State legislatures were generally in no position to attempt to exclude or condition the entry of foreign corporations or even tramp corporations with no economic ties to their incorporating state. Under those conditions, firms could choose their state of incorporation, and the deference to the incorporating state embodied in the internal affairs doctrine now honored firm choice.

During and after the merger movement, in-state groups that enjoyed the benefit of continuing relations with foreign corporations likely had concentrated interests at stake and could readily organize to assert those interests. For example, local customers—especially industrial consumers—and suppliers, and local managers and employees of foreign-incorporated firms would have large per capita stakes in the continued in-state activities of foreign corporations. Legislators as well would enjoy the political benefit of local economic development and an increased tax base from these economic activities. With these pressures and inducements to support local interaction with foreign corporations, legislatures would have been hard pressed to maintain laws generally excluding foreign corporations or significantly deterring their entry. Moreover, states' territorial monopolies on corporate law appeared unsalvageable.
Reluctance to demand conditions for entry probably precluded any thought of regulating foreign corporations’ internal affairs. With substantive liberalization, corporation laws no longer had much regulatory bite anyway. Therefore, there would have been little to gain from revisiting the existing internal affairs doctrine to attempt to impose local corporate rules on foreign corporations.\textsuperscript{104}

The selling of corporate charters was an innovation by political entrepreneurs who saw opportunity in fortuitous circumstances. These political entrepreneurs appreciated the public and private revenue-generating potential for corporate chartering. James Brooks Dill, a New York lawyer who lived in New Jersey during the late 1880s, is generally credited with the idea of selling corporate charters to raise state revenues.\textsuperscript{105} After failing to convince New York politicians to adopt his scheme, Dill went across the river to New Jersey.\textsuperscript{106} In addition to proposing liberalizing amendments to New Jersey’s corporation law and lobbying the governor for their passage, Dill saw to it that both he and important politicians

\textsuperscript{104} The liberalizing trend in corporate law applied to corporate internal affairs as well. Provisions less constraining to management were copied; provisions with the opposite bent were rebuffed. Recall, for example, New Jersey’s bid to facilitate corporate acquisitions by shielding directors’ business judgment concerning the value of property acquired for stock. See supra note 99. This was a dramatic liberalization in the rules of internal corporate management. New Jersey’s liberalizing provision was quickly copied, even by New York. By 1903, six other states had adopted provisions giving conclusive effect to directors’ judgment on the valuation of property taken as payment for stock. The six states were Connecticut, Delaware, Maine, New York, North Carolina, and West Virginia. MASSACHUSETTS REPORT, supra note 88, at 181.

Legislators also pursued regulatory substitution strategies, creating new territorially-based regulation for the benefit of local shareholders and other groups that had formerly enjoyed some protection under restrictive corporation laws. For example, beginning with Kansas in 1911, state legislatures enacted “blue sky” laws, state securities laws meant to protect local investors from unscrupulous corporate promoters. LOUIS LOSS & EDWARD M. COWETT, BLUE SKY LAW 8 & n.24 (1958). State securities commissions were established to review the merits of offering before they could be made to local investors. Only securities that received the blessing of the commission could be sold to the public, and the commission enjoyed a broad scope of review. Grounds for prohibiting an offering included a finding that any of the issuer’s organizational documents or business plan contained any “unfair, unjust, inequitable or oppressive” provision, or that the issuer “does not intend to do a fair and honest business,” or “does not promise a fair return on the stocks, bonds or other securities.” Id. Within two years of Kansas’ enactment, twenty-three other states had followed suit. Id. at 10. Almost all these later enactments were patterned after the Kansas model.

\textsuperscript{105} Stote, supra note 99, at 571.

\textsuperscript{106} See id. (describing New Jersey’s general corporation law of 1849).
personally profited from the chartermongering strategy. Dill founded a corporation services company—the Corporation Trust Company of New Jersey—for which the clerk of chancery served as an incorporator, and the governor and secretary of state served as directors. The latter eventually became president of the company.

The technological, economic, and legal changes that occurred in the mid-nineteenth century changed relative prices in favor of interstate firms transacting in interstate markets. Dill and the New Jersey politicians he recruited successfully responded to the demand for nonterritorial corporation law, and then economic pressures precluded legislatures from excluding foreign corporations or conditioning their entry. Interstate firms naturally developed constituencies in various states that stood to benefit from the firms’ doing business locally. Legislators and interest groups in each state would have seen no point to opposing recognition of foreign corporations and respect for foreign corporation law.

---

107 GRANDY, supra note 97, at 40.
108 A corporation services company handles the administrative work for corporate formation and maintenance in good standing. It can provide suitable articles of incorporation and file them with the secretary of state’s office. It can provide an in-state address for a firm’s principal office and an agent for service of process. It can provide incorporators or directors. The webpage for CT Corporation, a premier corporation services company, offers a typical set of services. CT Corporation, Law Firm Customers, at http://www.ctadvantage.com/public/lawFirmCustomers.html#Staffing (last visited Nov. 9, 2004).
109 GRANDY, supra note 97, at 40. His involvement “must have proven particularly useful as the secretary of state’s office regularly received inquiries about the law and referred them to one of the corporation service companies.” Id.
110 “The agent of [institutional] change is the individual entrepreneur responding to the incentives embodied in the institutional framework. The sources of change are changing relative prices or preferences.” DOUGLASS C. NORTH, INSTITUTIONS, INSTITUTIONAL CHANGE AND ECONOMIC PERFORMANCE 83 (1990).
111 With the merger movement, dramatic horizontal consolidation and vertical integration made interstate firms ubiquitous across important industries. Local employees now worked for foreign corporations. Local customers and suppliers had important relations with foreign corporations. Foreign corporations used local transportation and communication facilities. They might offer capital, managerial expertise, or scale economies that could keep the local plant in operation, when it would otherwise be shuttered. They might offer an interstate distribution system for locally produced goods.
113 Nonrecognition or attempts to apply local law to foreign corporations would have driven those firms out of the jurisdiction, only to do business in more hospitable states.
But this was neither planned nor inevitable. For our purposes, what is absent from this story is also important. No state set out to create or facilitate a national market for corporate charters. Instead, the choice of law convention that eventually enabled this regulatory market emerged earlier for unrelated reasons. At its origin, no interested groups would or could have anticipated its significance to the modern regulatory competition story.\textsuperscript{114} The doctrine was not created to enable regulatory competition, and if the doctrine had not already existed, it is doubtful that widespread coordination around such a choice-of-law convention could have been achieved among states.\textsuperscript{115}

Territorial application of local corporate law would typically have involved rules to protect local investors or creditors, and exercise of prescriptive jurisdiction would likely have been based on the presence of the firm's headquarters or predominance of firm assets, employees, investors, or business activities in the prescribing jurisdiction. \textit{See supra} note 64 and accompanying text. Firms could have avoided unattractive corporate law by simply relocating out of an unattractive jurisdiction or by otherwise avoiding those contacts that would trigger host state regulation, while continuing to sell products into the unfriendly jurisdiction.

This relatively easy exit option meant that a state had little to gain and something to lose—in terms of local tax base, business opportunities, employment, and other positive spillovers—by attempting to impose local corporate law in the face of a firm's election of foreign law. The reluctance of foreign corporations to do business in a recalcitrant state might harm in-state interests wishing to do business with such firms. The threat of firms' physical exit to avoid a state's undesirable corporate law forced states to accede to virtual exit—avoidance of the unattractive local law without the need for physical exit. Continuing to honor the long-standing convention of the internal affairs doctrine—albeit in this new context of firm mobility—enabled just that.

States' other obvious alternative—reforming the unattractive aspects of their corporate laws—has apparently also been pursued. Scholars have noted the substantial uniformity across states' corporate law statutes. \textit{Black, supra} note 44, at 588; \textit{Romano, supra} note 6, at 235.

\textsuperscript{114} The internal affairs doctrine is also not neatly and uniformly applied by the states. Consistent with a decentralized evolutionary story for the internal affairs doctrine, a few states that might be in a position to impose local corporate law on foreign corporations without driving them out have attempted to do so. California in particular takes a relatively aggressive position in imposing certain local corporate law rules on certain foreign corporations. \textit{See supra} note 64. New York has its own "outreach" statute as well. \textit{See supra} note 64. The behavior of California and New York is consistent with the interest group explanation for the internal affairs doctrine. For states with large internal markets like California and New York and many local corporations with local operations, in-state interests may be less worried about the threat of firms' physical exit than smaller states like Delaware and New Jersey. In-state interests would have been less enthusiastic about opposing such outreach statutes.

\textsuperscript{115} In the face of similar interjurisdictional economic pressures, for example, European states have not voluntarily adopted an internal affairs approach to corporate choice of law. \textit{Charny, supra} note 7, at 424-25.
IV. CHOICE OF LAW IN INTERNATIONAL SECURITIES REGULATION: TERRITORIALITY AND ITS PERSISTENCE

Moving from the domestic to the international context, no mechanism like the internal affairs doctrine exists. It is also unlikely to be replicated. National regulators and other important interests in each nation have powerful incentives and significant influence to perpetuate territorial securities regulation, especially in the most important capital markets.\(^\text{116}\)

A. THERE'S NO PLACE LIKE HOME

History matters and the history of the internal affairs doctrine helps explain how jurisdictional competition over corporate charters arose among U.S. states.\(^\text{117}\) Corporate formation in the United States historically carried connotations of sovereignty, so that the law under which a corporation was created might enjoy some respect and deference among states.\(^\text{118}\) Later, dramatic consolidation in important industries, economic dislocation, and the emergence of large interstate conglomerates created interest group alignments that made existing custom irreversible.\(^\text{119}\) But unlike corporate formation in the United States, issuance and trading of corporate securities appear not to carry any historical ideological association with sovereign powers nor any implication of comity among nations. Instead, securities regulation smacks of consumer protection.\(^\text{120}\) One might expect that nations would be reluctant to

\(^{116}\) See infra notes 119-27 and accompanying text.

\(^{117}\) See supra notes 81-94 and accompanying text.

\(^{118}\) See supra notes 89-91 and accompanying text.

\(^{119}\) See supra notes 112-15 and accompanying text.

\(^{120}\) Among the express purposes of the Securities Act of 1933 is the goal of "prevent[ing] frauds in the sale" of securities. Pub. L. No. 73-22, 48 Stat. 74, 74 (1933). The Securities Exchange Act of 1934 is meant, among other things, "to prevent inequitable and unfair practices on . . . exchanges and markets." S. REP. NO. 73-185, at 1 (1934) (conference report on final bill).
defer to foreign law for the protection of their own consumers, especially foreign law selected by the seller of the wares at issue. Also, unlike the great trusts at the turn of the twentieth century, whose size and economic strength enabled them to avoid doing business in unfriendly jurisdictions, issuers of securities—especially those in the most developed capital markets—generally cannot avoid their home country securities markets and home country securities laws.¹²¹

Largely because an issuer’s home country investors enjoy informational advantages over other investors, an issuer’s most attractive capital market is typically its home country market. Especially in the most important capital markets, issuers almost invariably issue securities in the home market first.¹²² Avoiding the home jurisdiction is not a viable option. This may explain why, among nations, securities regulation is basically territorial. Nations regulate securities activity that occurs within their borders. They need not offer their domestic issuers much choice because those issuers typically cannot avoid their home jurisdictions. Because issuers have no exit option, regulators enjoy a regulatory monopoly as to their domestic issuers.

Why is exit from home country securities regulation so difficult? By the time an issuer is considering selling securities to the public, the issuer already has something of a track record. It has established itself to some extent, typically in one country—its home country. It has headquarters and key operations, managers and other employees, relationships, goodwill, and other assets, most or all of which will be located in the same country. Even if these critical elements are dispersed across countries, the issuer will ordinarily have an identifiable center of gravity, a country with which it identifies and is identified. At this stage, the issuer’s critical components will not readily transplant internationally without significant loss of value.¹²³

¹²¹ See infra note 125 and accompanying text.
¹²² See infra note 125 and accompanying text.
¹²³ While the firm’s founders could theoretically have factored in the future possibility of issuing securities when they decided where to locate the firm and could therefore have accounted for the relative hospitality of various jurisdictions’ securities laws, chances are that more immediate factors dominated any consideration of securities law. Product markets,
Along with these established physical ties, the prospective issuer will typically have developed expertise in navigating the business and regulatory environment in its home jurisdiction by the time the issuer considers securities activities that would trigger significant regulation. This expertise is country-specific and, like the firm's physical assets, not readily transferable across international borders. A move across international borders would require the firm to adapt to a new business culture, a new regulatory environment, a new tax structure, perhaps a new language. Many key officers and employees would not wish to relocate. Immigration issues with the target jurisdiction might impede ready relocation of personnel. Trade barriers might make the original home market less accessible to the relocated firm's products.

Because of the firm's physical location in the jurisdiction and its past business activities, prospective investors in the jurisdiction are likely to enjoy informational advantages over prospective investors in other countries. The firm is a known quantity in its home country. Its products and marketing, its employees, its relationships with customers and suppliers, and its dealings with local government all provide information to local investors that may be less accessible to investors elsewhere. Because of the informational advantages local investors enjoy, they will generally be able to outbid their foreign rivals for the firm's securities. So the firm's costs of capital are likely to be lowest at home, at least in its initial securities offerings. This explains why firms ordinarily issue

\[\text{lab labor markets, availability of key inputs, and tax considerations, among other things, would have been more critical to the early success of the venture, without which a consideration of any securities offering would be premature.}\]

The home bias puzzle, that international investors suboptimally overweight their portfolios in favor of domestic stocks, is widely documented in the corporate finance literature. Magnus Dahlquist et al., Corporate Governance, Investor Protection and the Home Bias, 1 (June 2002) (unpublished manuscript, available at http://ssrn.com/abstract=320222) (stating that home bias is "the least controversial stylized fact in international finance"). See generally G. Andrew Karolyi & Rene M. Stulz, Are Financial Assets Priced Locally or Globally?, in 1B THE HANDBOOK OF THE ECONOMICS OF FINANCE 975 (George M. Constantinides et al. eds., 2003) (reviewing home bias literature); Karen K. Lewis, Trying to Explain Home Bias in Equities and Consumption, 37 J. ECON. LITERATURE 571 (1999) (reviewing home bias literature). For important discussions of the home bias, see generally Ian Cooper & Evi Kaplanis, Home Bias in Equity Portfolios, Inflation Hedging, and International Capital Market Equilibrium, 7 REV. FIN. STUD. 45 (1994) (testing whether home bias is caused by investors attempting to hedge inflation risk); Dahlquist et al., supra, at 1
securities in their home markets first and why they generally cannot avoid issuing in their home jurisdictions. Moreover, financial economists have shown that the price formation process for firms cross-listed on foreign stock exchanges is dominated by activity on the home country exchange, even when the foreign exchange is the superior exchange in terms of depth and liquidity.126


Financial economists have proposed several different explanations for the home bias, including the existence of information asymmetries as between foreign and domestic investors. See Coval & Moskowitz, supra, at 2045-46 (discussing explanations for home bias).

See Merritt B. Fox, The Political Economy of Statutory Reach: U.S. Disclosure Rules in a Globalizing Market for Securities, 97 MICH. L. REV. 696, 770-71 (1998) (“Despite the burden of compliance, avoiding the U.S. market traditionally has not made sense for U.S. issuers since the United States is the residence of a large portion of their most likely potential investors.”); Romano, supra note 13, at 2397 (“Resort solely to foreign capital markets for financing is not a viable option for publicly traded U.S. firms.”). Under the EU’s “passport” system for securities listings and public offerings, a firm could choose a regulatory regime other than that of its home state by making its initial offering in another member state. But “[i]n reality, very few issuers apparently choose to list outside of their home country given that issuers often find the warmest reception for their securities in their home markets.” Howell E. Jackson & Eric J. Pan, Regulatory Completion in International Securities Markets: Evidence from Europe in 1999—Part I, 56 BUS. LAW. 653, 678-79 (2001).


See Kenneth A. Froot & Emil Dabora, How Are Stock Prices Affected by the Location of Trade?, 53 J. FIN. ECON. 189, 189 (1999) (showing that stock prices of “Siamese-twin” companies do not move in lockstep, but that relative stock prices are highly correlated with relative stock market indexes of countries in which twins’ stocks trade most actively); Shmuel Hauser et al., International Transfer of Pricing Information Between Dually Listed Stocks, 21 J. FIN. RES. 139, 139 (1998) (analyzing dual-listed Israeli companies); Cheol S. Eun & Sanjiv Sabherwal, Cross-Border Trading and Price Discovery: Evidence from U.S.-Listed Canadian Stocks, 58 J. FIN. 549, 549 (2003) (finding that for most cross-listed Canadian firms, Toronto Stock Exchange dominated price discovery, and that degree of U.S. contribution to price discovery correlated with degree of competition for trades); JOACHIM GRAMMIG ET AL.,
This is consistent with the notion that hometown investors enjoy superior information about local firms.\textsuperscript{127}

It is this hometown effect that guarantees the regulatory monopolies that issuer choice proponents decry. Because firms have historically been more or less captive to their home country securities markets and cannot easily escape home country securities laws, local interests with stakes in the volume of local securities activity—stock exchanges, securities lawyers, accountants, underwriters, and brokerage firms—would not have felt threatened by the possibility of firm exit. Regulators and other policymakers would therefore not have felt much local pressure to accommodate issuers in order to forestall their exit. While excessive regulation that would dampen the amount of local securities activity was certainly to be avoided, the extreme measure of allowing issuers to choose their own regulation would have been unnecessary. Moreover, unlike the genesis of the internal affairs doctrine, no shared tradition or ideology exists among nations to give local deference to foreign securities law, whether selected by the issuer or otherwise. A policy to forsake territorial jurisdiction in deference to firm choice would not have been considered.

By contrast, choosing a state of incorporation among U.S. states is—and since the great merger movement, has been—a very different enterprise. If a state attempted to impose local corporate rules on foreign corporations with specified contacts in the state,\textsuperscript{128} many firms would have flexibility to relocate or relinquish the damning contacts in order to avoid inhospitable rules.\textsuperscript{129} Unlike international relocation, a firm relocating or restructuring across state lines does not fear new tariff barriers or other serious local

\textsuperscript{127} See Amir N. Licht, Legal Plug-Ins: Cultural Distance, Cross-Listing, and Corporate Governance Reform 22 BERKELEY J. INT'L L. 195, 209 (2004) ("Investors not only buy securities of firms which they know; they prefer securities of firms which they know better.").

\textsuperscript{128} See supra note 64.

\textsuperscript{129} Certainly for a firm's initial incorporation, while the firm may have already had some nontrivial economic activity located primarily in one state, the business will generally be at a much earlier stage in its development than a firm considering a public securities offering.
protectionism. Even for a relatively mature firm, physical relocation from one state to another would not be nearly as traumatic or value-decreasing as an international move. The simple moving of assets and employees would certainly be cheaper than moving abroad. Adjustment costs would likely be far lower. The regulatory environment would not likely be all that different in the new state. The language would remain unchanged. The currency would stay the same. The business culture and social environment would not likely be too different as compared to an international move.

Among U.S. states, then, relatively easy exit for firms searching for desirable corporate law, along with the preexisting internal affairs doctrine, pressured states to accommodate—both in terms of substantive corporate law rules and choice of law. Not so for securities law among nations. Firms' lack of international mobility meant that national regulators could insist on territoriality in securities regulation, imposing national laws on all issuance and trading of securities within their jurisdictions.

B. INTEREST GROUPS AND THE PERSISTENCE OF TERRITORIAL MONOPOLY

In this section, I explain the likely persistence and durability of territoriality in important capital markets. The operation of a national securities regulatory regime, combined with the historical difficulties of firms' physical exit from their home jurisdictions,

---

130 See supra notes 88-115 and accompanying text.
131 Moreover, the globalization of securities markets has made investors more mobile. See Jackson & Pan, supra note 125, at 655-56 (discussing effect of cross-border secondary market linkages). Investors interested in foreign securities are not limited solely to the choices offered on their national exchanges. They may be able to transact in foreign markets fairly easily. In addition, the explosion of institutional intermediaries has allowed investors to obtain foreign exposure for their portfolios through indirect holdings via mutual funds and pension funds. Given these various avenues for foreign securities investing, strict territoriality in securities regulation may not come under the same domestic pressure as a similar choice of law rule in the corporate law context.
132 For a discussion of minor moves toward cross-border regulatory cooperation, see generally Frederick Tung, Passports, Private Choice, and Private Interests: Regulatory Competition and Coordination in Corporate, Securities, and Bankruptcy Law, 3 CHI. J. INT'L L. 369 (2002) (comparing direct competition and regulatory passport approaches to international regulatory coordination).
would not surprisingly produce important interest groups with stakes in territorial regulation. Regulators and other interests have adopted strategies and developed expertise in pursuit of their private interests. They have invested in territoriality.

Continuing with the public choice assumptions of issuer choice proponents, we must conclude that regulators, like all monopolists, will wish to preserve their regulatory monopoly.\footnote{A move from the current mandatory territorial system to issuer choice would likely result in a number of issuers figuratively fleeing from the local regulation offered by the governments of major capital markets to lower cost regulatory regimes. The exit option offered by issuer choice might be especially attractive for domestic firms in these countries, which cannot avoid issuing in their home market and which are therefore bound to local regulation under the current territorial system. This would allow domestic issuers to escape from the overzealous regulation of their national regulators, effectively breaking existing regulatory monopolies.} As well, they will pursue a strategy of regulatory price discrimination in order to augment the reach of their bureaucracies.\footnote{See infra note 139 and accompanying text.} Private actors within each nation have also developed expertise and skill sets peculiarly tailored to their local regulation. Lawyers, accountants, underwriters, stock exchanges, and securities firms, among others, have all established organizations and practices premised on the continued existence of territorial regulation. They will likely support regulatory price discrimination and the territorial jurisdiction on which it depends.

I first discuss the role and influence of regulators in preserving existing territorial monopolies, as well as their maximizing strategy of regulatory price discrimination. I then address other interest groups.

1. Regulators and Regulatory Price Discrimination. Given the highly technical nature of securities regulation in developed capital markets, regulators in these markets will likely play a crucial role in any reform of international securities regulation. They are likely to be the most critical interest group for purposes of any international choice of law coordination.\footnote{Tung, supra note 21, at 1411.} Regulators in the largest and deepest capital markets, of course, enjoy significant benefits from the current system of territorial monopoly. They will be reluctant to forsake these benefits.
With territorial securities regulation, regulators effectively serve as gatekeepers to their national securities markets. Those desiring to offer, sell, or trade securities within the regulator's jurisdiction are required to comply with regulatory mandates. In essence, regulators exact a price for access to their national markets. The price is not so much paid in cash to the regulator—although some fees may be charged. Instead, the price is charged largely in the form of exaction of regulatory compliance—registration requirements, periodic reporting, and the like.\(^{136}\)

Securities regulators typically enjoy no direct financial benefit from promulgating regulations and exacting compliance. Any government fees go directly to the national treasury, and regulators have no specific stake in those fees. However, following our assumption that maximizing regulators pursue bureaucratic aggrandizement,\(^{137}\) they may strive to extend both the reach and complexity of their regulation. In this way, regulators increase their prestige and influence, and possibly their budgets. In addition, regulators may benefit important interest groups in the way securities law is structured.\(^{138}\)

Like other monopolists, the regulatory monopolist will charge a regulatory price above the competitive price.\(^{139}\) That is, it will

---

\(^{136}\) See Richard L. Revesz, Rehabilitating Interstate Competition: Rethinking the "Race-to-the-Bottom" Rationale for Federal Environmental Regulation, 67 N.Y.U. L. REV. 1210, 1234-35 (1992) (analogizing costs of environmental regulatory compliance with "sale price of a traditional good"); cf. Robert Cooter, Prices and Sanctions, 84 COLUM. L. REV. 1523, 1525 (1984) (giving examples of prices). Contrasting prices and sanctions as tools to effect legal compliance, Bob Cooter has defined a price as a payment of money that is required in order to do what is permitted. Id. at 1525.

\(^{137}\) See supra note 57 and accompanying text.

\(^{138}\) See Choi & Guzman, Portable Reciprocity, supra note 15, at 923 (describing regulator's incentive to offer popular regulatory regime in order to increase local volume of securities activity).

\(^{139}\) Issuer choice proponents argue that regulators pursue bureaucratic aggrandizement by maximizing the number of firms and volume of transactions subject to their regulation. Romano, supra note 1, at 7, quoting WILLIAM A. NISKANEN, JR., BUREAUCRACY AND REPRESENTATIVE GOVERNMENT 38-41 (1971) ("[R]egulators prefer to have within their jurisdiction more rather than fewer regulated firms and transactions."); see also Choi & Guzman, Portable Reciprocity, supra note 15, at 923 ("[R]egulators themselves benefit when many issuers and investors choose to be governed by their regulations. The regulators benefit from the increased size and importance of their own agencies.").

Besides numbers, though, the regulator will also likely care about the nature of the regulation it administers, preferring to administer complex and sophisticated regulation
overregulate.\textsuperscript{140} It will impose regulatory requirements more severe than issuers and investors would prefer. Especially in the most important capital markets, regulators will enjoy significant market power. Without ready substitutes, domestic issuers in these markets may have no alternative but to issue securities in their home markets, paying the regulator's price in terms of regulatory compliance.\textsuperscript{141}

\textsuperscript{140} The ability to charge an infinitely high price will be constrained not only by market forces—some would-be issuers may simply choose not to issue public securities—but also by politics. Issuers' costs of political action—for example, resort to legislative relief from overregulation by the bureaucracy—become relatively more attractive as regulatory pricing increases. So both exit and voice will serve to constrain regulatory pricing. See generally Albert O. Hirschman, Exit, Voice, and Loyalty: Responses to Decline in Firms, Organizations, and States (1972).

\textsuperscript{141} The regulatory monopolist's price will be set just like the traditional monopolist's price. In order to maximize its "profits," it will set its monopoly price such that marginal revenue equals marginal cost. Dennis W. Carlton & Jeffrey M. Perloff, Modern Industrial Organization 90 (3d ed. 1999). In this situation, however, the currency is bureaucratic prestige. We can think of bureaucratic "revenue" just like ordinary revenue. It will be the product of price and quantity. In other words, bureaucratic revenue will equal the regulatory price multiplied by the number of firms or transactions under regulation. Other things equal, higher revenue will translate into greater prestige and bureaucratic aggrandizement for the regulator.

On the other hand, bureaucratic "costs" must also be considered. Given fixed resources, there is a limit to the number of firms the regulator will wish to regulate. Bureaucratic aggrandizement increases with the number of firms under regulation only so long as the regulator can make a credible show of regulating. An inability to effectively regulate firms purportedly under regulation will damage the agency's prestige and influence. That is, there will be a point of diminishing returns to the regulator. Assuming a budget constraint, the regulator cannot hope to increase the number of firms under regulation indefinitely. There is a limit. Each additional firm under regulation will stretch the regulator's resources. Marginal bureaucratic revenue will equal marginal bureaucratic cost when the agency is indifferent—in terms of its own bureaucratic aggrandizement—to the addition of one more firm under regulation. Any marginal benefit in terms of prestige from regulating another firm is exactly offset by the detriment caused by the agency's diminished ability to appear competent in regulating its entire set of regulated entities.
Moreover, national securities regulators may not be content with their monopoly over domestic issuers. In pursuit of bureaucratic aggrandizement, regulators may wish to entice foreign issuers to issue and list their securities locally. But foreign issuers, less tied to the local market than domestic issuers, may be price sensitive. While major capital markets will hold some attraction for foreign issuers, those issuers may be unwilling to pay the regulatory price charged to domestic issuers for market access. Without the same hometown attachment to the local market, foreign issuers naturally have other ready alternatives to raise capital. Because of foreign issuers' higher elasticity of demand for access to the local market, the maximizing regulator should charge them a lower regulatory price than that charged to domestic issuers. The regulator will price discriminate, offering foreign issuers less stringent regulatory requirements than those applied to local issuers.

Securities regulation in the United States follows this pattern. Foreign issuers enjoy more relaxed requirements for registering public offerings in the United States. Their disclosure obligations

---


143 Identification of regulatory price discrimination as a plausible strategy for regulators in price setting jurisdictions is important to the ensuing interest group analysis because it more realistically describes the political and policy alternatives for the various interested groups than have previous commentators. To the extent issuer choice advocates have discussed the politics of issuer choice, they have tended to pose the policy alternatives in stark contrast. Private choice reform is contrasted to the status quo of mandatory disclosure, which is characterized as a monolithic endeavor by regulatory monopolists to force rules upon recalcitrant issuers. Identification of the price discrimination strategy suggests that regulators may be more responsive to market pressure and to pressure from interested groups than the standard regulatory monopolist description implies. This responsiveness tends to undermine not only claims concerning the inefficiency of the status quo but also issuer choice advocates' implicit assertion that interested groups exist that would prefer issuer choice.

144 Niskanen noted the possibility that certain bureaucracies would be able to price discriminate among customers. NISKANEN, supra note 139, at 34. See generally CARLTON & PERLOFF, supra note 141, at 287-96 (discussing price discrimination); TIROLE, supra note 142, at 137 (discussing price discrimination).

145 SEC rules define those firms that qualify for special treatment as "foreign private issuers." 17 C.F.R. § 240.3b-4(c) (2002). Any corporation incorporated or organized under the laws of any foreign country qualifies as a foreign private issuer, unless both (a) more than 50% of its outstanding voting securities are held of record directly or indirectly by U.S. residents; and (b) either (i) the majority of its executive officers or directors are U.S. citizens or residents, (ii) over 50% of its assets are located in the United States, or (iii) its business is administered principally in the United States. Id.
concerning management compensation, material transactions, and lines of business, for example, are less stringent than for domestic issuers.146 Foreign issuers are exempt from many of the rules to which domestic issuers are subject when listing shares on a national securities exchange.147 They are exempt from most of the proxy rules.148 Foreign issuers and their insiders are excused from the reporting obligations and short-swing profit rules under section 16 of the Securities Exchange Act of 1934.149 Foreign issuers’ periodic disclosure obligations are less stringent than those applied to domestic issuers.150 Similarly, even under the Sarbanes-Oxley Act, the most sweeping reform of U.S. securities regulation since its original New Deal enactment,151 foreign issuers enjoy exemptions from important requirements.152

146 Tung, supra note 21, at 1401-02. The SEC adopted three registration forms for use only by foreign issuers—Forms F-1, F-2, and F-3—in extending the integrated disclosure system. Adoption of Foreign Integrated Disclosure System, Securities Act Release No. 6437, 26 SEC Docket 964 (Nov. 19, 1982).


In general, even an issuer without publicly listed shares is required to register under the Exchange Act and be subject to Exchange Act rules if the issuer’s assets exceed $10 million, and it has a class of equity security with at least 500 holders of record. See 15 U.S.C. § 78l(g)(1) (2000) (describing registration requirement); 17 C.F.R. § 230.12g-1 (2002); 17 C.F.R. § 240.12g-1 (2002) (describing exemptions from registration). However, a foreign private issuer without publicly listed shares is exempt from Exchange Act registration and rules if it has no class of equity with more than 300 U.S. resident holders or if it furnishes the SEC the disclosure information provided in its home jurisdiction. 17 C.F.R. § 240.12g3-2 (2002).


149 Id.

150 Tung, supra note 21, at 1402-03.


152 For example, the Sarbanes-Oxley Act authorizes the SEC to promulgate rules requiring issuers to disclose on a “rapid and current basis” such additional information concerning material changes as the SEC determines “is necessary or useful for the protection of investors and in the public interest.” 15 U.S.C.A. § 78m(l) (1997 & Supp. 2004). As part of this new rulemaking authority, the SEC required issuers making any public announcement about past earnings performance to furnish a report to the SEC within five business days of the public announcement. Conditions for Use of Non-GAAP Financial Measures, Exchange Act Release No. 34-47226, at 10, 2003 WL 16117 (Jan. 22, 2003). This requirement did not apply to foreign issuers. See Dixie L. Johnson & Karl A. Groskaufmanis, FFHSJ Client Memorandum: The Post-Enron Corporate Governance Environment: Where Are We Now?
The other dominant market in the world, the United Kingdom, also appears to have followed a regulatory price discrimination strategy as to foreign issuers. The strategy seems especially important for the London Stock Exchange (LSE), since the market capitalization of overseas listed companies is nearly twice that of U.K. listed companies, and the LSE consistently has more foreign listings in absolute terms than any other major exchange. Annual listing fees are lower for overseas companies than for U.K. issuers. In its discretion, the UK Listing Authority (UKLA) may accept nonconforming financial statements from overseas applicants for listing. Similarly, the UKLA may allow an overseas applicant...
to omit certain information otherwise required in its listing particulars, depending on the nature of the regulation to which the applicant is subject in its home country. Preemptive rights, applicable to U.K. companies by virtue of the Companies Act 1985\textsuperscript{160} as well as the Listing Rules,\textsuperscript{161} do not apply to overseas companies. Overseas companies engaging in a secondary listing on the LSE enjoy relaxed reporting requirements in numerous areas,\textsuperscript{163} including those with respect to continuing obligations,\textsuperscript{164} directors' continuing obligations,\textsuperscript{165} and disclosure of major transactions.\textsuperscript{166}

Consistent with their assumed pursuit of bureaucratic aggrandizement, regulators in the strongest securities markets appear to pursue a strategy of regulatory price discrimination. These regulators will defend the territorial monopolies on which this strategy depends.

2. Other Interest Groups: Path Dependence and Increasing Returns. Regulators' druthers are not the only ones that matter. Legislators and executives influence the structure of securities law

\textsuperscript{159} Listing Rules, supra note 158, Rule 17.6.
\textsuperscript{160} Companies Act, 1985, c. b, §§ 89 & 95 (Eng.) (amended by Companies Act 1989). Under section 95, U.K.-listed companies may disapply the preemptive rights granted under section 89, but the Listing Rules and Investor Protection Committee guidelines require that any company doing so must seek a "disapplication entitlement" from its shareholders. Listing Rules, supra note 158, Rule 9.20; Investor Protection Committee, Guidelines on Pre-emption (issued Oct. 21, 1987).
\textsuperscript{161} Id. Rule 17.8. This rule apparently "disapplies" the preemption provisions of the Companies Act 1985 for overseas companies. MacNeil & Lau, supra note 155, at 802.
\textsuperscript{162} Listing Rules, supra note 158, Rule 17.14. One might suppose that from an investor protection standpoint, relaxed listing requirements for an overseas company with a secondary listing are justified since that company is already regulated by the exchange and the jurisdiction of its primary listing. However, the Listing Rules contain no general requirement that the UKLA ascertain the nature of the regulation in this primary jurisdiction or even identify the jurisdiction or the primary exchange.
\textsuperscript{163} See id. ch. 9 (describing listed companies' continuing disclosure and notification obligations).
\textsuperscript{164} See id. ch. 16 (describing listed companies' continuing notification obligations concerning, inter alia, directors' identities, directors' interests in company securities, and terms of employment).
\textsuperscript{165} See id. ch. 10 (describing notification requirements for major transactions).
as well. Legislators and executives could act to modify or abandon the current practice of territorially based prescriptive jurisdiction for securities regulation. They would be unlikely to do so over the objection of regulators, however, absent interest group support for such a change. Given its technical complexity and low visibility to the general public, international securities law is an area as to which legislators and executives are unlikely to hold strong personal preferences. Instead, they will respond to the demands of interest groups. Given regulators' significant informational and technical advantages over legislators and executives, interest groups would be required to both educate legislators and executives and spur them to action.

Important interest groups, however, have invested in and adapted to existing regulatory monopolies. They are likely to support the territorial status quo and regulatory price discrimination, not issuer choice. The long-established territorial approach to securities regulation could not help but have political effects within each nation. Not only do interest groups shape policies, but policies shape interest groups. And long-standing policies tend to strengthen interest groups that support those policies while causing opposing factions to wither.

Following the economic literature on
increasing returns and path dependence, scholars of political economy and economic history have pointed out this self-perpetuating nature of institutions. Most prominently, Douglass North has argued that institutions exhibit many of the same self-reinforcing mechanisms that induce the path dependence observed in mainstream microeconomics. For present purposes, learning effects and coordination effects are especially important in reinforcing the status quo.

a. Learning Effects. Learning effects improve a product or lower its costs the more widely the product is used. With national securities regulation, learning effects accrue over time as more issuers come under the national regulatory jurisdiction and various actors become familiar with the nuances of the system. The private

---

169 BRIAN W. ARTHUR, INCREASING RETURNS AND PATH DEPENDENCE IN THE ECONOMY 112 (1994). As Margaret Levi has explained:

Path dependence has to mean, if it is to mean anything, that once a country or region has started down a track, the costs of reversal are very high. There will be other choice points, but the entrenchments of certain institutional arrangements obstruct an easy reversal of the initial choice. Perhaps the better metaphor is a tree, rather than a path. From the same trunk, there are many different branches and smaller branches. Although it is possible to turn around or to clamber from one to the other—and essential if the chosen branch dies—the branch on which a climber begins is the one she tends to follow.


170 NORTH, supra note 110, at 94.

171 Other self-reinforcing mechanisms include high setup or fixed costs, which lead to falling unit costs as output increases; and adaptive expectations, which reflect users' desire to pick the "right" product in anticipation of future coordination benefits as others do likewise. Id. National securities regulatory systems exhibit each of these characteristics. They have large setup costs. In the most important capital markets, securities regulation is not merely a set of rules that issuers must follow. Securities regulation includes expert regulators, judges, stock exchanges that are largely responsible for proposing and imposing listing requirements on listed firms, and underwriters, lawyers, accountants, and other professional advisers to issuers. In addition, adaptive expectations emerge as increased activity under a national regulatory scheme signals the scheme's permanence.

In making the jump from products to institutions, North points out that the standard economic analysis of competing product technologies is not directly about competing technologies, but really about competition between organizations that embody the competing technologies. Id. As such, that analysis ultimately deals with organizational decisionmaking, similar to North's project of institutional analysis. See also Paul Pierson, Increasing Returns, Path Dependence, and the Study of Politics, 94 AM. POL. SCI. REV. 251, 255-56 (2000) (discussing North's contribution to institutional analysis).
actors who facilitate securities offerings and trading in established capital markets make significant investments in developing expertise related to their national regulatory systems. The availability of this expertise facilitates issuers' resort to national capital markets and the required navigation through the national regulatory system.

Those paid to advise issuers concerning regulation—primarily securities lawyers and accountants—will share similar incentives with regulators and can be expected to support territoriality and regulatory price discrimination.¹⁷² With their expertise in national securities law, lawyers have significant undiversifiable human capital investments that are more or less territorially bound. U.S. lawyers' stock in trade, for example, is their ability to advise with respect to U.S. law. They are expert at crafting disclosure documents for client firms subject to U.S. securities laws. Corporate and plaintiffs' securities lawyers are skilled at litigating class actions under the complex liability and procedural rules peculiar to the U.S. regime of private enforcement. Accountants likewise possess similar territorially bound expertise concerning financial disclosure requirements under their national securities law. U.S. accountants have developed expertise in producing and auditing the complex and detailed financial statements required of issuers under U.S. securities laws,¹⁷³ while at the same time avoiding the possible securities fraud liability that may follow an accounting misstep.¹⁷⁴ Lawyers and accountants have significant incentives to defend the status quo, including regulatory price discrimination, and to oppose issuer choice.¹⁷⁵

¹⁷² See Tung, supra note 21, at 1415 (explaining incentives to support territoriality and price discrimination).


¹⁷⁵ While law firms and accounting firms do diversify internationally, that diversification would likely have little or no effect on local lawyers' desire to maintain the existing territorial monopoly. See Tung, supra note 21, at 1417-18 (noting that because division of profits within law firms and accounting firms depends heavily on partners' ability to generate profits, individual lawyers and accountants will still wish to preserve value of their local expertise).
Stock exchanges, underwriters, and securities firms in important capital markets have somewhat different stakes. They could conceivably be tempted to support issuer choice on the promise of an increased volume of local securities activity. After all, these groups thrive on volume, regardless of whose law may apply. However, these groups also have large stakes in their current national regulatory structure. The current practice of regulatory price discrimination promises increased volume in the form of increasing numbers of foreign issuers. These various organizations may also benefit from existing informational advantages over other market participants. Mandatory disclosure in the United States, for example, is a boon to securities analysts, portfolio managers, and other securities professionals, who enjoy a host of free information about issuers that would otherwise be quite costly to assemble. For analysts in particular, issuers’ annual 10-K reports are “vital.”

These groups, no less than lawyers and accountants, have developed expertise in navigating their existing local regulatory regimes. A wholesale scrapping of the current regime might increase local volume, but it would almost certainly also imperil the value of the expertise these groups have developed under their local regimes. A switch to issuer choice might invite competition, as expertise under now-displaced territorial regimes might be less attractive to issuers and investors. On the other hand, regulatory price discrimination can promise increased volume without requiring exchanges and securities firms to forsake their local expertise. The NYSE, one outfit sure to benefit from an increase in the volume of securities sold and traded in the United States, has been a consistent advocate for the relaxation of disclosure requirements and accounting rules for foreign issuers, a position that exemplifies regulatory price discrimination. The NYSE has never voiced opposition to territorial regulation or advocated for issuer choice.

---

176 See SUSAN M. PHILLIPS & J. RICHARD ZECHER, THE SEC AND THE PUBLIC INTEREST 37 (1981), citing HOUSE COMM. ON INTERSTATE AND FOREIGN COMMERCE, 95TH CONG., REPORT OF THE ADVISORY COMMITTEE ON CORPORATE DISCLOSURE TO THE SECURITIES AND EXCHANGE COMMISSION 62 (Comm. Print 1977) (reporting 77.8% of sell-side and 91.3% of buy-side analysts indicated Form 10-K was vital to them).
177 Tung, supra note 21, at 1420, 1425.
Finally, issuers may have some political influence over the course of securities regulation. As with the other groups described above, issuers will enjoy learning effects in their current territorial regimes. Conceptually, they should oppose regulatory price discrimination, which enables their foreign rivals to pay lower regulatory "prices," but issuers seem not to have come together to voice any opposition. One might expect them to support issuer choice, which would free them to choose their own regulation. However, at least in the United States, it appears that issuers support harmonized regulation, which is exactly the opposite direction from issuer choice. The prospect of short-term switching costs may explain this lack of interest in issuer choice and support for harmonization. Incremental harmonization preserves existing learning effects for issuers, while also evening out regulatory costs with foreign rivals.

b. Coordination Effects. Securities offerings and trading in established capital markets depend on a thick institutional environment. Coordination effects may therefore be especially important for generating increasing returns and reinforcing the status quo. Coordination effects confer benefits to existing users in a system as new users adopt the system. Issuers and investors are the users of securities markets and securities laws. And the private interests discussed above—the lawyers and accountants, the exchanges and underwriters and securities firms—offer services that are complementary to securities markets and to each other. The size and importance of established securities markets are likely to increase over time, and the influence of these private interests will correspondingly grow.

Each issuer benefits from the existence of other issuers with securities trading in a market because more issuers attract more investors. A symmetrical analysis applies for investors. As more

178 See id. at 1425 (describing lack of opposition to regulatory price discrimination).
180 See Tung, supra note 21, at 1423 (describing problem of short-term switching costs).
181 NORTH, supra note 110, at 94.
and more issuers sell and list their securities in established markets, the markets draw more and more investors. Drawing more investors in turn makes the markets more attractive to existing and subsequent issuers and, in turn, to existing and subsequent investors.

Private interests with stakes in the system will benefit from this growth as demand for their professional services increases. This increased demand will draw more resources to these service enterprises. It will also likely generate increasing economies in the provision of these services.¹⁸² In addition, the complex institutional environment for securities regulation may generate increasing returns at a macro level among the complementary public institutions and private organizations that effect securities regulation and securities activity in established markets.

In the United States, for example, securities regulation relies not only on legislation, but on an array of public and private actors to promulgate rules, police compliance ex ante, and impose penalties for violations ex post. The SEC is the central institution with expertise developed over many decades. The SEC has authority over civil enforcement actions, while criminal matters are referred to the Department of Justice.¹⁸³ In addition, the SEC's ex ante oversight is crucial. The detailed guidance that results from the interaction of SEC staff with private securities lawyers through rule proposals and the public comment process, SEC releases, no-action letters, and more informal contacts has created not only a sophisticated and relatively determinate body of regulation, but also a knowledgeable cadre of private advisers and regulatory staff.¹⁸⁴ Stock exchanges, the National Association of Securities Dealers (NASD), and other self-regulatory organizations also play important roles by making and enforcing rules with respect to their

¹⁸² Increasing economies in the provision of securities law are also likely. In the context of product competition, Paul David has referred to this phenomenon as "system scale economies." See Paul A. David, Clio and the Economics of QWERTY, 75 AM. ECON. REV. 332, 335 (1985) (describing decreasing cost conditions as typewriting system converged to QWERTY keyboards).

¹⁸³ See HAZEN, supra note 174, § 16.2[8].

¹⁸⁴ See generally id. § 1.0[2] (describing formal and informal interaction between SEC and private securities bar).
members.\textsuperscript{185} Stock exchanges also impose listing requirements on their listed companies and are responsible for their enforcement.\textsuperscript{186} Private actions, some expressly provided by statute and others implied by courts,\textsuperscript{187} also provide enforcement punch. These private actions are inextricably tied to the courts and the rules of procedure regarding class actions. Courts therefore matter a great deal. Complementing this mosaic of regulatory institutions is a corps of professional advisers with expertise in navigating issuers through this system. The lawyers understand the system. The accountants understand the system. The underwriters do as well.

Actors across these various institutions and organizations have developed coordinated approaches to enabling securities activities and effecting securities laws. Well-worn practices already exist among regulatory and enforcement entities, among regulators and issuers and their professional advisers, and between regulators and stock exchanges. The pieces all fit together, more or less. The interaction over time among these various institutions and organizations has generated significant coordination effects, and growth in important capital markets will further enhance coordination benefits.

Given this well-developed expertise and coordination, peculiarly tailored for the existing institutional context, private actors benefit from the continuing existence of regulatory monopoly and regulatory price discrimination. Growth in important capital market countries is likely to lead securities regulation even further down the territorial path. As private interests prosper under territoriality, they will have stronger incentives and more resources to defend territoriality in the political arena. Besides being well financed and well organized, members of these private groups have both undiver-

\textsuperscript{185} Other self-regulatory organizations include the Public Company Accounting Oversight Board, formed in 2002 as part of the Sarbanes-Oxley Act to supervise public auditors and oversee standard setting for auditing, and the Municipal Securities Rulemaking Board, which sets rules of conduct for municipal securities brokers and dealers.

\textsuperscript{186} See supra notes 147-66 and accompanying text.

sified human capital investments and high per capita stakes in territoriality and regulatory price discrimination. They are likely to be quite effective in supporting this status quo.

Because of the large and long-standing investment that regulators and other interested groups have in their national regulatory regimes in important capital markets, territoriality and regulatory price discrimination are likely to persist. The U.S. corporate charter competition story and the emergence of the internal affairs doctrine among U.S. states offer no countervailing prospects. Choice of law rules respecting private choice in international securities regulation are unlikely.

V. THE GLOBAL MARKET FOR SECURITIES LAW

The foregoing discussion highlights the difficult choice of law cooperation that would be necessary for an international issuer choice system to emerge. Choice of law cooperation, however, is only the first serious obstacle. Even if domestic political entrenchment could be overcome such that important jurisdictions were willing to forfeit their existing territorial monopolies in favor of direct competition, there is still the question of whether and how nations might actively compete to offer desirable securities regulation. In the remainder of the Article, I consider other impediments to direct competition. Even assuming that nations could get past the problem of choice of law coordination, several other problems would plague an international issuer choice arrangement that are not addressed by the dominant U.S. corporate law regulatory competition story. Most importantly, there is likely to be a dearth of nations with both sufficient incentive and sufficient capacity to compete over securities law, an issue I address in this Part. In addition, enforcement of an issuer-chosen foreign regime would be messy. However law-giving and law-enforcing institutions were combined, the promulgating state would likely have only imprecise

---


189 See infra notes 192-95 and accompanying text.
control over implementation of its law in foreign nations. This would lead to legal indeterminacy that would impede competition. I discuss enforcement issues in Part VI.\(^\text{190}\)

Given these impediments, as well as the costs of opting out of home country law, issuers might not be willing to do so. They might just stay home. A switch to issuer choice would necessarily have to start where territorial regulation left off. So in its inception, competition over securities law would involve enticing issuers, primarily from established capital market countries, to abandon their home country regulatory regime in favor of a less familiar foreign regime. But if competition is weak and application of foreign law is indeterminate, even given the choice, issuers might not be willing to forsake home country law. Issuers understand their home country regime the best, as do their most likely investors. Issuers also enjoy political influence in their home country that they are unlikely to enjoy abroad, so they may be able to influence local regulation to their liking. Moreover, home country investors—an issuer's most likely investors—might impose a heavy discount on the securities of local issuers opting out of home country securities law. Investors' bias for their home country issuers may include a bias for home country law as well. Part VII elaborates on these predictions.\(^\text{191}\)

A. THE DEARTH OF COMPETITORS

The brief for welfare-enhancing corporate charter competition among U.S. states turns crucially on specific political and institutional factors, but the context for international competition over securities law is quite different. National securities regulators have different political opportunities and face different institutional constraints than U.S. state legislators. The structure of the hypothetical global market for securities law would also look very different from the U.S. corporate charter market. Given the structure of the market and the institutional constraints facing regulators, it is difficult to imagine many nations with both

\(^{190}\) See infra notes 318-29 and accompanying text.

\(^{191}\) See infra notes 330-44 and accompanying text.
sufficient incentives and sufficient capacity to compete internationally over securities law.

Established capital market countries would enjoy first-mover advantages, which can be critical in knowledge industries,\textsuperscript{192} including law. But these wealthy nations would have difficulty demonstrating a credible commitment to maintaining responsive regulation for their issuers—a key factor in explaining Delaware's success in U.S. corporate charter competition.\textsuperscript{193} The established capital market countries have public budgets that are too large to be able to show fiscal dependence on regulatory revenues.\textsuperscript{194} Moreover, given the relatively paltry amounts at stake in a global market for securities regulation, even smaller countries would run into similar credible commitment problems.\textsuperscript{195} The smallest countries have public budgets that might be small enough for regulatory revenues to matter, but these countries would have other problems. These smallest countries lack the expertise and administrative capacity to offer competitive securities law. Their smaller economies might make it difficult for them to shoulder the costs of new entry or increased investment in an unfamiliar market, especially given the possibility of entry-deterring strategies by their larger competitors.

Long-run competitors would be hard to find. Without long-run competitors, a global market for securities law would be thin and unsuccessful. This unattractive market for law would not entice issuers to opt out of their home country law. It would fail to generate competitive pressure on regulators. Below, I first explain the importance of credible commitment in the global market for securities law before considering various potential competitor nations.


\textsuperscript{193} See infra notes 196-201 and accompanying text.

\textsuperscript{194} See infra notes 211-21 and accompanying text.

\textsuperscript{195} See infra notes 271-82 and accompanying text.
A crucial aspect of the Delaware success story relates to Delaware's unique ability to demonstrate a credible commitment to its domestic corporations regarding the continuing quality of Delaware corporate law. The "law as a product" simile recognizes the relational aspect of the corporate charter. The corporate charter is not a good quickly consumed, but instead represents a relational contract between a corporation and its state of incorporation. A corporation expects to rely on the law of its state of incorporation indefinitely. A successful seller of corporate charters, like Delaware, must therefore demonstrate a credible commitment to prospective subscribers that it will forego postcontractual opportunism. Rather than altering corporate law rules to take advantage of captive corporations, the state will instead have to demonstrate its ongoing fidelity to its domestic corporations' changing needs, striving to offer and to maintain efficient law that maximizes firm values.

As earlier described, the U.S. charter competition story explains competition among U.S. states as being largely motivated by states' pursuit of chartering revenues. According to Romano, Delaware's success in the charter market turns in large measure on its relative dearth of alternative revenue sources and its resulting dependence on chartering revenues. This fiscal dependence signals Delaware's commitment to be responsive to the needs of its incorporated firms. Because of the significance of chartering revenues to Delaware's state budget, Delaware has much to lose by failing to be responsive. Its fiscal vulnerability is ironically also a source of its strength in the charter market. Delaware is effectively "a hostage to its success."

Delaware has also made specific investments in developing its specialized chancery court and a sophisticated and extensive body of corporate case law. These function-specific assets are said to

---

196 While some corporations may later reincorporate in a different state, few corporations contemplate such a move at the time of initial incorporation.
197 See supra note 43 and accompanying text.
199 Id.
provide further evidence of Delaware's commitment to offering optimal law. Because of the chancery court's specialized corporate law function, the chancery court has no value to Delaware in any other context. Likewise, case law precedents are only valuable if Delaware continues to attract significant corporate law adoptions. As with Delaware's fiscal dependence on chartering revenues, these specific investments serve as a hostage to Delaware corporations that enables Delaware's credible commitment to maintain optimal law.

Issuer choice proponents do not directly address the question of nations' credible commitment in selling securities regulation. Given the obvious parallels in the relational aspects of corporate and securities law, however, consideration seems warranted. Commitment devices may be even more crucial in international competition over securities regulation. In general, the necessity for commitment mechanisms depends on whether exit costs are high or low. If exit costs are low—i.e., if corporations can reincorporate at low cost, if issuers can switch regulatory regimes at low cost—then subscribers can easily unsubscribe. This threat of easy exit may mean that no additional commitment device is needed. The threat of exit is itself sufficient to curb supplier opportunism. But firms' switching costs are likely to be at least as high in international securities regulation as with U.S. corporate law. Corporate law is fairly uniform across U.S. states, so in the face of opportunistic corporate law "reform" by one state, or a state's mere inattention to firms' changing needs, firms incorporated there may easily find a suitable substitute. Reincorporation might entail some administrative and filing costs, but it is doubtful that those costs would be a serious deterrent for publicly traded companies.

Switching from one nation's securities regulatory regime to another, however, may be less straightforward. Securities laws across nations are much less similar than are corporate law regimes across U.S. states. Switching securities law may therefore entail a

200 Id. at 40.
201 Id. at 39-40; see also Oliver E. Williamson, Credible Commitments: Using Hostages to Support Exchange, 73 AM. ECON. REV. 519, 519 (1983) (asserting that hostages are often used to create credible commitments).
202 See Black, supra note 44, at 586-87 (arguing that reincorporation costs are low).
more drastic set of changes for a firm than reincorporation from one U.S. state to another. This discontinuity across regimes may make it more difficult for firms to switch. Firms would have to gain familiarity with the laws and administrative practices of another country. This may not be an easy task. Although firms can simply purchase professional advice on the relative merits of alternative regimes, much like a U.S. firm might do when it reincorporates, integrating a new securities regulatory regime into the firm’s existing legal and operational arrangements may be messy. New or different reporting requirements, for example, may have operational consequences. The fit between the new securities regime and the firm’s existing culture or legal commitments may also be awkward. Because of issuers’ high switching costs, it would be

203 Choi and Guzman have suggested that small nations may design regimes that are only “incrementally different” from larger countries’ regimes “in clear and easy to understand ways.” Choi & Guzman, Portable Reciprocity, supra note 15, at 934. This strategy, the analysis goes, would improve smaller countries’ chances of being successful sellers in the international market for securities law, since it would reduce issuers’ and investors’ costs of learning about the new regime. Id. Choi and Guzman offer the example of a small country copying the U.S. regime minus insider trading prohibitions. Id. This approach is not likely to create a comprehensive regime that is only “incrementally different” from the U.S. regime because the U.S. regime and those of other major capital markets consist of more than simple rules on paper. These regimes include expert administrative agencies and complex institutional relationships among government institutions, self-regulating organizations, and private firms and their professional advisers. See supra notes 145-66 and accompanying text. Without the ability to duplicate these other aspects of the regulatory infrastructure, not to mention such intangibles as legal culture, a small country’s knock off will not likely resemble the original very much.

204 For example, German accounting rules allow far more leeway for firms to manage their earnings reports than do U.S. rules. Daimler-Benz felt the sting of U.S. reporting requirements when it decided to list its shares on the NYSE in 1993. Daimler’s shares had been listed only in Germany before 1993. Reporting under U.S. securities laws and U.S. generally accepted accounting principles (GAAP) made transparent Daimler’s practice under the more liberal German accounting rules of smoothing out earnings from year-to-year by hiding earnings as reserves in the more profitable years and then drawing on those reserves in less profitable years to boost earnings. The contrasting results of these accounting rules was made clear in the very first year of Daimler’s U.S. listing, when it reported a $354 million profit under German accounting standards, but a loss of $1 billion under U.S. GAAP. James D. Cox, Regulatory Duopoly in U.S. Securities Markets, 99 COLUM. L. REV. 1200, 1203 (1999). The permission or prohibition of this sort of flexible earnings management may affect operational decisions.

205 For example, post-Enron reform in the United States relies heavily on an expanded role for independent directors to improve corporate accountability. See, e.g., 15 U.S.C.S. §§ 78f, 78j-1 (2004) (requiring, under Sarbanes-Oxley Act, that all audit committee members be independent directors); NYSE LISTED COMPANY MANUAL § 303A.01 (requiring that all listed companies’ boards include majority of independent directors); id. §§ 303A.04-.06
critical for countries to solve the commitment problem in order to be competitive in an international market for securities law.

C. ESTABLISHED CAPITAL MARKET COUNTRIES

In an issuer choice world, established capital market countries would enjoy enormous first-mover advantages in terms of selling securities law. U.S. securities regulation alone currently applies to about half the world's stock market capitalization. Adding Japan, the United Kingdom, Germany, and the Euronext countries, these few countries account for and regulate 75% of the world's stock market capitalization. Besides an installed base of issuers and investors, established markets also enjoy established securities regulation, mature regulatory agencies, sophisticated exchanges, and expert securities professionals to advise issuers. It appears that these nations start with crucial advantages in a global competition to sell securities law.

However, these first movers may not have sufficient incentive to compete to offer efficient securities regulation. Their wealth and

(requiring, under Sarbanes-Oxley Act, that each list company have nominating-corporate governance committee, compensation committee, and audit committee composed entirely of independent directors). However, as Amir Licht has noted, independent directors may be less useful in this regard in East Asia because of the cultural norm of conformity. Licht, supra note 127, at 224.

206 SCOTT & WELLONS, supra note 153, at 3.
207 Euronext was formed in 2000 with the merger of the Paris, Brussels, and Amsterdam exchanges. Euronext, History, at http://www.euronext.com/editorial/wide/0,4615,1732_4427342,00.html (last visited Nov. 10, 2004). At the beginning of 2002, Euronext also acquired Portugal's main exchange, the Bolsa de Valores de Lisboa e Porto, as well as the London International Financial Futures and Options Exchange. Id.
208 At the end of 2002, domestic market capitalization for these major markets were as follows (in trillions of U.S. dollars):

<table>
<thead>
<tr>
<th>Country</th>
<th>Market Capitalization</th>
</tr>
</thead>
<tbody>
<tr>
<td>United States</td>
<td>$11.0</td>
</tr>
<tr>
<td>Japan</td>
<td>2.1</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>1.8</td>
</tr>
<tr>
<td>Euronext</td>
<td>1.5</td>
</tr>
<tr>
<td>Germany</td>
<td>.69</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>$17.09</strong></td>
</tr>
</tbody>
</table>

World market capitalization at the end of 2002 was approximately USD $22.8 trillion. WORLD FEDERATION OF EXCHANGES (FIBV), MARKET CAPITALIZATION OF SHARES OF DOMESTIC COMPANIES, tbl. 1.3B (Apr. 25, 2003), http://www.world-exchanges.org/publications/TA1302.pdf [hereinafter FIBV tbl. 1.3B].
economic diversification mean that, unlike Delaware with its corporate chartering business, their governments and economies do not depend on success in the market for securities law. Without this dependence, these first movers may be unable to demonstrate a commitment to maintaining desirable regulation. Even if national regulators might wish to offer popular regulation in order to expand their regulatory purview, their pursuit of this end may be constrained by legislatures' indifference or even opposition.

1. Regulators' Constraints. In the issuer choice world, vigorous competition over securities regulation is assumed to be driven by regulators' pursuit of their own bureaucratic aggrandizement. Their drive to maximize the number of firms and the volume of transactions under their regulatory supervision will spur them to offer efficient law. Even granting this assumption, however, there is a step missing. Issuer choice proponents implicitly assume that nations could agree to radical choice of law reform to enable issuer choice and that all else would remain the same. In particular, regulators would continue to dominate securities regulatory policy. Were this so, regulators’ posited pursuit of bureaucratic aggrandizement might be sufficient to achieve some measure of competition. But all else is not likely to remain the same. Regulators’ latitude to pursue their own agendas is likely to be constricted in this parallel universe of issuer choice. Legislatures will likely matter.

The first half of this Article explained regulators’ dominant role in setting policy on international securities regulation and their opposition to choice of law reform allowing issuer choice. However, in this Part, I assume—counterfactually and against all odds—that choice of law coordination could be achieved. But if it could happen, presumably it would happen only over regulators’ strenuous objection. In this alternative universe, it is unlikely that regulators would dominate securities regulatory policy in the way they now do. Given the massive switch in the basic rules of prescriptive jurisdiction for national securities law, it is far more likely that legislatures will have gotten involved and made their influence felt in order to effect this fundamental change. Therefore,

209 See supra note 57 and accompanying text.
210 See supra notes 135-66 and accompanying text.
the simple assumption of regulators' pursuit of bureaucratic prestige must be supplemented in order to be able to predict vigorous competition over securities law. The behavior and influence of legislatures must be considered. Why would legislatures care to compete or allow agencies to do so? And how would legislatures demonstrate a credible commitment to staying competitive?

2. **Victims of Prosperity.** Legislatures in prosperous countries have no strong revenue incentives to support efforts by regulators to offer popular securities law under issuer choice. Regulators may be able to show some strong interest in maximizing subscriptions to their rules, but their ability to demonstrate commitment is limited. Any commitment will always be subject to legislative fiat, and the legislatures will not likely be able to demonstrate a credible commitment at all. Legislatures lack the specific interest in bureaucratic aggrandizement that is assumed to drive regulators. Instead, legislators will have broader interests in mind.

Adopting the revenue maximization goal that purports to explain Delaware's success suggests that only nations with relatively small budgets would be in a strong position to demonstrate a convincing commitment to supply and maintain optimal securities law. Only those nations that could show significant dependence on subscriber revenues from their securities law would be able to give issuers sufficient assurance of their intent to maintain desirable law and to disavow opportunism.\(^{211}\)

While Delaware may be a hostage to its own success,\(^{212}\) prosperous nations are victims of their own prosperity. Prosperous nations simply do not have sufficient dependence on their existing and prospective securities law revenues to offer a credible commitment.

---

\(^{211}\) This focus on Delaware is not untoward. While Delaware is nominally only one of many competitors for corporate charters among U.S. states, scholars on all sides of the debate seem to agree that the market for corporate charters is in reality a series of distinct bilateral markets in which each state competes with Delaware to retain its home corporations. See supra note 47. Ninety-seven percent of all public companies are incorporated either in their home state or in Delaware. Daines, supra note 47, at 1562. So Delaware is the competition. Moreover, many of the features that help explain Delaware's success in this competition also apply to New Jersey at the end of the nineteenth century, when it was the dominant exporter of corporate charters among U.S. states. GRANDY, supra note 115, at 79-80.

\(^{212}\) See supra note 199 and accompanying text.
Similarly, their existing investments in securities regulation and related institutions are probably not large enough relative to their enormous economies to make these institutions credible hostages. In fiscal year 2002, for example, the SEC collected fees of around \$1 billion,\textsuperscript{213} not a trifling sum but still only 0.05\% of the $2 trillion national budget.\textsuperscript{214} Loss of SEC revenues to the U.S. Treasury would not even cause a ripple in the overall budget. Likewise in the United Kingdom, the FSA took in £208.8 million in fees in fiscal year 2002-03.\textsuperscript{215} This amounted to a mere 0.05\% of the roughly £400 billion in U.K. government revenues that fiscal year.\textsuperscript{216}

And while the United States can boast of significant specific investments in its securities laws—an expert agency, case law, rules and forms, regulatory conventions memorialized in SEC releases and no-action letters—these specific assets would not seem to be useful as hostages without the fiscal dependence central to explaining Delaware's success.\textsuperscript{217}

It is very unlikely that lawmakers in prosperous nations would be willing to sufficiently augment investment in their regulatory institutions in order to demonstrate commitment to and dependence on the sale of securities law. With large, strong, and diversified


\textsuperscript{215}2002/03 Financial Services Authority, FSA Ann. Rep. 2002/03 115 (2003). These numbers overstate the significance of U.K. securities regulation as a proportion of overall government revenues since the FSA regulates all financial services in the United Kingdom, not only securities markets. The FSA regulates insurance companies, deposit taking institutions, and investment businesses, and it is also responsible for educating consumers about financial services. Inside the FSA: What the FSA Is All About, at http://www.fsa.gov.uk/media_centre/what_the_fsa_is_all_about.html (last modified July 28, 2003).


\textsuperscript{217}The extent of hostage regulatory assets in the United Kingdom is less clear given that the formal FSA regime is relatively new. See Elis Ferran, Examining the United Kingdom's Experience in Adopting the Single Financial Regulator Model, 28 Brook. J. Int'l L. 257, 273-76 (2003) (describing FSA's gradual, informal, ad hoc assimilation of other existing regulatory agencies beginning in 1997).
economies, it would be futile for those lawmakers to attempt to demonstrate dependence on regulation-related revenues. In a related context—proposed national corporate chartering in the United States—Romano has noted this same problem: "Given the sheer size of the federal budget, there would be no revenue incentive to constrain the national government from behaving opportunistically by, for instance, installing high franchise fees without delivering laws that corporations prefer."\(^\text{218}\)

Issuers and investors might readily believe that a regulatory agency would be responsive to their needs as a matter of the agency's own survival and its pursuit of bureaucratic aggrandizement.\(^\text{219}\) But the agency might not be able to convince issuers and investors that the legislature cares about the agency's survival or its ability to sell securities law. Given the right corporate scandal, legislators might easily respond to public pressure to enhance investor protection, rather than simply acquiesce to regulators' pursuit of maximum adoptions for bureaucratic aggrandizement.\(^\text{220}\) For example, legislatures may mandate higher disclosure or tinker with corporate governance rules.

In a prosperous nation, legislatures will have credible commitment problems, and regulators will have insufficient influence over their legislatures to assure efficient securities law. The whole issuer choice program aims to diminish the power of regulators by dismantling their territorial monopolies. Having lost the critical fight to preserve its territorial jurisdiction, such an agency would seem to have only very weak influence with its legislature.\(^\text{221}\) And

\(^{218}\) ROMANO, supra note 43, at 48.

\(^{219}\) Unlike legislators or other national policymakers, the regulator may not see any direct financial benefit from maximizing subscriber revenues. Whatever fees are collected will likely go into the national treasury to be doled out by national legislators without regard to the wishes of regulators. Certainly this will be true in the United States. Regulators will view themselves as merely contributing to a common pool of revenues, the ultimate distribution of which will be out of regulators' control and as to which they are likely to have almost no say. In these contexts, regulators are much more likely to pursue their own bureaucratic goals and not national revenue maximization.

\(^{220}\) See infra notes 237-52 and accompanying text.

\(^{221}\) The same goes for the lawyers, accountants, and other interest groups who benefit from regulatory monopoly, regulatory price discrimination, and increased securities activity under their domestic regime. Their interests would generally align with regulators' desire to maximize adoptions of their local system in an issuer choice world. There is some doubt, however, that these groups, having lost the fight over choice of law, would retain sufficient
if issuer choice advocates are correct that previously overregulated issuers would figuratively flee to less restrictive jurisdictions once given a choice of regulatory regime, the influence and prestige of former regulatory monopolists would be diminished even further.

3. Private Interests and Political Equilibrium. If revenue incentives could not drive legislatures in prosperous countries to pursue and maintain programs for popular securities law or enable them to demonstrate a credible commitment to such programs, perhaps private interests could play a remedial role in these regards. Groups with financial stakes in their national securities industry might be able to persuade legislators to support regulators in selling securities regulation. These interests probably stand to benefit from issuers’ adoption of their local regulatory regime on the theory that issuers adopting a given country’s regulation are likely to issue and list their securities in that jurisdiction as well. All other things equal, a jurisdiction with popular law will likely enjoy a higher volume of securities activity than one without. And these private interests benefit from increased volume. The profits at stake for these groups may be significant. It might be worth their while, therefore, to lobby legislatures to pursue—or at least to permit—regulation that would attract local securities activity.

The influence of private interests, however, may not be sufficient to guarantee regulation that would be consistently responsive to issuers’ desires. Credible commitment problems may therefore persist. While private interests will generally favor rules that issuers are likely to want to adopt, the preferences of these various interests over the legislature to offer a credible commitment to continued responsiveness to issuers’ and investors’ needs.

222 Investors in the issuer-selected jurisdiction will be familiar with the regulatory regime and will likely be receptive to the issuer’s securities. Choi & Guzman, Portable Reciprocity, supra note 15, at 923.

223 See supra notes 167-88 and accompanying text.

224 If the U.S. experience is any guide, revenues from advisory and other services could run into the billions. In 1999, the then-Big 5 accounting firms collectively audited about three-quarters of all U.S. public registrants. PUBLIC OVERSIGHT BOARD PANEL ON AUDIT EFFECTIVENESS, REPORT AND RECOMMENDATIONS 181-82 (Aug. 31, 2000). These accounting firms collected approximately $9.5 billion that year for accounting and auditing services. Id. This measure is concededly rough. In addition, it reflects private revenues based on regulatory monopoly. With competition over law, presumably costs of compliance would factor into any issuer’s choice-of-law decision. One would therefore expect downward competitive pressure on private revenues.
interest groups will not be uniform. Stock exchanges, for example, may be pure volume players—they may care only about the volume of local securities issuance and trading. Lawyers and accountants, by contrast, might wish for more complicated rules and requirements within their respective areas of expertise. The optimal level of regulation for generating legal and accounting fees is likely to be higher than for simply maximizing volume. More complex regulation would increase expected fee revenues, even if it might drive some issuers to other jurisdictions with less costly regulation. Lawyers and accountants would be willing to sacrifice some amount of local securities activity in pursuit of higher aggregate fees.225

The actual contours of regulation would turn on the political equilibrium among these groups, along with regulators' input. But this competitive equilibrium would not necessarily be consistent or stable. Small perturbations in the composition of the legislature or regulatory body or other important offices may affect the relative influence of various interest groups and the course of regulation.226

Even more significant for the instability of any given political equilibrium is the presence of other interest groups with the potential to influence regulation in particular issue areas. The prosperous countries with developed securities markets are liberal democracies that enjoy diversified economies. This environment generally spawns a plethora of well-organized, well-financed interest groups ready to mobilize to address issues of particular concern. Labor unions, for instance, may have no stake in the general contours of securities law, but they may mobilize to address specific concerns. In the United States, following the massive fraud-related losses sustained by company pension plans from the collapse


226 In the United States for example, a switch of the majority party in the Senate or the House of Representatives results in a change in committee chairs. Committee chairs may be extremely influential in affecting the course of legislation, and with respect to securities regulation, Democratic chairs are likely to support increased regulation, while Republican chairs tend to disfavor it. In addition, the President appoints commissioners to the SEC. 15 U.S.C. § 78d(a) (2000). A new President has significant power to change the direction of the Commission through this appointment power. Commissioners serve five-year terms, with one seat on the Commission becoming vacant each year. Id.
of Enron and others, unions have become visible advocates not only for reform of pension plan rules but also for corporate governance reform through federal securities law. The AFL-CIO has petitioned the SEC to change the proxy rules to allow shareholder nominees for boards of directors. Unions have been extremely active with shareholder resolutions, peppering issuers with reform proposals to be considered by shareholders at issuers' annual meetings. Proposals offer fundamental reform on auditor independence and director accountability and curbs on executive pay. In 2002, following Enron's demise, unions were responsible for 40% of all shareholder proposals, far more than any other institutional investor. This represented a marked increase from unions' past activities as shareholder proponents. Unions have also been strong backers of newly enacted SEC rules requiring mutual funds to disclose their proxy voting practices and voting records.

Related to this abundance of effective interest groups, the general public in prosperous countries may also affect the course of securities regulation. While securities law is not a subject widely followed by the general public, and most people do not stay informed about


229 Weiss et al., supra note 228, at 116.

230 Amy Borrus & Paula Dwyer, Getting the Boss to Behave: Big Labor has Led the Charge for Corporate-Governance Reform, BUS. WK., July 15, 2002, at 110.

231 Weiss, supra note 228, at 116.

232 Id.

233 Borrus & Dwyer, supra note 230, at 110.

it or have strong opinions on it, a momentous scandal or other cataclysmic event may place securities regulation on the "public agenda." Then securities regulation becomes front-page news. Citizens may be affected as shareholders or employees. Citizens and the popular media may agitate for change in the face of the latest crisis. They may closely monitor the actions of policymakers. In this context, public pressure may overcome the influence of even well-organized and well-financed interest groups. Reform in the direction of popular sentiment may win the day. This reform is most likely to involve stronger investor protection. It is not likely to track issuer preferences, efficiency, or a securities volume-maximizing strategy.

The Sarbanes-Oxley Act offers only the most recent example of regulatory reform driven by the public agenda. Public outrage at public company management began with accounting scandals, but has since widened to include high profile insider trading,

---


Those not specially affected by regulatory information do not ordinarily invest in acquiring it. However, at any given time in any given polity, there is a small set of issues that has become the object of intense public attention. These issues are very widely attended to. They are covered in virtually every issue of every printed news medium, and are reported on constantly by the broadcast media. These issues pervade the information atmosphere . . . . Let us call the set of these issues the "public agenda."

Id.

236 More generally, to the extent that the desires of the general public regarding securities law diverge from efficiency—a not unlikely condition—then policymakers in an issuer choice world would depend on political slack to accomplish their volume-maximizing strategy. See id. at 192 (explaining slack-reducing effect and consequences of putting issue on public agenda).


238 See, e.g., Constance L. Hays, Judge Declines to Dismiss 2 Charges in Stewart Case, N.Y. TIMES, Nov. 19, 2003, at C3 (discussing charges against Martha Stewart); SEC Sues Two Other Waksals in ImClone Case, L.A. TIMES, Oct. 11, 2003, at C3 (discussing insider trading cases involving Waksal & Stewart).
sive executive compensation,\textsuperscript{239} fraud by brokerage firms\textsuperscript{240} and improper trading of mutual funds.\textsuperscript{241} With its fundamental corporate governance reforms,\textsuperscript{242} the Act undoubtedly raises compliance costs for public firms. One estimate suggests the largest firms will spend an average of $4.7 million in out-of-pocket costs in the first year of compliance just to implement required internal controls.\textsuperscript{243} Other increased cost estimates range from $1 to 3 million, depending on the size of the firm.\textsuperscript{244} Some U.S. companies have responded by delisting and going private.\textsuperscript{245} Foreign issuers have also been deterred from coming to the United States. Shortly after passage of the Sarbanes-Oxley Act, Porsche AG of Germany and Benfield Group Ltd., a British insurance concern, abandoned plans to list their securities in the United States, citing specific concerns about the Act.\textsuperscript{246} Daiwa Securities and Fuji Photo Film of Japan also delayed listing their securities in the United States because of the unsettled regulatory environment.\textsuperscript{247}

In the United Kingdom, the current regulatory structure emerged from scandal-ridden circumstances as well. The FSA was created

\begin{footnotesize}
\begin{itemize}
  \item \textsuperscript{239} Richard Grasso was forced to resign as the head of the NYSE after his $187.5 million retirement package was publicly disclosed. Prominent members of the board of directors soon followed with their resignations. Laurie P. Cohen et al., \textit{NYSE's Reed Scraps Report, Plans New One: A Top-to-Bottom Examination Is Set of Exchange's Governance; Lead Director McCall Resigns}, \textit{WALL ST. J.}, Sept. 26, 2003, at C1.
  \item \textsuperscript{240} Weiss et al., supra note 228, at 116.
  \item \textsuperscript{241} Laura Johannes et al., \textit{Fraud Charges Widen Scope of Scandal Facing Mutual Funds}, \textit{WALL ST. J.}, Dec. 12, 2003, at C1.
  \item \textsuperscript{242} See supra note 152.
  \item \textsuperscript{244} \textit{A (Going) Private Matter: To Be a Public Company, or Not to Be?}, \textit{ECONOMIST}, Mar. 22, 2003, at 58.
  \item \textsuperscript{247} Craig Karmin, \textit{Foreign Firms Lose Urge to Sell Stock in U.S.}, \textit{WALL ST. J.}, July 24, 2003, at C1.
\end{itemize}
\end{footnotesize}
to be the super regulator for all financial services in the United Kingdom, including not only securities and futures trading, but also deposit-taking institutions, insurance firms, and investment businesses. The FSA was formed on the heels of several high profile financial scandals, including Robert Maxwell’s multimillion dollar misappropriation of his company’s pension funds and a major scandal involving the mis-selling of pension investment products. Both episodes were traced to regulatory failures under a system largely dependent on self-regulating organizations. As under the Sarbanes-Oxley Act in the United States, regulated entities under the relatively new FSA have expressed fears of higher regulatory costs, a fear that even the FSA has acknowledged.

In prosperous countries with established securities markets, then, the political equilibrium for securities law is subject to disruption from several sources. Even the groups that depend on active securities markets for their livelihood have somewhat differing stakes in the structure of regulation. They will not always agree on the straightforward volume-maximizing strategy that purportedly results in responsive and efficient regulation. Other interest groups in prosperous countries may also emerge to affect particular issue areas in ways that may be difficult to predict ex ante. Even the general public may weigh in on those relatively rare occasions when securities regulation makes it to the public agenda.

Contrast this with Delaware’s political economy. Most of Delaware’s chartering revenues come from large corporations located out-of-state. Because these corporations’ headquarters, operations, assets, and employees are in other states, interest groups that might otherwise affect the development of corporate law have no purchase in Delaware. Labor, environmental, and

---

248 See supra note 215.
249 Ferran, supra note 217, at 267-68.
250 Id. at 288.
251 DAVID LASCELLES, WAKING UP TO THE FSA: HOW THE CITY VIEWS ITS NEW REGULATOR 17-18 (2001); Ferran, supra note 217, at 287.
253 Macey & Miller, supra note 225, at 490.
254 Id.
community interests focus their energies and influence on the jurisdictions in which firms operate, and not on the state of incorporation. And to Delaware's general public, chartering revenues are an unqualified boon with few if any countervailing costs.

Without a strong revenue incentive to unite legislators and drive them to back popular and responsive securities law, prosperous countries will have difficulty demonstrating a credible commitment to maintaining efficient and responsive securities regulation. The existence of multiple domestic interest groups that may affect securities regulation highlights the inability of policymakers to bond themselves to offering responsive rules. The same economics that render a prosperous country unable to demonstrate a commitment to maintaining optimal securities law also suggest why legislatures in those countries would be disinclined to pursue regulatory revenues at all.

D. CAPACITY VS. COMMITMENT: PROBLEMS FOR SMALLER NATIONS

If the foregoing observations are correct, then smaller, economically less diversified nations would seem in some respects best positioned to be able to compete in an issuer choice world. Their economic conditions would seem to give them strong incentives to pursue regulatory revenues. These conditions would also enable them to show dependence on regulatory revenues and to convince issuers of their commitment to a program of efficient and responsive regulation.

On the other hand, the very smallest nations may have no ability to offer any credible regulatory infrastructure. If existing securities laws in the dominant international capital markets—the United States and United Kingdom—are even close to optimal, small countries without many alternative sources of revenue may be

255 Id.
severely disadvantaged. They may not be able or willing to offer the sophisticated regulation that predominates in international markets and is familiar to the world's international investors.\textsuperscript{257} Especially for those countries without existing securities markets, developing the requisite legal and administrative capacity from scratch and maintaining and financing it may be too risky and daunting a project.\textsuperscript{258}

Perhaps nations with relatively small government budgets and relatively large stock markets would be our best bet. Small budgets enable credible commitment. Large stock markets suggest the existence of important regulatory infrastructure, which makes the government's active pursuit of regulatory revenues less risky.\textsuperscript{259}

\textsuperscript{257} See Jackson & Pan, supra note 125, at 686-87 (describing market-driven demand for high disclosure in pan-European offerings).

Suppose, on the other hand, that U.S.-U.K. style regulation is not optimal for many issuers, but that a much less elaborate approach is. Some issuers might desire the relatively simple, nonintrusive rules and procedures that such countries may be capable of supplying. This approach might not require the intricate and expensive regulatory apparatus relied upon in the dominant capital markets. Romano has argued that even though smaller states may not be able to capture scale economies in terms of government enforcement efforts, they could still rely on private enforcement, much the same way the SEC relies on private enforcement to supplement its own regulatory efforts. Romano, supra note 1, at 518. "A need for a minimum state size for enforcement purposes is therefore not likely to create a substantial barrier to the effectiveness of regulatory competition in the securities law context." Id.

Even assuming simple rules without ex ante regulation were desirable for some issuers, a nation intending to compete in an international market for securities law would still need a dependable court system and capable lawyers and other securities professionals. Bernard S. Black, The Legal and Institutional Preconditions for Strong Securities Markets, 48 UCLA L. Rev. 781, 816 (2001). Some legal infrastructure and legal, financial, and accounting expertise would still be required. A small country without a stock market is unlikely to possess these features, and creating these institutional preconditions would not be simple or quick. Even relying on private arbitration as the primary enforcement device would require participation of skilled lawyers and the possible coercive sanction of a court. It is perhaps possible that this coercive sanction could be provided via the issuer's submission to the adjudicative jurisdiction of some other nation with a strong court system. However, relying on another nation's enforcement apparatus might impair the prescribing nation's ability to control the contours of its securities law product. Incentive problems may also plague the performance of any rented courts. See infra notes 318-24 and accompanying text.

Finally, even if simple rules with private enforcement were attractive to some issuers and investors, that sort of regulation might easily be duplicated among competitors, so that nations might have some difficulty profiting in that market segment.

\textsuperscript{259} Some absolute minimum stock-market size is probably necessary to assure sufficient
Below, I first discuss the difficulties that smaller nations would face in trying to develop regulatory infrastructure. I then consider whether countries exist that may offer the right combination of characteristics to suggest their likely success in the global market for securities regulation. Finally, I note that even if such nations exist, they may have trouble overcoming the strategic behavior of their more established rivals.

1. Regulatory Infrastructure Investments. A viable regulatory product would likely include some nontrivial level of ex ante regulatory oversight. This would require a professional bureaucracy with some amount of administrative capacity, as well as courts and private advisers. For example, U.S. securities regulation relies on a whole host of public institutions and private organizations—the SEC, the Department of Justice, stock exchanges, lawyers, accountants, underwriters, analysts, brokers and dealers—to make and enforce rules and to advise issuers and investors. Other established capital markets as well rely on professional regulators, sophisticated stock exchanges, and expert private advisers to make their systems work. To be internationally competitive, a small nation would have to be willing to invest in the development and ongoing refinement of its regulatory system.

How many small states will divert resources to pursuing uncertain payoffs in a competitive market for securities regulation? Their very lack of diversification, which would theoretically enable their credible commitment to maintaining optimal securities law, would seem to make the proposed investment in regulatory competition especially risky. Less prosperous countries, especially those without existing securities markets, may be unable or unwilling to make hostage investments with uncertain financial and political payoffs.

Moreover, even if such a strategy made sense for a nation as a whole, collective action and free-riding problems would hinder individual lawmakers who might be interested in pursuing regula-

---

260 See supra notes 208-17 and accompanying text.
261 See supra notes 215-16 and accompanying text (describing U.K. system).
ory revenues.\textsuperscript{262} Even if lawmakers believed that the pursuit of such revenues would be fruitful for their nation and that specific investments were justified, each individual lawmaker would be dissuaded from initiating such a program because of her inability to capture all the gains from the endeavor. Assuming that revenues would accrue to the state treasury without any special earmarking, lawmakers as a group might benefit from the larger budget, but it is unlikely that those responsible for initiating the program could exclude others from this general benefit. Unless individual lawmakers foresaw particular gains to themselves from pursuing a program of devising and selling securities regulation, none would initiate or participate in such a project,\textsuperscript{263} especially if alternative avenues exist for advancing their own individual political interests.\textsuperscript{264}

Even in Delaware, while the chancery court may serve a hostage function today, it was not intentionally created to serve that function.\textsuperscript{265} To the extent it does, this is a matter of historical accident. Apparently, no other U.S. state has been able to replicate this hostage strategy, which may suggest that political or economic obstacles exist that prevent governments from intentionally undertaking such hostage investments.\textsuperscript{266} Delaware may be especially suited to overcoming legislative collective action and free rider problems; its legislature is among the smallest in the United States.\textsuperscript{267} Each legislator is therefore likely to be able to anticipate

\textsuperscript{262} The extent of these problems depends of course on the form of government involved. More authoritarian regimes would not encounter these problems that are familiar to democratic systems.


\textsuperscript{266} Kahan & Kamar, \textit{supra} note 47, at 733-34.

and garner individual benefit from the enhanced revenues and larger state budget from successful sales of Delaware corporate law.\textsuperscript{268} Individual legislators can also more easily monitor each other's efforts than in larger bodies. Free riding is therefore likely to be less of a problem than in a larger body.\textsuperscript{269}

By contrast, in order to compete internationally over securities law, lawmakers in small countries would have to overcome incentive and commitment problems, as well as the collective action costs across the legislative and regulatory process. In addition, the public and private institutions required for internationally competitive securities law are far more elaborate and specialized than those necessary for corporate law in the United States, making investments in securities law all the more risky.

Having highlighted the difficulty for smaller nations of actively engaging in regulatory competition over securities law, I now consider in detail the promise of certain plausible competitors—nations with small government budgets and respectable stock markets.\textsuperscript{270} For a given country, a critical mass of domestic issuers

de.us/Legislature.nsf?Opendatabase (last visited Nov. 11, 2004).


\textsuperscript{269} One might instead view lawyers as the primary interest group motivating changes in corporate law, as opposed to legislators themselves. Macey & Miller, supra note 225, at 473; Ribstein, supra note 267, at 1009. In that case, a small legislature may be less responsive than a large one. With a large legislature, competition among legislators may lower the price of influence for interest groups, making it cheaper to obtain changes in the law. While transaction costs of obtaining the required majority to pass legislation may also rise as the size of the legislature increases, the downward price pressure from competition may dominate. William F. Shughart II & Robert D. Tollison, Corporate Chartering: An Exploration in the Economics of Legal Change, 23 ECON. INQ. 585, 592, 595 (1985).

The lawyer-centered view is problematic, however. It does not explain the existing revenue benefits to the state's coffers. If lawyers' maximand is the amount of legal work generated by firms' adoption of Delaware corporate law, lawyers would presumably rather the state give away charters for free. But as discussed, Delaware garners a nontrivial share of its state budget in the form of charter fees. See supra note 253.

\textsuperscript{270} TABLE 1 contains relevant data for all forty-seven nations represented by stock exchanges in the World Federation of Exchanges (FIBV), which forms the basis for this sample. See TABLE 1, infra p. 607. FIBV exchanges comprise over 97% of world stock market capitalization, and membership requirements suggest that these are the world's more sophisticated exchanges. See World Federation of Exchanges, Members, http://www.world-exchanges.org/WFE/home.asp?action=document&menu=2&nav=ie (last visited Nov. 11, 2004) (stating membership requirements for FIBV).
may matter most, since only those issuers are likely to be regulated primarily by their home country laws. Most export industries in sophisticated products begin as domestic industries; producers emerge to service the local market first and then expand into foreign markets. A strong domestic demand for securities law may be a necessary precondition for a nation to go global with its regulatory product. Countries without existing local demand would likely have difficulty initiating a program for internationally competitive securities law.

When these criteria are applied to the various nations, not many show promise to be serious competitors. Under plausible assumptions concerning the size of the global market for securities law, only for countries with very small budgets would prospective regulatory revenues be sufficient to enable those countries to demonstrate dependence on and a credible commitment to the pursuit of such revenues. But these countries may still lack appropriate infrastructure.

2. Credible Commitment and World Market Share. Even outside of the established capital market countries, nations may still have difficulty demonstrating a credible international commitment to maintaining efficient securities law. The size of the international market for securities regulation may simply be too small for many nations to show fiscal dependence on prospective regulatory revenues. Relative to the size of national budgets, the revenues available from selling securities law may simply be insignificant.

Some back-of-the-envelope calculations will illustrate. From 1998 to 2002, the SEC garnered, on average, about $1.8 billion in fees.\(^2\) That number can be extrapolated to get a ballpark estimate for the size of the world market for securities law. Given that the United States accounts for nearly half the world’s market capitalization,\(^3\) doubling the SEC’s regulatory revenues gives a rough estimate for the size of the world market of $3.6 billion per year.\(^4\)

Of course, this estimate is quite rough, and one might quarrel with

\(^2\) Securities and Exchange Commission, supra note 213.
\(^3\) Scott & Wellons, supra note 153, at 3.
\(^4\) Subsequent figures and comparisons are given in U.S. dollars (USD).
the precision of this extrapolation on several fronts.\textsuperscript{274} Despite its crudeness, however, this estimate will suffice for present purposes. If anything, this estimate is likely to be high. As the biggest and most influential regulatory monopolist, the SEC’s market power presumably extends to its fee structure as well. Competition would likely erode this market power and lower fees worldwide.\textsuperscript{275}

One way of thinking about a nation’s prospects for success in the market is to consider the revenues it might hope to garner from selling securities law. Consider, in particular, prospective revenues relative to (a) the nation’s public budget and (b) the size of the world market for securities law. A given nation’s hoped-for revenue stream would have to be large enough to be worth pursuing. That is, the project would have to be worth the nation’s while. And like the issue of credible commitment, this will depend on the project’s prospective value relative to the nation’s public budget. Higher revenues relative to national budget are better, of course, both in terms of giving a nation sufficient incentive to undertake the project and in terms of improving the nation’s ability to demonstrate fiscal dependence. But the higher are the hoped-for revenues, the larger is the world market share that a nation would have to achieve. How big a world market share could a smaller nation expect to garner in the short term, especially given that any global issuer choice regime would start with established capital market countries dominating the market for securities law?

When we look at the budgets of nations with stock markets and compare their existing government revenues with their potential revenues from entering the global market for securities law, one aspect of the numbers that stands out is that USD $3.6 billion is not a very large pie. Even a very small nation would have to hope to garner a fairly large market share in order both to make entry worth the nation’s while and to show dependence sufficient to demonstrate a credible commitment. The small size of the market cuts out all but the smallest nations. Even nations like New

\textsuperscript{274} This extrapolation assumes a linear relationship between market capitalization and regulatory revenues. It assumes that revenues garnered by the SEC are representative of the behavior of issuers and national regulators worldwide.

\textsuperscript{275} In any event, the estimate is likely to be within an order of magnitude of the right number. Even doubling the estimate does not much change the ensuing analysis.
Zealand, Singapore, and Hong Kong have government budgets that dwarf the world market for securities law.\textsuperscript{276} Tiny Singapore, an island nation with 4.6 million inhabitants and aspirations to be an international financial center, has annual government revenues approaching USD $28 billion.\textsuperscript{277} Even if Singapore captured half the world market, the assumed revenue stream of USD $1.8 billion would amount to only 6.5% of Singapore’s annual government revenues, a percentage that is probably too small to demonstrate fiscal dependence and a credible commitment.\textsuperscript{278}

Assume that regulatory revenues would have to comprise 10% of a nation’s public revenues in order for that nation to be able to demonstrate a credible commitment to responsive securities law. FIGURE 1\textsuperscript{279} shows the world market share that various nations would have to hope for in order to achieve regulatory revenues that would meet this 10% threshold.\textsuperscript{280} The most conspicuous feature of the chart is the few countries represented. Only the seventeen nations indicated have annual government revenues small enough that something less than 100% of the world market could comprise at least 10% of their national revenues.\textsuperscript{281}

\begin{footnotesize}
\textsuperscript{276} See TABLE 1, supra p. 607.
\textsuperscript{277} THE WORLD FACTBOOK 2003, supra note 214, Singapore.
\textsuperscript{278} Remember by comparison that Delaware's charter revenues account for over 20% of its state budget, and historically the figure has averaged over 15%. See supra note 214.
\textsuperscript{279} See FIGURE 1, infra p. 606.
\textsuperscript{280} This 10% threshold is fairly conservative given the Delaware comparison.
\textsuperscript{281} APPENDIX 1 contains a similar chart illustrating nations' world market share requirement at a 5% national revenue threshold. In general, the required world market share (RWMS) depends on the size of each country's national revenues (NATREV) and the target percentage of national revenues deemed sufficient to demonstrate credible commitment (COMPCT). More particularly:

\[ RWMS = \frac{(COMPCT \times NATREV)}{3.6}, \]

where NATREV is denominated in billions of USD.
\end{footnotesize}
A look at the countries represented in FIGURE 1 shows further cause for pessimism that many nations could demonstrate a credible commitment for international securities law. At one end of the spectrum, South Africa would need to be confident of garnering almost 89% of the world market in order to meet the 10% national revenue threshold. Such high confidence would be both unlikely and foolhardy. TABLE 1 shows just how insignificant is the world market for securities law relative to national revenues. For the overwhelming majority of countries, the world market would have to be many times larger in order to attract their serious attention.

282 TABLE 1, infra p. 607.
and to enable them to demonstrate fiscal dependence on regulatory revenues.

<table>
<thead>
<tr>
<th>COUNTRY</th>
<th>NATIONAL REVENUES $</th>
<th>NATIONAL MARKET CAPITALIZATION$</th>
<th>SHARE OF WORLD MARKET FOR SECURITIES LAW FOR 10% FISCAL DEPENDENCE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bermuda</td>
<td>0.6</td>
<td>2.2</td>
<td>1.7%</td>
</tr>
<tr>
<td>Malta</td>
<td>1.5</td>
<td>4.0</td>
<td>4.2%</td>
</tr>
<tr>
<td>Sri Lanka</td>
<td>3.0</td>
<td>1.1</td>
<td>8.3%</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>4.4</td>
<td>34.0</td>
<td>12.3%</td>
</tr>
<tr>
<td>Slovenia</td>
<td>8.1</td>
<td>3.1</td>
<td>22.5%</td>
</tr>
<tr>
<td>Peru</td>
<td>8.9</td>
<td>9.7</td>
<td>24.8%</td>
</tr>
<tr>
<td>Philippines</td>
<td>10.2</td>
<td>25.3</td>
<td>28.3%</td>
</tr>
<tr>
<td>Hungary</td>
<td>13.0</td>
<td>10.3</td>
<td>36.1%</td>
</tr>
<tr>
<td>Chile</td>
<td>16.0</td>
<td>60.4</td>
<td>44.4%</td>
</tr>
<tr>
<td>Malaysia</td>
<td>16.4</td>
<td>113.2</td>
<td>45.6%</td>
</tr>
<tr>
<td>New Zealand</td>
<td>16.7</td>
<td>18.2</td>
<td>46.4%</td>
</tr>
<tr>
<td>Thailand</td>
<td>21.0</td>
<td>29.2</td>
<td>58.3%</td>
</tr>
<tr>
<td>China, Hong Kong</td>
<td>22.9</td>
<td>623.4</td>
<td>63.6%</td>
</tr>
<tr>
<td>Ireland</td>
<td>25.7</td>
<td>81.9</td>
<td>71.4%</td>
</tr>
<tr>
<td>Indonesia</td>
<td>26.0</td>
<td>26.8</td>
<td>72.2%</td>
</tr>
<tr>
<td>Singapore</td>
<td>27.9</td>
<td>155.1</td>
<td>77.5%</td>
</tr>
<tr>
<td>South Africa</td>
<td>32.0</td>
<td>131.3</td>
<td>88.9%</td>
</tr>
<tr>
<td>Finland</td>
<td>36.1</td>
<td>293.6</td>
<td>100.3%</td>
</tr>
<tr>
<td>Israel</td>
<td>40.0</td>
<td>65.3</td>
<td>111.1%</td>
</tr>
<tr>
<td>Taiwan</td>
<td>42.7</td>
<td>247.6</td>
<td>118.7%</td>
</tr>
<tr>
<td>Argentina</td>
<td>44.0</td>
<td>45.8</td>
<td>122.2%</td>
</tr>
<tr>
<td>India</td>
<td>44.3</td>
<td>-</td>
<td>123.1%</td>
</tr>
<tr>
<td>Portugal</td>
<td>48.6</td>
<td>60.7</td>
<td>135.0%</td>
</tr>
<tr>
<td>Poland</td>
<td>51.6</td>
<td>31.4</td>
<td>143.4%</td>
</tr>
<tr>
<td>Greece</td>
<td>53.9</td>
<td>107.5</td>
<td>149.6%</td>
</tr>
<tr>
<td>Turkey</td>
<td>54.5</td>
<td>69.7</td>
<td>151.4%</td>
</tr>
<tr>
<td>Austria</td>
<td>56.3</td>
<td>29.9</td>
<td>156.4%</td>
</tr>
<tr>
<td>Iran</td>
<td>60.0</td>
<td>5.9</td>
<td>166.8%</td>
</tr>
<tr>
<td>Denmark</td>
<td>61.1</td>
<td>111.8</td>
<td>169.6%</td>
</tr>
<tr>
<td>Switzerland</td>
<td>71.6</td>
<td>792.3</td>
<td>198.9%</td>
</tr>
<tr>
<td>Norway</td>
<td>71.7</td>
<td>65.8</td>
<td>199.2%</td>
</tr>
<tr>
<td>Australia</td>
<td>86.8</td>
<td>372.8</td>
<td>241.1%</td>
</tr>
<tr>
<td>Brazil</td>
<td>100.6</td>
<td>226.2</td>
<td>279.4%</td>
</tr>
</tbody>
</table>
Year 2000 data except for Taiwan (2001).
** U.S. market capitalization includes Amex, Chicago, Nasdaq, and NYSE.
\(^b\) Source: World Federation of Exchanges.

At the other end of the spectrum, Figure 1 shows that for the smallest countries like Bermuda, Malta, and Sri Lanka, only a modest world market share would be needed to induce their interest in competing and to enable them to demonstrate credible commitment. However, these countries may be too small to provide a securities regulatory infrastructure that would appeal to international investors.

3. **Size Does Matter.** Size may matter along several fronts. Small annual revenues mean few resources to devote to securities regulation and regulatory infrastructure. A small stock market—in terms of number and market value of domestic issuers—likely means an informal, undeveloped, unsophisticated regulatory system.\(^{283}\) Several countries are considered below along these dimensions.

Bermuda is the country in the sample with the smallest government revenues, USD $610 million in 2000.\(^{284}\) Capturing even a

\(^{283}\) As earlier noted, domestic issuers may matter most in this regard because, as with most sophisticated products, successful exports are typically preceded by successful domestic production and consumption.

small share of the world market would mean a great deal to Bermuda's budget. So in an issuer-choice world, Bermuda might have incentive to embark on a program of active competition for issuers. Demonstrating fiscal dependence on regulatory revenues and a credible commitment to such a regulatory program would also be feasible. Moreover, Bermuda enjoys some reputation as a safe haven for certain types of financial activity driven by U.S. and other overseas companies. For example, it is the third largest insurance and reinsurance market in the world after New York and London. Perhaps Bermuda is endowed with the right combination of smallness and financial sophistication to be able to sell securities law globally?

Unfortunately, with respect to securities law, Bermuda suffers deficiencies typical of small countries. Its government budget is simply too small to enable it to devote resources to providing sophisticated world-class regulation. The Bermuda Monetary Authority (BMA) is charged with supervising the Bermuda Stock Exchange (BSX). In 2000, the BMA's total operating expenses were just under USD $5 million. And supervision of the BSX is only one of BMA's multiple and varied tasks. It regulates all financial institutions in Bermuda, including not just the stock exchange, but banks, deposit companies, trust companies, investment companies, and collective investment schemes. The BMA also manages Bermuda's exchange controls and regulates foreign currency transactions. It issues and redeems notes and coins. Needless to say, current resources devoted to regulation of the securities market in Bermuda are not great. The demand for sophisticated regulation is also not great. Bermuda's stock market

---

287 Id. at 62. In 2003, the latest year for which data is available. BMA's operating expenses were just under USD $10 million. 2003 BERM MONETARY AUTHORITY, REP. AND ACCTS. 61 (2004). By comparison, operating expenses for Hong Kong's Securities and Futures Commission were roughly USD $47.7 million in 2003, and its focus is squarely on securities market regulation. 2002-2003 SEC. AND FUTURES COMMISSION ANN. REP. 79.
289 Id.
290 Id.
is minuscule in terms of its domestic issuers. In 2000, domestic issuers listed on the BSX numbered only twenty-two, with an aggregate market value of only USD $2.2 billion.\footnote{Malta, the next smallest country on our list,\footnote{292} offers a similar story. An island nation of 400,000 people,\footnote{293} Malta’s government revenues for 2000 totaled USD $1.5 billion.\footnote{294} In 2000, the Malta Stock Exchange listed fourteen domestic issuers valued at USD $4 billion.\footnote{295} The entire operating expenses for the exchange in 2000, which included its costs of self-regulation, totaled less than 750,000 Maltese lira, or about USD $2 million.\footnote{296} This small operating budget seems appropriate for such a small exchange. At the same time, though, it is difficult to imagine this tiny operation serving as the foundation for world class securities regulation.}

As we move through the list to countries with larger government revenues, TABLE 1 shows that they generally also have larger stock markets. The latter makes them more viable as potential international suppliers of securities regulation, though their larger budgets also make them less likely to be able to show credible commitment and less motivated to pursue regulatory revenues in the first place.

\footnote{\footnote{291} Singapore’s domestic market capitalization in 2000, by contrast, was over USD $155 billion. FIBV tbl. 1.1, 1.3B, supra note 208. The aggregate USD volume of trading on the BSX appears quite high. It typically exceeds the volume of trading on the national exchanges in Sweden or Australia, for example. In 2002, total trading volume on the BSX was almost USD $414 billion. WORLD FEDERATION OF EXCHANGES (FIBV), TOTAL VALUE OF SHARE TRADING, tbl. 1.4B (Apr. 25, 2003), http://www.world-exchanges.org/publications/TAX420.pdf [hereinafter FIBV tbl. 1.4B]. For the same period, trading volume on the Stockholm Stock Exchange was roughly USD $280 billion, and for the Australian Stock Exchange, trading volume was approximately USD $295 billion. \textit{Id.} However, the high BSX volume is deceptive, consisting almost exclusively of trading in the shares of a relative handful of foreign companies cross-listed in Bermuda. In 2002, trading volume in domestic companies, of which there were twenty-two, amounted to less than two-tenths of 1% of total BSX trading. WORLD FEDERATION OF EXCHANGES (FIBV), NUMBER OF COMPANIES WITH SHARES LISTED, tbl. 1.1 (Apr. 25, 2003), http://www.world-exchanges.org/publications/TAX1102.pdf [hereinafter FIBV tbl. 1.1]. BSX foreign company listings totaled thirty-two that same year. \textit{Id.}}

\footnote{\footnote{292} TABLE 1, supra p. 607. \footnote{293} WORLD FACTBOOK 2003, supra note 214, Malta. \footnote{294} \textit{Id.} \footnote{295} FIBV tbl. 1.1, supra note 291; FIBV tbl. 1.3B, supra note 208. \footnote{296} Before October 2002, the Malta Stock Exchange was self-regulating. 2002 MALTA STOCK EXCHANGE, ANN. REP. 11 (2003), \textit{available at} http://www.borzamalta.com.mt/annualreports/ar2002.pdf. The Financial Markets Act, which took effect on October 1, 2002, placed most of the regulatory authority over the stock exchange in the hands of the Malta Financial Services Authority (MFSA). \textit{Id.}}
Luxembourg may offer an optimal combination of small budget and healthy stock market. The Luxembourg Exchange had fifty-four listed domestic issuers in 2000, with a combined market value of USD $34 billion, significantly higher than Malta or Bermuda. In addition, Luxembourg's government revenues of USD $4.4 billion are small enough that it would only need a 12.3% world market share in order to have its regulatory revenues equal 10% of overall revenues. Data on the operating budget for its securities regulatory authority would be useful in refining this assessment, but unfortunately, consistent with Luxembourg's fabled reputation for financial secrecy, annual reports for Luxembourg's financial authority, la Commission du Surveillance du Secteur Financier (CSSF), include no budget data, and none were readily available otherwise.

As we move through TABLE 1, no other country seems to show much promise. National revenues get much larger very quickly, so that hopeful competitors would have to be quite confident of garnering a fairly large world market share in short order. Ultimately, there may be few if any nations with the right characteristics to be successful long-term competitors. The global market for securities regulation may be so small that only the smallest nations could demonstrate dependence on regulatory revenues. But not many of these nations appear willing and able to invest in world-class regulatory infrastructure. FIGURE 2 illustrates this dearth of competitors. It locates countries based on their 2000

---

297 FIBV tbl. 1.1, supra note 291; FIBV tbl. 1.3B, supra note 208. The Luxembourg Exchange also listed 216 foreign issuers in 2000, but the total value of foreign shares traded in 2000 was very small, less than 1% of the value of domestic shares traded. FIBV tbl. 1.4, supra note 291; FIBV tbl. 1.4B, supra note 291.

298 See TABLE 1, supra p. 607.

299 Id.


301 TABLE 1, supra p. 607.

302 Consider the Philippines, for example, no financial powerhouse. Only three spots higher on the list than Luxembourg in terms of national revenue, the Philippines' national revenues more than double those of Luxembourg. TABLE 1, supra p. 607.

303 This is so even assuming a larger world market and that a smaller percentage fiscal dependence would be sufficient to demonstrate commitment. See infra APPENDIX I.

304 FIGURE 2, infra p. 612.
government revenues\textsuperscript{305} and the USD value of their domestic stock markets,\textsuperscript{306} taking the ten FIBV nations with the smallest government revenues. The most promising candidates, those with small revenues and large stock markets, appear toward the upper left-hand quadrant of the space. Notice the dearth of countries. Luxembourg seems the most promising. Consider as well the possibility that some absolute minimum size of domestic stock market may be required in order to assure sufficient economies of scale to enable the jurisdiction to support the necessary institutional arrangements for competitive regulation. Even drawing that line at USD $15 billion in market capitalization eliminates most of our candidates.

\begin{figure}[h]
\centering
\includegraphics[width=\textwidth]{figure2.png}
\caption{National Revenues v. National Market Cap}
\end{figure}

\begin{itemize}
\itemVietnam
\itemPhilippines (10.2, 55.3)
\itemLuxembourg (4.4, 34.6)
\itemChile (16.6, 66.4)
\itemMalaysia (16.4, 113.2)
\itemSri Lanka (2.0, 1.1)
\itemBermuda (0.6, 2.2)
\itemMalta (1.5, 2.0)
\itemSlovenia (3.1, 3.1)
\itemPeru (8.9, 9.7)
\itemHungary (13.3, 11.9)
\end{itemize}

\begin{itemize}
\item See TABLE 1, supra p. 607.
\item FIBV tbl. 1.3B, supra note 208.
\end{itemize}
FIGURE 3 takes the next ten smallest nations by government revenues. Notice that national revenues and national market cap are significantly larger for these ten nations than for the smallest ten reflected in FIGURE 2. Only if one believes either that the size of the world market is much larger than USD $3.6 billion or that some percentage much smaller than 10% of total government revenues is sufficient to demonstrate a credible commitment, or both, may these larger nations be viable candidates.

(11th-20th Smallest FIBV Nations--2000 Data)

4. Rivals' Strategic Behavior. Even assuming some among these smaller nations would have both sufficient capacity and sufficient incentives to compete in an issuer choice world, they would still have to be able to make money doing it. These smaller nations would have to be able to charge issuers enough to make a profit.

307 FIGURE 3, infra p. 613.
308 FIGURE 2, supra p. 612.
The fact that Delaware can do this with corporate law in the United States tells us nothing about the viability of the analogous strategy in international competition over securities regulation. Delaware was lucky when New Jersey voluntarily bowed out of its frontrunning position in the chartermongering game in 1913. At the time, Delaware was already poised to take over New Jersey's first-mover advantage. Delaware had adopted New Jersey's general incorporation statute essentially verbatim in 1899. The next year, a Delaware court declared that the legislature must have intended that its courts follow New Jersey precedents in interpreting the statute.

No similar first-mover advantage would accrue to upstart nations in a global market for securities law. Regulators in established capital markets like the United States and United Kingdom might deter entry or additional investment by competitors through a variety of pricing strategies. Without changing the content of any substantive rules, established capital market regulators might simply offer their securities laws for free. Given that the SEC, for example, has no direct economic stake in any government revenues generated by securities filing fees, fines, and the like, and given that the cost to the U.S. government as a whole of offering securities law is negligible, revenue generation may not be a priority. In addition, the same powerful interests that currently benefit from U.S. regulatory monopoly might, in an issuer choice world, oppose any attempts to exact high fees from issuers, since that might dissuade issuers from retaining U.S. rules that benefit existing interests. In effect, the United States and other important capital

---

309 See GRANDY, supra note 97, at 80-82 (describing Governor Wilson's lame duck advocacy of Seven Sisters legislation effectively removing New Jersey from charter competition game).
310 Id. at 80.
311 Wilmington City Ry. v. People's Ry., 47 A. 245, 254 (Del. Ch. 1900).
312 Though regulators in established capital markets may have difficulty demonstrating a credible commitment to efficient and responsive securities regulation, see supra notes 206-55 and accompanying text, they may still be able to frustrate the efforts of upstart competitors.
314 See SECURITIES AND EXCHANGE COMMISSION, SEC 2002 ANNUAL REPORT 180 (showing appropriations ranging from approximately $320 million in FY 1998 to $515 million in FY 2002).
markets might be willing to give away their securities regulation for free in order to help cross-sell other products, like legal, underwriting, and accounting services, in order to benefit important constituents. Regulators' revenue incentives are likely to be weak. They may instead prefer to maximize their market share, which both augments their bureaucratic heft and benefits important constituents who may provide political support.

Or established capital markets might make only marginal changes in their substantive rules to discourage upstarts. Like the lead yacht in a regatta, major capital markets may simply do enough to stay in the lead and drive out competitors. Upstart competitors would have to offer securities law sufficiently superior to those of established capital market countries that issuers would not only be willing to switch securities law but would be willing to pay out-of-pocket for it as well. The margin of superiority would have to be large enough to both (a) allow the upstart to charge a high enough fee to issuers to make the project profitable in the long run, and (b) leave adopting issuers with a net benefit after having

---

315 Cf. Macey & Miller, supra note 225, at 494 (identifying Delaware corporate bar as important interest group, which legislature favors with legal rules that increase lawyers' fee revenues).

316 Using a yachting metaphor, Ian Ayres illustrates the possibility of supply side inefficiencies in the context of U.S. charter competition, which may likely also apply to international competition over securities regulation. In the game between the lead yacht and a trailing yacht, even if the lead yacht takes an efficient tack, a trailing yacht may not. Instead, figuring that it cannot catch the lead yacht simply by mimicking its tack, the trailing yacht may choose another direction in the hope of gaining on the leader if the wind shifts. In response, the lead yacht may "cover"—mimic the trailing yacht's tack. This might not be the most efficient course, but it may best protect the leading yacht's lead. If the wind shifts, both yachts would be similarly affected. Ian Ayres, Supply Side Inefficiencies and Competitive Federalism, in INTERNATIONAL REGULATORY COMPETITION AND COORDINATION 239, 246 (William Bratton et al. eds., 1996).

Delaware may behave this way with regard to corporate law innovations, and there is some historical evidence of this approach. In international securities regulatory competition as well, a leading jurisdiction in the competition may have insufficient incentive to innovate efficiently. Switching costs may be high, so that a leader will be able to maintain its lead merely by covering other countries' innovations. This cover strategy, in turn, may discourage trailing jurisdictions from innovating in the first place.

317 In the short run, a country might be willing to pursue market-share pricing—that is, pricing with a goal of capturing market share. However, to the extent this strategy requires pricing below marginal cost, the small and relatively poor nation that is assumed to be the most likely competitor in terms of incentives is unlikely to have sufficient resources to sustain such pricing for long. Moreover, the prospect of having to undertake such a costly and risky strategy would likely deter a nation from pursuing the investment in the first place.
paid such a fee. These conditions suggest that regulators in established capital market countries might easily frustrate upstarts through strategic modification of their laws and fee structures.

Given the potential new investment costs facing an upstart, which are likely to be substantial, and the possibility that the dominant nations might respond to competition with competitive adjustments to their own regulations, upstarts would seem to face fairly daunting prospects.

VI. ENFORCEMENT

In addition to the dearth of competitors in an issuer choice world, enforcement across international borders would be messy. Nations' regulatory exports might therefore present issuers with excessive indeterminacy, a problem with no parallel in U.S. corporate law. This indeterminacy would tend to blunt competition.

A. MIX AND MATCH TRANSNATIONAL ENFORCEMENT

Scholars disagree as to whether privately chosen securities law should be enforced by the courts and other institutions of the issuer's chosen regime or those of the issuer's home country.318 In either case, enforcement problems are likely to hinder direct competition in ways that do not affect U.S. corporate charter competition.

Regime-selected regulators and institutions may be best situated to enforce, since they will generally be experts on the nuances of the legal rules to be applied.319 In addition, centralizing litigation and other enforcement activity in this way enables consistent development of the regime-selected law, as compared to other approaches that involve interpretation by various nations' courts or regulators.320 Because issuers from different countries may choose the same nation's regulation, relying on the courts or other enforce-

318 See supra note 49 and accompanying text.
319 Romano, supra note 1, at 407; see also Choi & Guzman, Portable Reciprocity, supra note 15, at 931 (recommending regime jurisdiction as default rule).
320 Tung, supra note 21, at 1428.
ment institutions in each issuer’s home country to enforce the 
regime-selected law might result in a mishmash of varying prece-
dents, all attempting to interpret one nation’s laws. Finally, the 
benefits of regulatory competition are maximized when the legisla-
tive, interpretive, and enforcement functions come under the same 
sovereign. When authority over outcomes is split between the rule 
givers of one state and the interpretive and enforcement organs of 
another, the rule-giving state is impeded in its ability to respond to 
consumer demand. It cannot guarantee that its regulatory product 
will be sufficiently nuanced to display all the features consumers 
want.321

Moreover, regime-selected institutions have one other significant 
factor recommending them. Enforcement must be seen as an 
integral aspect to the product itself, and if nations are meant to be 
competing suppliers in an international market for regulatory 
products, then only the supplier has the right incentives to “service” 
the product properly. Other countries’ institutions—regulators in 
the issuer’s home country, for example—may not have sufficient 
incentive or sufficient administrative capacity to enforce the regime-
selected rules faithfully. As competitors in the international market 
for securities law, they may even have incentive to do just the 
opposite. Other countries’ enforcers may have incentive to sabotage 
competitors’ products by tinkering with enforcement. It is not 
difficult to imagine situations, for example, in which home country 
enforcers may be able to favor local interests in particular cases, 
while at the same time creating confusion over application of 
another state’s rules. Such an enforcement strategy would serve to 
discourage local firms from choosing nonlocal rules, advantaging the 
local regulatory product in the local market.

On the other hand, the issuer’s wrongful acts or conduct to be 
regulated, which would form the basis for any government enforce-
ment action or private suit, are most likely to occur in the issuer’s 
home country. In terms of supervising or investigating such 
conduct, local institutions in the home country are likely to be more

321 Romano, supra note 1, at 407 and n.46; see also Ronald J. Daniels, Should Provinces 
(discussing lack of charter competition among Canadian provinces).
effective given their familiarity with local business practices.\textsuperscript{322} Being "on the ground" may give home country regulators a natural advantage over their foreign counterparts. Enforcing judgments would also be easier because of the presence of the issuer's assets. The home country may therefore be the most convenient venue for regulating conduct, gathering evidence, and realizing on the firm's assets.\textsuperscript{323} It may ultimately be easier for home country regulators to master the various substantive laws they must enforce under issuer choice than it would be for foreign regulators to operate in the local legal environment.\textsuperscript{324}

Enforcement by regime-selected regulators and institutions may also be expensive. Especially for regulatory regimes that rely on significant ex ante regulatory oversight, like the U.S. and U.K. systems, the regular interaction that routinely occurs between regulators and issuers might be difficult or costly to replicate for issuers with no preexisting connection to the selected regulatory jurisdiction.

So regime-selected regulators and institutions will have operational difficulties implementing their rules in foreign lands, and local regulators may lack the legal expertise in local issuers' chosen regulatory regimes—and may lack appropriate incentives—to be able to render appropriate outcomes. Because of these difficulties, issuers may have trouble predicting the content of foreign securities laws and the consequences of selecting any one. Regulators will enjoy only incomplete control over the contours of their regulatory products, and their ability to respond to consumer feedback, especially complaints about indeterminacy, will be correspondingly blunted.

B. ENFORCEMENT OF CORPORATE LAW IN THE U.S. BY CONTRAST

As for U.S. states and corporate charter competition, states to some extent face a similar bifurcation as between lawmaking and

\textsuperscript{322} Tung, supra note 21, at 1428.
\textsuperscript{323} Steven Walt, Introduction: Privatization and Its Prospects, 41 VA. J. INT'L L. 517, 527 (2001); Choi & Guzman, Portable Reciprocity, supra note 15, at 928.
\textsuperscript{324} Walt, supra note 323, at 527.
enforcement. However, this does not create the same problems that would plague issuer choice.

Corporate law in the United States is enforced primarily through private actions in state and federal courts. Case law therefore forms a crucial element in the corporate law product each state offers. Because jurisdiction and venue rules do not require that corporate law disputes be brought in the courts of the state of incorporation, a given state relies to some extent on federal courts and the courts of other states in interpreting and enforcing its corporate law.

Given this structure, one might suppose that states would face similar problems of incomplete control in enforcing their rules as described above for issuer choice. Especially if states were truly competitors over corporate law, each state might worry that other states' courts might attempt to sabotage the first state's corporate law product with muddled opinions interpreting the first state's corporate law. However, this seems not to be an issue among states. No trend has appeared to suggest that out-of-state interpretations of local corporate law have been more often objectionable or wrong than decisions by local courts.

To the U.S. lawyer, this is not surprising. Given that corporate law exhibits substantial uniformity across states, and given a common national language and business culture, big or frequent mistakes in interpreting other states' corporate law seem unlikely, certainly much less likely than for the kind of cross-border enforcement of national securities laws that issuer choice would require. The possibility of judicial sabotage of out-of-state corporate law also seems farfetched. Asking or expecting judges to misapply corporate laws of other states in an effort to increase the relative attractiveness of local law would be unseemly, and judges would generally resist any such recruitment efforts. In addition, unlike regulators charged with promulgating and enforcing securities law, judges in the United States are generalists. Besides Delaware, no other state maintains a specialized court to hear corporate law cases. For most judges, corporate law cases form only a small part of their

325 See supra note 115 and accompanying text.
326 Kahan & Kamar, supra note 47, at 708.
caseloads. Judges would therefore not tend to feel any special institutional commitment to selling local corporate law, especially not by compromising their own professional judgment in interpreting out-of-state corporate law.

VII. STAYING HOME

With all of the foregoing hurdles to direct competition, the choices facing issuers in an issuer choice world seem not particularly appealing. Given the choice, would issuers opt out of home country securities law in favor of other law? Switching from the existing practice of territorial regulation to issuer choice, the early competition over securities law would primarily involve enticing issuers—mainly from established capital market countries—to opt out of an established and familiar regulatory regime in favor of a less familiar and perhaps less seasoned regulatory structure. Issuers might not be willing to opt out.

---

327 Even in the handful of states that have established specialized business courts, corporate cases comprise only a small part of a judge's caseload. Id. at 710. Commercial and contract disputes predominate, and not corporate cases. Id. at 712.

328 In Delaware, judges embrace an institutional commitment to improving Delaware corporate law. See Andrew G.T. Moore, II, State Competition: Panel Response, 8 CARDOZO L.REV. 779, 782 (1987) (quoting Justice Moore of Delaware Supreme Court, "I think Delaware corporate law will continue to evolve in order to meet the needs of corporate America. The Delaware courts feel strongly that this is our responsibility.").

329 Even if state court judges were willing to sabotage out-of-state corporate law in a bid to make local charters more attractive, they would seem to have little to gain from the attempt. Disrespecting a firm's chosen corporate law in this way would have the same effect as attempting to mandate local corporate law territorially. Far from making local law more attractive, disregard for firm choice of corporate law in either form would more likely drive businesses to locate elsewhere or otherwise avoid those in-state contacts that would trigger these courts' jurisdiction.

330 An issuer choice proponent might parry this inquiry with a "chicken soup" defense. Offering issuers a choice might (or might not) help, but it can't hurt. Cf. Lucian Arye Bebchuk & Allen Ferrell, A New Approach to Takeover Law and Regulatory Competition, 87 VA. L. REV. 111, 149-50 (2001) (making similar argument for their proposal for federal choice-enhancing intervention to enable shareholders to opt out of manager-selected takeover defenses). However, as the discussion in the text suggests, a drastic change in choice of law would likely generate all sorts of risk and uncertainty for issuers and investors, even if not one issuer ultimately opts out of its home country securities regime. Risk and uncertainty, of course, are not free.

331 For firms making their initial offerings, home country law is likely to be attractive for reasons similar to those discussed in the text.
The foregoing discussion has shown that issuers are not likely to have many attractive foreign regimes from which to choose. The structure of the market for securities law does not seem conducive to producing competitive alternatives for issuers, and enforcement problems would also serve to dull competition. In this Part, I point out the relative attraction of home country law and some costs to issuers of opting out. Choosing foreign law effectively forsakes a whole host of home country institutional and organizational complementarities with home country securities law. Choosing foreign law forsakes valuable learning and coordination effects derived from well-worn institutional practices among government and private actors operating under territorial monopoly. The unproven technology of a foreign regulation matched to other local legal institutions would be unpredictable and might cause investors to impose a heavy discount on the securities of any issuer opting out of home country law. Investors' bias for their home country issuers likely includes a bias for home country law as well. No similar problems afflict U.S. corporate charter competition.

A. INSTITUTIONAL COMPLEMENTARITIES AND MISMATCHES

Issuers would encounter numerous costs in attempting to switch from home country securities regulation to that of a foreign jurisdiction. Under long-standing territorial regulation, it should not be surprising that other laws and institutions in each nation have developed in a complementary fashion with its securities regulation. Besides the letter of the law itself, securities trading and regulation may depend on complex interactions among various regulatory and enforcement entities, among regulators and issuers and their professional advisers, and among regulators and stock exchanges and other self-regulating organizations. Well-worn institutional practices already exist. Besides enforcement, discussed in Part VI, these institutional practices include ex ante supervision and guidance for issuers, listing standards and practices, and

332 See supra notes 117-31 and accompanying text (discussing investors' home bias).
333 See supra notes 318-29 and accompanying text.
regulation of brokers and dealers, among other things. The pieces all fit together, more or less. All the players understand the system. They know what to expect.

As North has noted, this matrix of complementary institutions and organizations generates "massive increasing returns." The interaction over time of various regulatory institutions with each other and with private advisers has generated significant learning effects and coordination effects. In addition, as regulation is more widely applied and the network of complementary organizations grows, the system becomes more streamlined. These learning and coordination effects would be forsaken by any local issuer opting out of home country regulation in favor of foreign law. Home country institutions and organizations would have to start from scratch with new foreign law.

Transplanting another nation's securities law into existing institutional arrangements would be messy and unpredictable. Agreements among nations for issuer choice would likely only be able to address the most basic issues. The remaining issues would have to be worked out over time—and basically from scratch—through painstaking regulatory tussles over the many novel questions that issuer choice would generate. To list just a few examples from the United States—many of which would also arise in other established capital markets—how would self-regulatory organizations in the local market operate under a foreign law? Would there be different answers depending on the foreign regime selected? How would stock exchange listing requirements dovetail with foreign law? To what extent would local laws against fraud be displaced by foreign law? What about private enforcement mechanisms? Would those follow local law or foreign regime-selected rules?

---

334 See supra notes 183-86 and accompanying text.
335 NORTH, supra note 110, at 95.
336 See supra notes 171-88 and accompanying text.
338 The experience of the EU is also instructive. In attempting to craft a mechanism to enable European-wide retail public offerings, the Council promulgated the Public Offers Directive. Jackson & Pan, supra note 125, at 662. This was meant to create a "regulatory passport" system, allowing issuers to make public offerings of securities throughout the EU
By opting out of home country law, an issuer effectively forsakes a tried and true technology for a novel one. With the unavoidable institutional mixing and matching that issuer choice entails, the learning in each home country starts from zero. Much of the learning is not likely to be transferable across the various foreign regulatory regimes from which a local issuer might choose. Because each foreign regime is likely to exhibit its own quirks and features, many of the lessons learned in the home country from matching an issuer-selected foreign securities regime to other home country institutions may be unique to that foreign regime. For example, when one Japanese issuer chooses Bahamian securities law to govern its securities activities and another chooses German law, the problems of integrating Bahamian securities law into the web of other Japanese legal and regulatory institutions are likely to be different from the problems that arise from integrating German law. Learning and coordination effects in each home country might accrue only slowly and episodically.\textsuperscript{339} Periodic bilateral or multilateral renegotiation of international issuer choice agreements might also be required.

Under home country securities law matched to other home country institutions, these issues go away. Their easy disappearance makes it easy to overlook the massive learning and interorganizational coordination that have already accrued through past experience in each nation with its territorial securities regulation.\textsuperscript{340} Without the legal certainty that comes from prior learning, investors in important capital markets would likely apply relying only on their home country offering documents. However, the requirement of host country regulatory approval has hampered the usefulness of the Public Offers Directive. It has had virtually no impact on public offerings within the EU. \textit{Id.} at 680. On regulatory passports generally, see Tung, \textit{supra} note 132.

\textsuperscript{339} Choi and Guzman suggest that a nation could facilitate switching by offering regulation only "incrementally different in clear and easy to understand ways" from an established regime, so that only a little new learning must be done for an issuer to switch. Choi \& Guzman, \textit{Portable Reciprocity}, \textit{supra} note 15, at 934. This suggestion, however, ignores the labyrinthine institutional context in which securities regulation operates in established capital markets.

\textsuperscript{340} For example, the volumes of SEC releases and no-action letters attest to the devil-in-the-details nature of securities regulation in the United States, the demand for certainty by issuers and investors, and the "learn by doing" that has responded to this demand.
a heavy discount to the securities of issuers who abandon their
home country regulation in favor of foreign law.\textsuperscript{341}

Not only are issuers and investors already familiar with home
country regulation, but they are likely to enjoy political influence at
home that they may not enjoy abroad. They may be in a position to
take political action at home to influence regulation to their liking.
As with investors’ general home country bias, both issuers and
investors also enjoy better information about the direction of
political and regulatory winds in their home jurisdiction than in
other jurisdictions. Especially if regulators in important capital
markets develop a practice and reputation for strategically match-
ing other nations’ innovations,\textsuperscript{342} issuers might as well stay home.
Established regulators may drive out upstarts through this
matching strategy.\textsuperscript{343}

With corporate law in the United States, by comparison, no
similar institutional problems exist. Not only are corporate laws
fairly similar across jurisdictions, but courts and court rules are as
well.

B. AGENCY ISSUES

Related to the learning and coordination effects, agency issues
might cause firms to stay at home as well. Not only are issuers
familiar with their home country regulatory landscape, but their
lawyers are as well. For the same reason that home country
lawyers would likely oppose local recognition of foreign securities
law, in an issuer choice world lawyers may attempt to steer their
clients to home country law. Choosing local law enables the firm’s
local lawyers to maximize their fees from issuers. An issuer’s choice

\textsuperscript{341} Even if the market’s unpredictability discount were only a short-term phenomenon, as issuers, regulators, and others worked out the implications of mix-and-match regulation someone would have to go first. Some issuer would have to be the guinea pig. It may be that few issuers would be willing to suffer these higher capital costs.

\textsuperscript{342} See supra notes 309-17 and accompanying text.

\textsuperscript{343} Those same established regulators might not be too successful at poaching issuers from other established capital market countries, however, because of their inability to demonstrate commitment to a program of responsive regulation. See supra notes 206-21 and accompanying text.
of foreign law, however, would likely force its home country lawyers to share fees with foreign lawyers. Introducing the need for foreign lawyers might also enable those foreign lawyers to grab other types of the issuer's legal work at the expense of the home country lawyers. \textsuperscript{344}

VIII. CONCLUSION

"Law as a product" provides a powerful conception favoring regulatory competition. And corporate charter competition among U.S. states offers a plausible success story. It is the darling of regulatory competition advocates, who rely on this story as a basis for advocating for the extension of private choice to other areas outside of corporate law. Whether this seeming success story can be replicated in other contexts, however, is unclear.

Application of the model to international securities regulation seems quite natural at first blush. Given the close affinity of securities regulation with corporate law and their significant overlap, it might be expected that competitive mechanisms that work in one context would be applicable to the other. I have argued, however, that the analogy does not hold. The general affinity between these two areas of law tells us little about whether regulatory competition in U.S. corporate law portends anything for international securities regulation. Important differences in political economy as between U.S. states in a federal system and independent nations in an anarchic global context make the charter competition model inapposite.

The choice of law rule respecting private choice that emerged among U.S. states for corporate law—the internal affairs doctrine—is unlikely to be replicated among nations for securities regulation. The historical and political conditions in the two contexts are quite different. Without such a rule, issuer choice is not possible. Even assuming this choice of law problem could be

\textsuperscript{344} Similar agency issues may explain some observed home-state bias in U.S. firms' incorporation choices. Bebchuk & Cohen, supra note 47, at 397; Daines, supra note 47, at 1584.
overcome, U.S. states' presumed incentives and capacities to compete over corporate law may not translate well into the context of international securities regulation. In this latter context, active competitors may be hard to find. For established capital market countries, regulatory revenues may be too small to enable such countries to demonstrate the fiscal dependence that is critical for credible commitment. All but the smallest nations would have difficulty showing fiscal dependence. The smallest nations, on the other hand, are unlikely to have sufficient legal and regulatory infrastructure to be able to offer sophisticated, internationally competitive securities law. With these constraints, there would likely be a dearth of serious competitors in a global market for securities law. Cross-border enforcement problems would also likely impede competition. The transnational mix-and-match of legal institutions required to enforce issuer-selected foreign law is unlikely to generate predictable rules responsive to the needs of issuers and investors.

The various impediments to direct competition suggest that issuers would not have appealing choices in an issuer choice world. The predictability of home country regulation and the stronger political influence issuers enjoy at home may cause them to stay home, even given an exit option.

Competitive federalism operates best in a federalist system. No such system exists internationally. Whether a system could emerge to facilitate stable international competition over securities law is unclear. What is clear, however, is that U.S. corporate charter competition is not the right model.
APPENDIX I

FIGURE 4 and TABLE 2 show the prospects for competition, assuming that a nation's credible commitment to responsive securities law could be demonstrated when regulatory revenues comprise 5% of a nation's public revenues.

FIGURE 4: Required World Market Share for 5% Fiscal Dependence

2000 Data
### TABLE 2
National Revenues, National Market Capitalization, and Required World Market Share for 5% Fiscal Dependence

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Bermuda</td>
<td>0.6</td>
<td>2.2</td>
<td>0.8%</td>
</tr>
<tr>
<td>Malta</td>
<td>1.5</td>
<td>4.0</td>
<td>2.1%</td>
</tr>
<tr>
<td>Sri Lanka</td>
<td>3.0</td>
<td>1.1</td>
<td>4.2%</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>4.4</td>
<td>34.0</td>
<td>6.2%</td>
</tr>
<tr>
<td>Slovenia</td>
<td>8.1</td>
<td>3.1</td>
<td>11.2%</td>
</tr>
<tr>
<td>Peru</td>
<td>8.9</td>
<td>9.7</td>
<td>12.4%</td>
</tr>
<tr>
<td>Philippines</td>
<td>10.2</td>
<td>25.3</td>
<td>14.2%</td>
</tr>
<tr>
<td>Hungary</td>
<td>13.0</td>
<td>10.3</td>
<td>18.1%</td>
</tr>
<tr>
<td>Chile</td>
<td>16.0</td>
<td>60.4</td>
<td>22.2%</td>
</tr>
<tr>
<td>Malaysia</td>
<td>16.4</td>
<td>113.2</td>
<td>22.8%</td>
</tr>
<tr>
<td>New Zealand</td>
<td>16.7</td>
<td>18.2</td>
<td>23.2%</td>
</tr>
<tr>
<td>Thailand</td>
<td>21.0</td>
<td>29.2</td>
<td>29.2%</td>
</tr>
<tr>
<td>China, Hong Kong</td>
<td>22.9</td>
<td>623.4</td>
<td>31.8%</td>
</tr>
<tr>
<td>Ireland</td>
<td>25.7</td>
<td>81.9</td>
<td>35.7%</td>
</tr>
<tr>
<td>Indonesia</td>
<td>26.0</td>
<td>26.8</td>
<td>36.1%</td>
</tr>
<tr>
<td>Singapore</td>
<td>27.9</td>
<td>155.1</td>
<td>38.8%</td>
</tr>
<tr>
<td>South Africa</td>
<td>32.0</td>
<td>131.3</td>
<td>44.5%</td>
</tr>
<tr>
<td>Finland</td>
<td>36.1</td>
<td>293.6</td>
<td>50.1%</td>
</tr>
<tr>
<td>Israel</td>
<td>40.0</td>
<td>65.3</td>
<td>55.6%</td>
</tr>
<tr>
<td>Taiwan</td>
<td>42.7</td>
<td>247.6</td>
<td>59.4%</td>
</tr>
<tr>
<td>Argentina</td>
<td>44.0</td>
<td>45.8</td>
<td>61.1%</td>
</tr>
<tr>
<td>India</td>
<td>44.3</td>
<td>-</td>
<td>61.5%</td>
</tr>
<tr>
<td>Portugal</td>
<td>48.6</td>
<td>60.7</td>
<td>67.5%</td>
</tr>
<tr>
<td>Poland</td>
<td>51.6</td>
<td>31.4</td>
<td>71.7%</td>
</tr>
<tr>
<td>Greece</td>
<td>53.9</td>
<td>107.5</td>
<td>74.8%</td>
</tr>
<tr>
<td>Turkey</td>
<td>54.5</td>
<td>69.7</td>
<td>75.7%</td>
</tr>
<tr>
<td>Austria</td>
<td>56.3</td>
<td>29.9</td>
<td>78.2%</td>
</tr>
<tr>
<td>Iran</td>
<td>60.0</td>
<td>5.9</td>
<td>83.4%</td>
</tr>
<tr>
<td>Denmark</td>
<td>61.1</td>
<td>111.8</td>
<td>84.8%</td>
</tr>
<tr>
<td>Switzerland</td>
<td>71.6</td>
<td>792.3</td>
<td>99.4%</td>
</tr>
<tr>
<td>Norway</td>
<td>71.7</td>
<td>65.8</td>
<td>99.6%</td>
</tr>
<tr>
<td>Australia</td>
<td>86.8</td>
<td>372.8</td>
<td>120.6%</td>
</tr>
<tr>
<td>Brazil</td>
<td>100.6</td>
<td>226.2</td>
<td>139.7%</td>
</tr>
<tr>
<td>Spain</td>
<td>105.0</td>
<td>504.2</td>
<td>145.8%</td>
</tr>
<tr>
<td>Belgium</td>
<td>113.4</td>
<td>182.5</td>
<td>157.6%</td>
</tr>
<tr>
<td>Korea</td>
<td>118.1</td>
<td>148.4</td>
<td>164.0%</td>
</tr>
<tr>
<td>Country</td>
<td>2000 Value</td>
<td>2001 Value</td>
<td>Growth (%)</td>
</tr>
<tr>
<td>---------------------</td>
<td>------------</td>
<td>------------</td>
<td>------------</td>
</tr>
<tr>
<td>Mexico</td>
<td>125.0</td>
<td>125.2</td>
<td>173.6%</td>
</tr>
<tr>
<td>Sweden</td>
<td>133.0</td>
<td>328.3</td>
<td>184.7%</td>
</tr>
<tr>
<td>Netherlands</td>
<td>158.0</td>
<td>640.5</td>
<td>219.4%</td>
</tr>
<tr>
<td>China, Mainland</td>
<td>161.8</td>
<td>-</td>
<td>224.7%</td>
</tr>
<tr>
<td>Canada</td>
<td>178.6</td>
<td>770.1</td>
<td>248.1%</td>
</tr>
<tr>
<td>France</td>
<td>210.0</td>
<td>1,446.6</td>
<td>291.7%</td>
</tr>
<tr>
<td>Japan</td>
<td>463.0</td>
<td>3,193.9</td>
<td>643.1%</td>
</tr>
<tr>
<td>Italy</td>
<td>488.0</td>
<td>768.4</td>
<td>677.8%</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>555.2</td>
<td>2,612.2</td>
<td>771.1%</td>
</tr>
<tr>
<td>Germany</td>
<td>586.5</td>
<td>1,270.2</td>
<td>814.6%</td>
</tr>
<tr>
<td>United States**</td>
<td>2,109.7</td>
<td>15,214.6</td>
<td>2930.2%</td>
</tr>
</tbody>
</table>

Year 2000 data except for Taiwan (2001).

** U.S. market capitalization includes Amex, Chicago, Nasdaq, and NYSE.


b Source: World Federation of Exchanges.