GEORGIA vs. DELAWARE – CHOICE OF STATE OF INCORPORATION

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Introduction.

One of the most frequent questions confronting business lawyers in Georgia is the question of whether a corporate entity should either incorporate or reincorporate in Delaware or should be formed and operated as a Georgia corporation.

The answer to this question necessarily varies depending upon the setting in which it is posed. It is safe to say that for Georgia based closely-held businesses it is difficult, if not impossible, to justify the extra expense in formation, maintenance of dual qualifications (Georgia and Delaware) and, perhaps most importantly, franchise tax liability in Delaware, in order to justify the use of a Delaware corporate entity, especially when Georgia will serve as well or better as a matter of operational structure.

The issue is more squarely joined, however, when that corporate entity undertakes its first round of venture capital financing, engages in complex transactions such as mergers with a public company or, perhaps most acutely, goes public. In these settings, all of which are extremely important milestones in the corporation's life cycle, the decision is more difficult and more subtle. Often there is less than full appreciation of the significant differences that result in opting for either Georgia or Delaware.

The second and more extensive part of this paper is a summary of comparisons of the Georgia and Delaware corporate codes. These appendices are intended to be usable as a convenient reference tool to assist Georgia lawyers who are familiar with the Georgia Corporate Code in identifying and reviewing comparable provisions of Delaware and Georgia corporate law in a prompt and expeditious matter. It will also assist in identifying significant differences between the operations of the statutes.

Overview.

[1] I would particularly like to thank James Budd who has been of invaluable assistance in the completion and editing of this paper. Additional thanks to Stan Blackburn, Dana Kull, Professor Bill Carney and many members of my firm for various comments, suggestions, opinions and insights. All opinions expressed and errors contained herein are solely those of the author.

Delaware's corporate code[2] is a distinct and original statute which evolved over many years. It has particularly been affected by dynamic interaction with the New York City Bar and investment and financial houses based in New York City.[3] The Georgia statute[4], on the other hand, is derived from the Model Business Corporation Code with selected but substantial borrowings from Delaware and other statutes.[5] Both statutes have a high degree of flexibility and many similarities in operation and both are highly accommodative of the needs of modern corporate transactions. Later in this paper, we will focus on some of the more significant differences.

In truth, the decision on whether to choose Georgia or Delaware is rarely driven by the subtlety within the corporate codes themselves. These differences, as discussed below, may be significant, and in some cases may militate for or against a decision. However, there are other equally or indeed more important considerations which must also be addressed.

Major Decision Points.

1. Acceptance. One clear advantage that Delaware has as the choice for the state of incorporation is the widespread acceptance of Delaware law by lawyers, financial houses, and the securities markets. In many respects Delaware law is the *lingua franca* of corporate law. Irrespective of whether Delaware is inherently better or worse as a choice of law, it is widely accepted. Much as debate as to the technological superiority of VHS vs. Betamax formats was rendered academic by the market acceptance of the VHS format, much of the debate over the "superiority" of Delaware law over other state law is irrelevant.

Although such widespread acceptance may be a result of historical forces and the continued usage may often be an unanalyzed default reaction, the reality is that there is a large body of users throughout the United States who are familiar with the substantive provisions of Delaware corporate law. The use of Delaware does facilitate national and international transactions, particularly when the parties (and their counsel) originate in different U.S. (or foreign) jurisdictions.

Indeed, on reflection, this may well be the most compelling reason for the incorporation in Delaware in the circumstances upon which we are focusing. The issue then becomes what considerations rebut this choice.

2. Economic Value. In the public company setting, it has been argued that Delaware incorporation can actually result in an increase in value. The commentators and studies are divided on the question of whether there is a premium ascribed by the financial markets to the choice of Delaware law for incorporation, at least for publicly traded companies.

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[2] Delaware General Corporations Law 8 Del. C. §101 et. seq.

[3] *See* Demetrios G. Kaouris, *Is Delaware Still a Haven for Incorporation?*, 20 Del.J. Corp.L. 965 (1995).

[4] Georgia Business Corporations Law O.C.G.A. §14-2-101 et. seq.

[5] *See* William J. Carney, *Georgia's New Business Corporation Code*, Ga. State Bar Journal, Vol. 24, No. 4, May 1988. *See also*, William E. Eason, Jr,. *Some Distinctive Features of the Georgia Business Code*, Georgia Bar Journal, Vol. 28, No. 2, November 1991; William J. Carney, *Changes in Corporate Practice Under Georgia's New Business Corporations Code*, 40 Mercer L.Rev. 655 (1989).

Several scholars have focused on the fact that Delaware law facilitates the relatively easy sale of companies in the public market through its combination of well developed case law policed by efficient courts and a generally "shareholder friendly" structure. Thus the inability of Delaware corporations to adopt a shareholders' rights plan ("poison pill"), which cannot be revoked without the consent of at least some members of the incumbent board (a "deadhand plan"), arguably favors ready liquidity of Delaware corporate entities. In theory, this could add to value. Under this analysis, Delaware businesses are more likely to receive successful takeover bids, more hostile takeovers are likely to be successful after a negotiated premium, and therefore there may actually be a premium associated with this choice of Delaware as the jurisdiction of organization.[6]

Others, however, have examined the evidence and argue that, in fact, there is no detectable correlation between Delaware incorporation and any market premium value. Indeed, there some evidence to the contrary.[7] Therefore, to say that the choice of Delaware should be made for economic reasons is questionable at best.

And, of course, unless the company is public, the debate is largely irrelevant as the sale of a private company will invariably be a negotiated, consensual transaction.

3. <u>Clarity and Precedent</u>. It has often been said that a clear bad rule is better than an unclear good rule because a clear bad rule permits parties to plan their affairs with certainty and predictability, whereas an unclear good rule does not. This is often articulated as a compelling argument in favor of Delaware. Specifically, the plethora of precedent on significant issues in Delaware, distinguished from the relative lack of precedential authority in Georgia and other jurisdictions coupled with the Chancery Court system, arguably creates a much more predictable body of law within which to operate. As one of my partners remarked, "Georgia simply has too many cases of first impression."

Stated differently and pragmatically, even if Delaware law is not superior, it is sometimes clearer, or at least it is easier to obtain more definitive advice on a course of conduct from sophisticated counsel with a relatively higher degree of confidence as to the ultimate outcome.

For example, in the context of the statutory standards applicable to a director's conduct in the consideration of a business combination, there is no Georgia case law. The so-called "business judgment rule" is, however, closely related to this statutory standard of conduct[8]. The courts of most states that have statutory provisions the same as, or similar to, Georgia's look to Delaware case law interpreting the business judgment rule as persuasive authority in analyzing directors' duties in this setting. Thus, while the Georgia courts would not be bound by the

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[6] *See* Robert Daines, *Does Delaware Law Improve Firm Value?* 5 (New York University Center for Law and Business Working Paper #CLB-99-011, Columbia Law School Center for Studies in Law and Economics Working Paper No. 159, 1999).

[7] *See* Elliot J. Weiss and Lawrence J. White, *Of Econometrics and Indeterminacy: A Study of Investors' Reactions to "Changes" in Corporate Law*, 75 Calif.L.Rev. 551, 552 (1987).

[8] "The elements of the business judgment rule and the circumstances for its application are continuing to be developed by the courts. In view of that continuing judicial development, Section 14-2-830 does not try to codify the business judgment rule or to delineate the differences, if any, between that rule and the standards of director conduct set forth in this section." O.C.G.A. § 14-2-830 off. cmt.

Delaware cases, it is reasonable to believe that Georgia courts would look to the Delaware cases for guidance in determining whether directors of a Georgia corporation had fulfilled their legal obligations in considering proposed business combinations.[9]

As a consequence, in this and some other situations there is something to the "one horse in the barn" aspect of Delaware corporate law: even if Georgia law is applicable, in many instances resort will need to be had to Delaware precedents in the analysis of potentially difficult issues. Stated in its most mercenary fashion, in some cases there will be a reason to retain Delaware special counsel and incur the associated legal expenses, even if the transaction is one of Georgia corporate law.

By the same token, there are areas where Georgia trumps Delaware on the issue of clarity. The Georgia statutory conflicting interest rules, for instance, are objective and more precise than the Delaware statute with its heavy gloss of decisional precedents. Thus, Delaware is not always the clearer jurisdiction and sometimes the body of precedent is not helpful. Indeed, there is a substantial body of scholarly analysis which suggests that Delaware avoids brightline objective standards and opts for subjective criteria, as this encourages the proliferation of litigation and more business for Delaware lawyers.[10]

4. Effectiveness of Anti-Takeover Defenses. One question of great importance to public companies as to whether to select Delaware as the state of incorporation is the scope of anti-takeover defenses available for Delaware corporations to hostile takeovers. The great debate about the business justification for anti-takeover defenses generally is the argument that it permits the incumbent board the power to extract a greater premium from the hostile tender. If one is of this opinion, then the ability to resist hostile takeovers in a public setting is a desirable result.

Although Delaware is not unfavorable to the incumbent Board, the clear obligation of the Board to maximize shareholder value imposed by Delaware law, and the trilogy of the *Unocal*, *Time-Warner* and *Revlon* decisions impose a heavy burden on the incumbent Board seeking to resist the hostile tender or an ensuing auction of the company.[11] So if implementation of the strongest possible anti-takeover defenses is a paramount concern, it seems reasonably clear that

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[9] Santee Oil Company, Inc. v. Cox, 217 S.E. 2d 789, at 791 (S.C., 1985) (South Carolina law); International Ins. Co. v. Johns, 874 F.2d 1447, 1459 (11th Cir. 1989) (Florida law); Cottle v. Storer Communication, Inc. 849 F.2d 570 (11th Cir. 1988) (Ohio law); Gelco Corp. v. Coniston Partners, 652 F. Supp. 829 (D. Minn. 1986) *aff'd in part and vacated in part on other grounds*, 811 F.2d 414 (8th Cir. 1987). Dynamics Corp. of America v. CTS Corp., 794 F.2d 250, 253 (7th Cir. 1986) (Indiana law), *rev'd*, 481 U.S. 69 (1987); and Edelman v. Fruehauf Corp., 798 F.2d 882 (6th Cir. 1986) (Michigan law). *See also*, RUSSELL M. ROBINSON, II, ROBINSON ON NORTH CAROLINA CORPORATION LAW § 9.8 (1990) ("There is virtually no North Carolina case law on changes of control in a public corporation. Therefore, as in most other states, the North Carolina courts will probably be guided on this subject primarily by the Delaware decisions, which have extensively defined management responsibilities and procedures in an extraordinary abundance of corporate takeovers and buyouts during the past decade.")

[10] See William J. Carney, *The Production of Corporate Law*. 71 S.Cal.L.Rev. 715 (1998); Douglas M. Branson, *Indeterminacy: The Final Ingredient in an Interest Group Analysis of Corporate Law*, 43 Vand.L.Rev. 85 (1990).

[11] *See* 8 Del. C. §203. *See also*, Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946 (Del. 1985) ("Unocal"); Paramount Comm., Inc. v. Time, Inc., 571 A.2d 1140 (Del. 1989) ("Time-Warner"); Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173 (Del. 1986) ("Revlon"). Note the Georgia anti-takeover statute has higher thresholds and permits the Board to consider matters in addition to maximization of shareholder value.

Georgia is the superior jurisdiction. Thus, whether one opts for Georgia vs. Delaware in a public setting company may well focus on whether one wishes to maximize the powers of incumbent board management or, on the other hand, to facilitate takeover. Georgia's recently enacted anti-takeover statute (O.C.G.A. §14-2-624(2)(d)) permits a limited six month deadhand poison pill.[12] Such pills are not permitted in Delaware.[13]

In summary, if a primary consideration in the choice of state of incorporation is the ability to strengthen the hand of incumbent management to defend against a hostile takeover (and arguably, negotiate a higher premium on sale), it seems reasonably clear that Georgia is at a substantial advantage over Delaware.

5. Litigation Realities.

(a) Quickness of a Dispute Resolution. Delaware, with its unique Chancery Court system for the litigation of corporate matters, has a sophisticated judiciary and a highly skilled bar which is able to address quickly and expeditiously corporate disputes, generally without the intervention of the jury.[14] This is a particularly noteworthy factor in the takeover setting. This structure is often argued as a principal advantage of incorporation in Delaware and the utilization of that system.

Of course, as any litigant knows, there is a potentially darker side to this reality. From the point of view of the potential defendant takeover target, promptness of resolution is not always the optimum result. To the contrary, delay is often to the benefit of the defendant. So incumbent management could well conclude that Georgia presents a more sympathetic forum for the defendant.

(b) Sensitivity to Shareholders. Moreover, there is a consistent and powerful strain in Delaware jurisprudence deriving from the Chancery Courts to limit the power of incumbent management to frustrate the attentions of the unwanted suitor.[15] The same cannot be said for Georgia.

(c) Home Court Advantage. Finally, there can be little question that a Georgia based company defending a potential hostile takeover action or a shareholder class action suit in the Georgia court system may well result in a hearing by a judiciary (and ultimately a jury) more sympathetic to the potential target. As the *Invacare* litigation and subsequent legislative response indicates, there may be a tendency of Georgia courts to "protect our own" which would clearly be missing in litigation in Delaware.[16]

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[12] *See* O.C.G.A. §14-2-624(d)(2).

[13] *See*, Quickturn Design Systems, Inc. v. Healthdyne Technologies, Inc., 721 A.2d, 1281 (Del. 1998).

[14] See Lewis S. Black, Jr. *Why Delaware? A Practitioner Gives Reasons For Incorporation*, Corporate Counsel Weekly, Vol. 14, No. 40, Oct. 20, 1999.

[15] *See* Unocal, Time-Warner, and Revlon, *supra* note 11.

[16] *Compare* Invacare Corp. v. Healthdyne Technologies, Inc., 968 F. Supp. 1578 (N.D. Ga. 1997) and Quickturn Design Systems, Inc. v. Shapiro, 721 A2d 1281 (Del. 1998).

(d) Forum Shopping Considerations. An important issue which non-Georgia practitioners often overlook in this area is the fact that corporations incorporated in Delaware are always subject to suit in Delaware or, from corporate management's perspective, much worse, in the Southern District of New York (assuming applicable diversity and/or subject matter jurisdictional requirements can be met). This is true, even if the company's principal place of business is in Georgia and the company has no operational structure in Delaware. Under the so-called "bulge rule"[17] of the Federal Rules of Civil Procedure, a Delaware corporation is potentially subject to litigation in the Southern District of New York. This suggests several potential reasons for the use of Georgia:

1. If the corporation is incorporated and domiciled in Georgia, and the litigation proceeds in federal (or state) courts in Georgia, logistically it will be less expensive and less disruptive for the Georgia defendant to deal with the litigation process.

If, on the other hand, the litigation is in the Southern District of New York, the corporation will incur the costs, expense and disruption of defending the action in a less convenient forum. This will be potentially disruptive to the corporation through:

- management time and disruption required in travel away from home;
- lack of convenient access to books, records, documents and corporate home office support structure; and
- last, but certainly not least, the necessity for engaging counsel in New York who are unfamiliar with the company, and incurring expenses at New York rates and costs.

2. The plaintiff's securities bar is well represented by firms which litigate frequently in the Southern District of New York as well as in the Delaware system. The plaintiff's securities bar generally has offices in New York City and is well organized to proceed with class action litigation in those courts. The comparable bar in the state of Georgia is not nearly so active or so large.

3. The issue of "home court" advantage is difficult to evaluate, but many seasoned litigators, when pressed, will express a clear preference to defend an action in Georgia.

[17] Fed. R. Civ. P. 4(k). Rule 4(k) states that service of process allowed if it "is served at a place within a judicial district of the United States and not more than 100 miles from the place from which the summons issues."

6. Tax Considerations

(a) Franchise Taxes

1. Delaware. Most practitioners are aware of the fact that Delaware obtains a significant portion of its revenue from its corporate franchise tax.[18] The Delaware franchise tax is a significant cost, and certainly a good reason for a Georgia based business not to incorporate in Delaware, at least prior to an initial public offering. The corporation computes its tax under each of the two methods described, and the amount of tax is the lesser of the two amounts.[19]

The Delaware franchise tax is computed and based on one of two methods: the "authorized share" method or the "assumed par value capital" method. All corporations formed under the laws of Delaware are subject to the Delaware Franchise Tax.

(a) Authorized Share Method. The "Authorized Share Method" is computed based solely on the number of authorized (**as opposed to issued**) shares of capital stock of a Delaware corporation.

Not over 3,000 authorized shares $30.00
Over 3,000 but not over 5,000 authorized shares $50.00
Over 5,000 but not over 10,000 authorized shares $90.00
Over 10,000 authorized shares $90.00
plus $50.00 for each additional 10,000 in authorized shares or part thereof.

It should be noted that the tax is imposed on **authorized** but not on issued shares of capital stock. Since many companies which are pursuing either venture capital or public offerings will have substantial authorized stock, this tax is potentially a significant cost and clearly should be considered before the option of incorporating or reincorporating in Delaware is selected.

(b) Assumed Par-Value Capital. The second method of determining the annual Delaware Franchise Tax amount is based on the "assumed par-value capital" method. This method of computing the Delaware Franchise Tax generally requires a corporation to pay $200.00 for each $1,000,000.00 of "assumed par-value capital," or fraction thereof.

The amount of a corporation's "assumed par-value capital" is based on the following formula: The amount of the corporation's "total gross assets," as listed on Schedule L to the corporation's federal income tax return, is divided by the total number of the corporation's **issued** shares (whether or not

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[18] *See* Demetrios G. Kaouris, *Is Delaware Still a Haven for Incorporation?,* 20 Del.J. Corp.L. 965 (1995).
[19] Del. Code Ann. §8-5-502, et seq.

such shares have a par value). The resulting quotient, which represents the average asset value per issued share, is then multiplied by the authorized par-value shares in order to determine the corporation's "assumed par-value capital."

For every $1,000,000.00 in "assumed par-value capital," or fraction thereof, the corporation must pay $200.00 in Delaware Franchise Tax.

(c) Cap. Whichever method is used, the annual franchise tax is capped at $150,000.

2. Georgia. Georgia imposes a Minimum Net Worth Tax. The Georgia Net Worth Tax is a graduated tax based upon a corporation's net worth. For a new corporation, the net worth is the beginning net worth. Thereafter, it is the Net Worth on the first day of the corporation's net worth taxable year.

Net worth is defined to include: (1) issued capital stock, which is calculated by multiplying the number of issued shares of stock of the corporation by the stock's par value, (2) paid in surplus, which is the amount paid for the issued stock that is over and above the calculation of (1) above and (3) retained earnings. Treasury stock should not be deducted from issued capital stock when determining net worth.

The minimum tax on a corporation's net worth is $10.00 and that is due on net worth that does not exceed $10,000. The maximum tax on a corporation's net worth is $5,000 which is due for corporations with a net worth over and above $22,000,000. The tax is a graduated tax between the minimum and the maximum, based on the corporation's net worth.

(b) Income Tax**.**

1. Delaware. Delaware imposes an 8.7% tax on the income of corporations which is apportioned or allocated to Delaware using its apportionment and allocation formula. However, even most non-tax corporate lawyers are familiar with the fact that Delaware has an important exemption for income earned by passive holding companies (sometimes referred to as "passive investment companies" ("PIC's") or ("Delaware holding companies")).[20]

Although it is a rare case where a holding company parent will in fact meet this test, this does present potential planning opportunities, particularly for the creation of an intellectual property holding company or finance subsidiaries. An illustration of this is attached as Diagram A.

2. Georgia. Georgia imposes a 6% corporate income tax on income apportioned or allocated to Georgia. However, Georgia has no comparable provision to the Delaware PIC. Because Georgia uses the three factor

[20] 30 Del. C. §1902.

apportionment formula, with doubleweighted sales computation[21], Georgia is generally a good tax jurisdiction for operating corporations with substantial sales volume outside of Georgia. However, Georgia cannot compare favorably with the tax savings provided by a Delaware PIC as to investment income. For Georgia Corporations, income from intangibles is situsedto the corporation's domicile in Georgia and is taxable here.[22]

3. Versus Non-U.S. Parent. It should be noted that from a tax perspective, **no** U.S. jurisdiction is the best jurisdiction for an ultimate holding company parent if the company has multi-national operations with substantial income in foreign countries, as testimony before Congress recently highlighted.[23] In fact, a multi-national U.S. operation will generally be better served tax-wise if its ultimate parent entity can be reposed in either a tax haven or at least a tax friendly jurisdiction other than the United States. See Diagram B attached.

7. Share Exchange. Although both Georgia and Delaware facilitate the use of a traditional acquisitive transactions through the ability to utilize reverse triangular mergers, in Georgia the share exchange is also a permissible form of business combination. In Delaware no such mechanism is provided for in the statute.

8. Legal Costs of Formation and Operation. The variations in costs of incorporation and operating in Delaware or Georgia are not significant. Both states are moving aggressively into the electronic age, although the ability to file faxed documents in Delaware is a particularly convenient aspect of using Delaware which Georgia has not yet emulated.

Similarly, insofar as legal fees are concerned, many Georgia corporate lawyers are almost equally at home with the Delaware code and have prototype documents for both states. Moreover, Georgia lawyers regularly give Delaware corporate law opinions. It is a widespread practice that non-Delaware lawyers can and often do give Delaware corporate law opinions in connection with various matters of corporate organization, authority, and capitalization. Although the opining lawyer presumably takes on the same standards of care in such circumstances as a lawyer admitted in Delaware, the practice is recognized as permitted under Georgia standards of practice.[24] In routine corporate transactions, the practical risk is minimal. In more difficult cases, however, retention of special Delaware counsel and the associated additional cost may prove necessary, especially in sale of business or merger settings.

9. Corporate Governance Issues. The following highlights some of the major corporate law differences between the two jurisdictions.

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[21] O.C.G.A. §47-8-31(d).

[22] O.C.G.A. § 47-8-31(d).

[23] See Tax Notes, March, 15 1999 (summarizing testimony before the Senate Finance Committee of March 10, 1999).

[24] Report on Legal Opinions to Third Parties in Corporate Transactions as approved and endorsed by the Executive Committee of the Corporate Banking Law Section of the State Bar of Georgia, January 1, 1992.

(a) Indemnification. Although formerly Delaware's mandatory indemnification was broader than that offered by Georgia, amendments to the Georgia Act have eliminated significant distinctions. In Delaware, a director or officer may be exonerated "on the merits or otherwise," and this phrase has been interpreted by the Delaware courts to indemnify a director or officer even if the director or officer obtains dismissal of some but not all counts of wrongdoing.[25]

As to permissive indemnification, Delaware law contains essentially the same language as the Model Act which is incorporated in the Georgia statutes.[26]

Georgia provides for court-ordered indemnification in appropriate circumstances. There is no comparable provision in Delaware.[27] .

(b) Duties of officers and directors.

1. Duty of Care.

Georgia. Georgia's duty of care is codified and requires a "good faith belief" on the part of the director or officer in question. While former Georgia law required an objective standard of "reasonable belief," the current law standard tests the action by the "totality of the situation."[28]

Delaware. By contrast, Delaware's duty of care is under a common law standard.[29] The business judgment rule is an acknowledgment of the managerial prerogatives of Delaware directors under Section 141(a).[30] It is a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith, and in the honest belief that the action taken was in the best interests of the company.[31] Absent an abuse of discretion, that judgment will be respected by the courts. The burden is on the party challenging the action to establish this burden was not met.

In Delaware, the business judgment rule is a rebuttable presumption, and the courts generally will not second-guess decisions made in good faith by an independent and fully informed board. The business judgment rule serves to allocate the burden of proof in the first instance to a plaintiff who is

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[25] *See*, Merritt-Chapman & Scott Corp. v. Wolfson, 321 A.2d 138 (Del. Super. 1974). *Compare* O.C.G.A. §§ 14-2-851 et seq. and 8 Del. C. § 145.
[26] *Compare* O.C.G.A. §§ 14-2-851 et seq; 8 Del. C. § 145.
[27] *See* O.C.G.A. § 14-2-854.
[28] *See* O.C.G.A. § 14-2-830.
[29] *See* Zapata Corp. v. Maldonado, 430 A2d at 782; Kaplan v. Centex Corp., Del. Ch., 284 A.2d 119, 124 (1971); Robinson v. Pittsburgh Oil Refinery Corp., Del. Ch., 126 A. 46 (1924).
[30] *See* Zapata Corp. v. Maldonado, 430 A.2d at 782.
[31] Kaplan v. Centex Corp., Del. Ch., 284 A.2d 119, 124 (1971); Robinson v. Pittsburgh Oil Refinery Corp., Del. Ch., 126 A. 46 (1924).

seeking to challenge the conduct of the directors.[32] The duty of care is a duty of informed decision making.[33]

2. Duty of loyalty

Georgia. In determining whether there was a breach of loyalty, Georgia retains an objective standard.[34]

Delaware: Delaware uses a subjective standard and focuses on the effect of the financial interest on the director in question.[35]

Even though the business judgment rule and Delaware Code section 144 serve somewhat different purposes and cannot be interpreted identically, they are closely related.[36] In Delaware, § 144 does not alter the basic duty of loyalty owed by a director to the corporation which the director serves or shift the burden of proof imposed by common law upon directors to demonstrate the intrinsic fairness of the transaction to the corporation.[37] However, approval of the transaction by a disinterested majority of directors brings the business judgment rule into play and shifts the burden of proof to the challenging party.[38]

3. Conflicting Interest Transactions.

Georgia. The Georgia corporate code defines "conflicting interest" and specifically identifies the potential parties and how to remove a transaction from the purview of this rule.[39] In determining whether a director was influenced, Georgia uses an objective standard.

Delaware. Delaware law lists potential parties to conflicting interest transactions, but such list is not comprehensive, and the definition is derived common law. Under Delaware law, the tests for whether to enjoin the transaction, set it aside, or allow damages are similar.[40] Delaware uses a subjective standard and focuses on the effect of the financial interest on the director in question.[41]

(c) Amendment to Change the Number of Directors**.**

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[32] Cinerama, Inc. v. Technicolor, Inc., 663 A.2d 1156, 1162 (Del. 1995). *See* Puma v. Marriott, 283 A.2d 693, 695 (Del. Ch. 1971); Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984).
[33] Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984).
[34] *See* Comments to O.C.G.A. §14-2-860.
[35] For Georgia, *see* O.C.G.A. § 14-2-860 et seq.; Parks v. Multimedia Technologies, Inc., 520 S.E.2d 517 (1999). For Delaware, *see* 8 Del. C. §§ 102(b)(7), 144; Cede & Co. v. Technicolor, Inc., 634 A.2d 345, 364 (Del. 1993); Cinerarma, Inc. v. Technicolor, Inc., 663 A.2d 1134, 1151 (Del. Ch. 1994).
[36] HMG/Courtland Properties v. Gray, 749 A.2d 94, 112 (Del. Ch. 1999).
[37] Johnston v. Greene, 121 A.2d 919 (Del. 1956).
[38] Cede & Co. v. Technicolor, Inc., 634 A.2d 345, 366 (Del. 1993).
[39] *See* O.C.G.A. § 14-2-860.
[40] 8 Del. C. § 144(a)(3).
[41] O.C.G.A. § 14-2-860; Cede & Co. v. Technicolor, Inc., 634 A.2d 345, 364 (Del. 1993).

Georgia. In Georgia, the articles of incorporation may authorize the shareholders or the directors to fix or change the number of directors within a minimum and maximum, but if there is cumulative voting, such an amendment is not effective if the number of negative votes would be sufficient to elect a director.[42]

Delaware. In Delaware, the procedure for changing the number of directors is the same regardless of whether there is cumulative voting.[43]

(d) Creation of Staggered Boards**.**

Georgia. In Georgia, creating a staggered board by amendment to the articles of incorporation requires an affirmative vote by an absolute majority of voting shares.[44] To create a staggered board by amendment to the bylaws, the motion would need merely a majority of votes cast among the quorum at a shareholders' meeting.[45]

Delaware. In Delaware, to adopt such a bylaw, absent a prohibiting provision in the articles of incorporation or bylaws, would require a majority of shares present among the quorum at a shareholders' meeting.[46]

(e) Duties of Officers**.**

Georgia. In Georgia, a nondirector officer with discretionary authority must meet the same standards of conduct required of directors under O.C.G.A. § 14-2-830. An officer's ability to rely on information in satisfying this duty may be more limited than a director's depending on circumstances.[47]

Delaware. In Delaware, an officer's duties are established not by statute but by the bylaws or a resolution of the board.[48] The officers of a Delaware corporation are its agents, and the principles of agency law to a large degree define the officers' powers vis-à-vis third parties.[49]

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[42] *See* O.C.G.A. §14-2-803.
[43] *Compare* O.C.G.A. § 14-2-803 and 8 Del. C. § 141.
[44] *See* O.C.G.A. § 14-2-1020(c).
[45] *See* O.C.G.A. § 14-2-725(c).
[46] *See* 8 Del. C. § 216(2).
[47] *See* O.C.G.A. § 14-2-842(b).
[48] *See* 8 Del. C. § 142.
[49] *See* Joseph Greenspoon's Sons Iron & Steel Co. v. Pecos Valley Gas Co., 156 A. 350, 351 (Del. Super. 1931); Canister Co. v. National Can Corp., 63 F. Supp. 361 (D. Del. 1945).

(f) Inspection of Records**.**

Georgia. In Georgia, the right to inspect the restricted records of a corporation may be limited by the articles or bylaws for shareholders owning 2% or less of the shares outstanding.[50] A qualified shareholder may obtain a court order allowing an inspection.[51]

Delaware. In Delaware, a shareholder has the right to inspect the corporation's books and records upon written demand under oath of proper purpose, and the burden is on the corporation to establish that the shareholder has an improper purpose.[52] Any doubt of this right should be resolved in favor of the statutory right of the shareholder.[53]

(g) Shareholder Agreements.

Georgia. In Georgia, shareholder agreements that govern the exercise of corporate powers, the management of the business, and the relationships among directors as well as the relationships among the shareholders are valid if not contrary to public policy so long as the corporation is not publicly held. Such an agreement, if it limits the discretion or powers of the board of directors, shifts liability for acts of the directors upon the person in whom the agreement vests such powers and discretion.[54]

Delaware. In Delaware, shareholder agreements may bind the votes of the shareholders regarding the election of directors and proposals recommended by the board, but they may not limit the discretion or powers of the board.[55]

(h) Calling of Meetings.

Georgia. In Georgia and other Model Act states, unless modified by bylaws, 25% of the shareholders may call a special meeting.[56]

Delaware. Under Delaware law, a corporation's articles can contain provisions which make it virtually impossible for shareholders to call a special meeting.[57]

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[50] O.C.G.A. § 14-2-1602(e).
[51] *See* O.C.G.A. §14-2-1604.
[52] 8 Del. C. § 220.
[53] *See* State ex rel. Foster v. Standard Oil Co., 18 A.2d 235 (Del. 1941).
[54] *See* O.C.G.A. § 14-2-732.
[55] *See* 8 Del. C. §211(b).
[56] *See* O.C.G.A. §14-2-702(a).
[57] *See* 8 Del.C. §211.

(i) Anti-Takeover Statutes.

Georgia. In Georgia, business combinations with interested shareholders (10% to 90%) are prohibited for 5 years unless the board approved the transaction or combination that made the person an interested shareholder.[58] As noted above, deadhand poison pills for up to six months are permitted.

Delaware. In Delaware, business combinations with interested shareholders (15% to 85%) are prohibited for 3 years unless the board has approved the transaction or combination that made the person an interested shareholder.[59] Deadhand provisions are not permitted.

(j) Changes in Quorum.

Georgia. In Georgia, an amendment to the articles of incorporation or bylaws that changes or deletes a greater quorum or voting requirement must meet the same quorum requirement and be adopted by the same vote and voting groups required under the provision to be amended.[60]

Delaware. Delaware does not specifically address the issue of changes in quorum. Delaware law simply states that a corporation's certificate of incorporation or bylaws may specify the number of shares that constitute a quorum but that number cannot be set at less than one-third of the shares entitled to vote at a meeting.[61]

(k) Actions With Written Consent of Shareholders in Lieu of a Meeting.

Georgia. In Georgia, shareholders may take action by written consent in lieu of voting at a shareholders meeting. All such actions taken must be by unanimous consent unless the Articles of Incorporation provide otherwise, in which case majority consents are permitted.[62]

Delaware. In Delaware, shareholders may take action by written consent in lieu of voting at a shareholders meeting. Delaware law permits a corporation, pursuant to a provision in its Certificate of Incorporation, to eliminate the ability of shareholders to act by written consent.[63]

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[58] *See* O.C.G.A. § 14-2-1132. Irrebuttable v. rebuttable, 14-2-1131 & 1132 v. 8 Del. C. § 203. *See* Appendix pgs. 54-55.
[59] *See* 8 Del. C. § 203.
[60] *See* O.C.G.A. § 14-2-727.
[61] *See* 8 Del. C. § 216.
[62] *See* O.C.G.A. §14-2-704.
[63] *See* 8 Del. C. §228.

(l) Voting By Written Ballot.

Georgia. In Georgia there is no specific mention of the right to vote by written ballot.

Delaware. In Delaware, the right to vote by written ballot may be restricted if so provided in the Certificate of Incorporation.[64]

(m) Removal of Directors.

Georgia. In Georgia, except as otherwise provided in the corporation's Articles of Incorporation, a director of a corporation that has a staggered board of directors may be removed only with cause.[65]

Delaware. Delaware law is the same on this point.[66]

(n) Board of Directors Vacancies.

Georgia. In Georgia, unless the Articles of Incorporation or a bylaw adopted by shareholders provides otherwise, vacancies and newly created directorships may be filled by the shareholders, by the board of directors, or by a majority of the directors remaining in office, even if such directors constitute less than a quorum.[67]

Delaware. In Delaware, vacancies and newly created directorships may be filled by a majority of the directors then in office, even if such directors constitute less than a quorum.[68]

(o) Pre-emptive Rights.

Georgia. In Georgia, shareholders of all corporations do not have pre-emptive rights to acquire the corporation's unissued or treasury shares, if any, except to the extent the articles of incorporation so provide.[69]

Delaware. In Delaware, every corporation may create and issue rights or options entitling shareholders to purchase from the corporation any shares of its capital stock of any class or classes.[70]

(p) Par Value/Capital/Surplus.

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[64] *See* 8 Del C. §211.
[65] *See* O.C.G.A. §14-2-808.
[66] *See* 8 Del. C. §141.
[67] *See* O.C.G.A. §14-2-810.
[68] *See* 8 Del. C. §223.
[69] *See* O.C.G.A. §14-2-630.
[70] *See* 8 Del. C. §157.

Georgia. Georgia law dispenses with the concept of par value for most purposes, as well as "capital" and "surplus." Par value is retained as a concept for the purposes of computing certain tax liabilities.[71]

Delaware. The concept of par value, capital and surplus are retained under Delaware law and factor into such issues as the power to declare dividends.[72]

(q) Dissenter's Rights.

Georgia. In Georgia, no such rights exist with respect to a merger or consolidation by a corporation the shares of which are either listed on a national securities exchange or held of record by more than 2,000 shareholders if such shareholders are required to receive only shares of the surviving corporation, shares of any other corporation which is either listed on a national securities exchange or held of record by more than 2,000 shareholders.[73]

Delaware. Delaware law is essentially the same on this point.[74]

(r) Derivative Actions.

Georgia. In Georgia, a shareholder may not commence or maintain a Derivative proceeding unless the shareholder was a shareholder of the corporation at the time of the act or omission complained of or became a shareholder through transfer by operation of law from someone who was a shareholder at the time, and that shareholder must fairly and adequately represent the interests of the corporation in enforcing the rights of the corporation.[75]

Delaware. Delaware law is similar to Georgia law on this point. However, there is no requirement that the shareholder fairly and adequately represent the interests of the corporation in enforcing the corporation's rights.[76]

Conclusion.

In summary, it appears that Delaware provides no meaningful advantages as a state of incorporation for a Georgia based company until such time as the company considers going public.

At the venture funding stage, although many venture capital firms and out of state lawyers may push for reincorporation of a Georgia corporation into a Delaware entity in

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[71] *See* O.C.G.A. §601.
[72] *See* 8 Del. C. §§ 151, 154.
[73] See O.C.G.A. §14-2-250(d).
[74] *See* 8 Del. C. § 262. *See also*, William J. Carney, *Georgia's New Business Corporation Code*, Ga. State Bar Journal, Vol. 24, No. 4, May 1988.
[75] *See* O.C.G.A. §14-2-740 *et. seq.*
[76] *See* 8 Del. C. §327.

connection with a venture capital funding, there appears to be no clear advantage to the company or the investors in doing so, other than for the sense of comfort this gives out-of-state counsel. This must be weighed against significant potential detriments, most notably the franchise tax cost.

Finally, in the context of becoming a public company, the decision becomes more subtle and requires focus on a number of significant issues. By no means is the answer an automatic one, nor should it be taken without consideration of both the pros and cons.