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Delaware Authorizes Stocks on Blockchain

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On July 21st, Delaware Governor John Carney Jr. signed SB 69 into law. SB 69 amends the Delaware General Corporation Law ("DGCL") to explicitly authorize the use of distributed ledger technology in the administration of Delaware corporate records, including stock ledgers.

Distributed ledger (or "blockchain") technology-based platforms enable peer-to-peer transactions and eliminate the need for a trusted intermediary to verify and process the transactions. The potential applications of such technology in the administration of corporate records, and stock ledgers in particular, are tremendous.

As amended, DGCL §224 provides that corporate records administered by or on behalf of a Delaware corporation may be kept on "one or more electronic networks or databases (including one or more distributed electronic networks or databases)." Thus §224 explicitly authorizes the use of blockchains in the course of general corporate recordkeeping.

DGCL §219 extends that authorization specifically to stock ledgers. Notably, SB 69 amends DGCL §219(c) to define "stock ledgers" as one or more ledgers, containing certain stipulated information, that are recorded in accordance with §224.

Amendments to §§ 151, 202, 232 and 364 further facilitate the introduction of blockchain technology in corporate recordkeeping by allowing for electronic transmissions of certain required written notice to be made using a distributed ledger.

Not just any blockchain-based ledger, however, will suffice. For one, electronic corporate records must be capable of being converted into legible paper form within a reasonable time. Second, like all other Delaware stock ledgers, a blockchain ledger must be able to (i) be used to prepare a list of stockholders entitled to vote, (ii) record information required by the DGCL to be maintained in the ledger and (iii) record transfers of stock pursuant to Article 8 of the Delaware Uniform Commercial Code.

Taken together, the SB 69 amendments permit certain distributed ledgers to function as stock ledgers for Delaware corporations. This opens the door for such companies to issue, execute, settle, redeem and trade stock in such a way as to harness the benefits of the blockchain.[1]

An array of individualized and systemic benefits may be captured in the process, including:

- By eliminating intermediaries, blockchain shares might settle within moments rather than days, increasing market liquidity while freeing up capital and lowering transaction costs.

- An immutable, transparent ledger could dictate with complete certainty where each share is at any given moment in time. Bank and regulators would be better able to manage risk, and issuers to manage their capitalization tables.

- In removing the need to distinguish between beneficial and record owners, a blockchain ledger can lead to greater certainty and fairness in the realization of stockholder rights.

- Potential and existing stockholders could interact directly with issuers, and with one another, on a trusted peer-to-peer basis. This could revolutionize the ways in which issuers access the capital markets and how stockholders vote and transfer their shares.

There are also reasons for skepticism. When it comes to the application of blockchain technology to corporate governance and the capital markets, critical questions remain unanswered.

It is not yet clear blockchain technology is suited or ready to take on a major role in the global securities marketplace. While transparency may be valuable in certain instances, it could also, for instance, deter activist investors from establishing stake in a company in need of real overhaul. Likewise, the relative immutability of a given ledger may be beneficial, until a mistake occurs that ought to but cannot be readily reversed. Further, existing blockchain technology cannot currently handle the incredible daily volume of capital markets transactions with sufficient speed, if at all. A shift from permissionless to permissioned distributed ledgers certainly helps to avail some of these concerns, but in so doing raises its own set of problems with respect to access, scalability, immutability and the reinforcement of incumbents' bias toward legacy systems.

What is nonetheless certain is that there is a tremendous amount of interest, investment and momentum behind the push to apply blockchain technology to improve the fairness and functioning of the capital markets. SB 69's passage constitutes another promising, possibly historic step in that direction. And Delaware, home to two thirds of listed Fortune 500 companies and 85% of the IPOs in the United States, figures to be a key player in the days to come.

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[1] This may be done piecemeal or perhaps by creating a completely new "distributed ledger share class" that would live out its entire security lifecycle on the blockchain.

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