

To: Corporations, Securities and Financial Institutions Committee, The Florida Bar Business Law Section

From: Subcommittee on Choice of Jurisdiction for forming For-Profit Corporations Survey

Submitted by Co-Chairs Dan Aronson and Stuart Cohn

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A survey of Business Law Section members was conducted during three weeks in March 2021, in an effort to determine the extent to which Florida lawyers are choosing Florida or other States as the jurisdiction of incorporation for their clients and the reasons that affect those decisions.

The 16-question survey was developed by the Subcommittee Co-Chairs after receiving input from Subcommittee members. The complete, tabulated survey results can be found at <https://www.surveymonkey.com/results/SM-G3VB69889/>

Nearly 200 lawyers responded to the survey. Not all respondents answered all questions. Over 70% of the respondents had more than 16 years of practice. Just over 30% of the respondents were solo practitioners. Nearly 20% were with firms in excess of 100 lawyers in Florida, while just under 14% were with firms of 51-100 lawyers in Florida.

Although LLCs have become the entity of choice for many start-ups and real estate-related entities, there continues to be a large number of corporations formed in Florida. There are over 800,000 corporations registered in Florida (including Over 98,000 formed in 2020) compared to approximately 1.7 million LLCs. The following is a summary of the Survey results:

Choice of State of Incorporation

In response to the Survey question regarding the percentage of corporations formed outside Florida in the past 5 years:

<u>Percentage of Corporations</u>	<u>Respondents' Percentage</u>
1-20%	56%
21-40%	14%
41-60%	13%
61-80%	9%
81-100%	8%

Not surprisingly, the majority of corporations organized by respondents are formed in Florida. The combined 41-100% categories total 30%.

Most Popular State(s) for Incorporation Outside Florida

<u>State</u>	<u>Percentage Response</u>
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Delaware	73%
Nevada	2%
New York	1%
Others	25%

Also as expected, Delaware was the overwhelming choice of states outside Florida to incorporate, with 73% of the respondents choosing that state. The remainder were scattered throughout the country. No other state had more than a few incorporations. Wyoming was selected by 3 respondents; Nevada was selected by two respondents.

Extrapolating from the figures, it appears that approximately 30-35% of companies formed by Survey respondents are incorporated outside Florida, with the bulk in Delaware.

Principal Decision-Makers

In terms of the principal decision-makers in determining (or influencing) the state of incorporation, the responses were:

<u>Decision-Maker</u>	<u>Percentage Response</u>
Counsel	38%
Client	36%
VC or other Investors	19%
CPA	7%
Other	2%

It is difficult to ascertain what percentage of the “client” response is based on an actual client preference or whether some respondents were simply expressing that the bottom-line decision was that of their clients. Perhaps a bit of both.

Principal Influences for Choice of State of Incorporation

Respondents were asked to rate from 1-5, 5 being the highest, the principal factors influencing the choice of a state of incorporation. Based on responses rated 4 or 5, the most influential factors noted were:

<u>Factor</u>	<u>Percentage Response</u>
Location of business or HQ	67%
Corporate statute	63%
Expectation of outside investors	62%
Ease of administrative procedures	53%
Privacy expectations	52%

Type of entity	45%
“Judicial system”	44%
Filing, formation, and fees	43%
Maturity of business	36%
Size of business	26%

We believe that the principal influencing factor, business and/or HQ location, reflects the fact that many Florida-based start-ups are incorporated in Florida. However, as reflected in other responses, when outside investors are present or anticipated, that factor weighs heavily in favor of incorporation outside Florida, particularly in Delaware. The “Judicial system” factor (couched as “quality, consistency and/or speed of judicial system”), while significant, did not rate as high as the location, administrative ease or privacy expectations factors.

Key Aspects in Florida Causing Out-of-State Incorporations

In an effort to further delineate factors affecting choice of state to incorporate, respondents were given an open question and asked to list the principal factors in Florida causing them to recommend to clients out-of-state incorporations. These are essentially negative Florida factors. Only 86 respondents answered this question. We have categorized the responses as best we could from the written comments, as follows:

<u>Factor</u>	<u>Percentage Response</u>
Judicial system and case law	21%
Privacy and required public disclosure	19%
Outside investor preference	12%
Administrative processing	7%
Client preference	3%

The remaining written responses were widely varied and difficult to categorize. For example, responses such as corporate friendliness, clarity of rules and historical reputation may all have been factors causing outside investors to require incorporation in Delaware or another state, but the “outside investor preference” percentage reflects only those responses that specifically noted that factor.

Key Factors in Florida Causing Counsel to Recommend Florida Incorporation

These are positive factors for Florida incorporations. The number of respondents to this open-ended question was only 82. It was difficult again to discern general categories based on the variety of responses. Again, we have categorized the responses as best we could from the written responses, as follows:

<u>Factor</u>	<u>Percentage Response</u>
Convenience and ease of formation	27%

Less expensive to form	20%
Good statute	12%
Lower state taxes	11%
Office location	7%
Favorable legal environment	4%

Again there could be some overlap among the categories. The lower number of respondents also appears to have affected the relationship of these answers to other Survey responses. For example, business location had received a much higher response to an earlier Survey question.

Effect of Florida’s Recent Corporate Statutory Revisions

Respondents were asked if the recent modernization of and substantial revisions to Florida’s corporate statute encouraged in-state incorporations. The responses were:

	<u>Not at All</u>	<u>Somewhat</u>	<u>Quite a Bit</u>
Start-ups	45%	44%	11%
Significant Florida Operations	44%	41%	16%
Multiple Shareholders	45%	43%	12%

The responses suggest that the recent substantial statutory revisions have been at least somewhat influential in leading Florida-based practitioners to encourage more domestic incorporations, although there are other significant factors beyond the statute’s reach, such as the presence of outside investors, privacy expectations and judicial system.

Reincorporations

Respondents were asked if they ever reincorporated Florida corporations outside the State of Florida and the reasons why. The responses (in descending order) were:

Never have	52%
Outside new investors	28%
Relocation of business	11%
Business growth	3%
Business maturity	2%
Other	3%

General observations and “take-aways” from the Survey: Overall, there is a fair amount of positives favoring Florida incorporations. Well over a majority of the corporations organized by Survey respondents (Florida-based practitioners) are formed in Florida. A key factor that causes incorporation elsewhere is the presence or anticipation of outside investors. Whether for reasons of reputation, familiarity/established usage, judicial system or other factors, outside investors often favor Delaware

incorporations. The high quality of Delaware’s judicial system and abundant case law is clearly a factor even in the absence of outside investor influence. Florida’s modernized corporate statute appears to be a positive factor favoring Florida incorporations. Although not directly questioned, the Survey did not reveal any major area where statutory reform is needed. We believe that another positive factor favoring initial Florida incorporation is the ease through our corporate statute of converting a Florida corporation to a foreign (non-Florida) corporation should subsequent factors engender a determination to change the state of incorporation.

Whether the number and percentage of future in-state incorporations will increase or decrease may be affected by continuing factors not related to Florida’s statute, although it does appear that further education of the Bar regarding the advantages (in many situations) and quality of Florida’s statute would be justified. The Subcommittee also noted that many corporations today are formed by entrepreneurs and founders using internet sites. The effect of those sites on state-of-incorporation decisions is not clear.

Limited Liability Companies

The survey also sought information regarding the formation of LLCs. Three questions were asked:

Principal Choice for Closely Held LLCs Without Significant Outside Investors:

Florida	80%
Delaware	17%
Others	3%

Is Florida Your Principal Choice (for forming LLCs) for the following types of LLCs? [STU – I SUGGEST ORDER THESE IN DESCENDING ORDER]

Single member	66%
Real estate	83%
Holding Company LLCs	68%
Multi-member	79%
Manager-managed	82%

Top three (3) factors influencing choice of LLC formation state:

Business/HQ location	66%
Expectation of Outside investors	53%
LLC statute	36%
Administrative ease	30%
Privacy Expectation	29%

Nature of entity	28%
Filing and fees	25%
Judicial system	21%
Business size	11%
Business maturity	11%

Three observations from the Survey responses related to LLCs: (1) The preference for out-of-state formation is not as strong for LLCs as for corporations; (2) the general notion that Delaware has a much higher quality judicial system and case law does not play as big a role for LLCs as for corporations; and (3) given the risk to single member LLCs caused by the Florida Supreme Court's *Olmstead* decision, now codified in Ch. 605.0503(4), we were surprised that a high percentage of single member LLCs continue to be formed in Florida. Perhaps such LLCs expect to soon have multiple members thus avoiding the foreclosure potential of the *Olmstead* decision.

Subcommittee Members: Co-Chairs Dan Aronson and Stuart Cohn, Stuart Ames, Lou Conti, Gardner Davis, Richard Denmon, David Felman, Leslie Hudock, Stefan Rubin, Phil Schwartz, Gary Teblum, Greg Yadley. BLS Fellow: Toni Tsvetanova