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Re Leonard  
Comments

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Aug 19 1976

MEMORANDUM

TO: J. R. Leonard  
FROM: J. R. Gunn *JRG*  
SUBJECT: General Comments on Mariana Islands Briefing  
Paper #12, Corporations

The central economic rationale of the corporation as a form of business enterprise stems from the fact that large-scale production is technically and economically efficient in that it reduces the unit costs of production. This is socially advantageous and should be encouraged as a matter of public policy. The corporate structure of enterprise enables larger units of capital to be subscribed more easily than any other business form, primarily because it enables investors to pool, and therefore minimize, the irreducible risks of business life. In the absence of limited liability and independent corporate life, enterprises -- and especially manufacturing enterprises -- would be much smaller, and real unit costs much higher, than they are through the legal device of the corporation.

This fundamental reasoning cannot be expected to have much impact in the Marianas case. The market is too small and geographically too dispersed for it to benefit significantly from scale economies, particularly as these apply to manufacturing operations. More relevant to the Marianas is consideration of the attraction of investment from outside the Commonwealth. In this regard it is of considerable economic importance that the Commonwealth give careful thought to creating a legal environment in which corporate activity can flourish; provided of course that such prosperity can be controlled and directed in such a way as to be beneficial

to the people of the Marianas as well as to the corporation. From this, the critical question would seem to be how to create the proper environment for corporate activity in the Commonwealth.

The Briefing Paper uses states' constitutions as a guide and frame of reference and observes that, while most states do have constitutional articles specifically governing corporations, present commentators and analysts are not at all sure such specificity is a good thing. This view is strengthened by the fact that states which have new or revised constitutions have uniformly omitted any such articles. The conclusion which I draw from the Briefing Paper is that, other things equal, the Marianas probably should leave well enough alone and not have a specific corporate article.

I question whether state constitutions are the relevant criteria for the Marianas decision on whether or not to have such an article. Rather, the decision would seem to be most appropriately made on the basis of the contribution which such an article could make to the kind of corporate activity which the Commonwealth deems most desirable. This of course requires first a determination of exactly what kind of corporate activity is wanted, a question which lies beyond the scope of the Briefing Paper. Once that issue is resolved, however, it is relevant to ask whether the inclusion in the Constitution of such an article, however worded, on corporations would enhance their development. My own judgment is that a properly worded article would have a positive effect on corporate development in the Islands. Accordingly,

I would encourage the Convention delegates to include such an article in their Constitution.

As to the provisions of the article, the ten basic subjects discussed in the Briefing Paper pretty well cover the waterfront. As the Briefing Paper notes, however, most states' constitutions go back to a period when there was concern over the abuse of corporate privilege. Many problems formerly associated with abusive corporate practices have subsequently been corrected by legislation and need not be of constitutional concern at this time. Consequently, many of the ten basic points are unnecessary. In fact, it is probably sufficient to adopt a very brief provision such as that used by the Illinois Constitution (see Briefing Paper note 3, page 2). The important thing is that the language be chosen in such a way as to put potential investors on notice that the Marianas wishes to encourage corporate activity harmonious with the social and economic development of the Commonwealth.

One further very minor comment on the Briefing Paper: paragraph 2 on page 11 is a duplicate of most of paragraph 1 on page 1, and should be deleted or at least recast.