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Dual Class Stock

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Abstract

This chapter examines dual class common stock. Dual class stock has evolved from a vehicle used largely by insiders in family owned and media companies to retain control into a popular capital structure for founders and initial shareholders in technology start-ups. After briefly reviewing the history of dual class stock, the chapter recounts the longstanding debate over its desirability, in which defenders tout the ability of dual class to enable founders to realize their idiosyncratic visions for the firm, while critics express concern over the creation of agency costs. The chapter describes how this policy debate has led to efforts to restrict or restrain the use of dual class through stock exchange listing bans, index exclusions, proxy advisor recommendations, and sunset provision. It concludes by observing that the debate over dual class is overly simplistic in framing the issue as a binary choice. Rather dual class stock exposes the possibilities and challenges associated with the customization of shareholder control in the corporation. In particular, dual class highlights both the challenge in identifying who is a controlling shareholder and the implications of that control for traditional fiduciary duties.

Keywords: Corporate governance, dual class stock, capital structure, agency costs, stock exchange, sunset provision, shareholders, corporations, fiduciary duties, public companies, IPO market, technology industry, ownership, control, European Law, empirical studies, policy debates

JEL Classifications: G32, G38, K22

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DUAL CLASS STOCK

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Abstract

This chapter examines dual class common stock. Dual class stock has evolved from a vehicle used largely by insiders in family owned and media companies to retain control into a popular capital structure for founders and initial shareholders in technology start-ups. After briefly reviewing the history of dual class stock, the chapter recounts the longstanding debate over its desirability, in which defenders tout the ability of dual class to enable founders to realize their idiosyncratic visions for the firm, while critics express concern over the creation of agency costs. The chapter describes how this policy debate has led to efforts to restrict or restrain the use of dual class through stock exchange listing bans, index exclusions, proxy advisor recommendations, and sunset provision. It concludes by observing that the debate over dual class is overly simplistic in framing the issue as a binary choice. Rather dual class stock exposes the possibilities and challenges associated with the customization of shareholder control in the corporation. In particular, dual class highlights both the challenge in identifying who is a controlling shareholder and the implications of that control for traditional fiduciary duties.

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Introduction

The incidence of corporations with disparate voting structures, structures that this chapter will broadly term "dual class stock" continues to increase. In the United States, this growth is concentrated in smaller public companies, particularly those in the lower half of the Russell 3000,[1] and is largely due to the proportion of companies that conduct an initial public offering (IPO) with a dual class structure.[2] In the first half of 2021, for example, almost a quarter of newly public U.S. companies had dual class stock.[3] However, in Europe dual class stock is also ubiquitous in some countries – primarily through loyalty shares. One recent paper has found that "[m]ore than twice as many companies in France have unequal voting rights than those that don't have."[4] In Nordic countries, almost a third of companies have structures with unequal voting rights.[5]

Dual class stock refers to a capital structure in which a corporation issues two or more classes of common stock that have identical economic rights but differential voting rights. The classic dual class structure, sometimes described as a high vote/low vote structure, involves two classes — high vote stock, held by insiders, that is entitled to multiple votes per share, and low vote stock, held by the public, that is entitled to a single vote per share. The ratio of voting rights between the high and low vote stock varies – a common ratio is 10:1, but corporations have issued high vote stock with as many as 100 votes per share. Dual class stock structures can also involve more than two classes of stock, as well as stock that carries no voting rights at all.

Dual class structures have been around since the 1900s. The controversy over their use dates back almost as long. Opponents argue that dual class structures create agency costs and allow corporate insiders to take advantage of public shareholders. Proponents defend dual class structures for their ability to protect the corporation's ability to achieve its founders' long term strategic vision from the short term demands of public investors. Although scholars have sought to test the impact of dual class structures empirically, to date, the results of those efforts are inconclusive. The absence of definitive empirical evidence has not prevented opponents from seeking to ban or limit the use of dual class stock, or to cabin its effect through sunset provisions that require a company to convert to a single class voting structure after the passage of a specified number of years or upon the occurrence of designated events.

This chapter provide a brief history of dual class stock and situates recent developments, including the growing use of loyalty shares outside the U.S., in that history. It describes the competing arguments about dual class structures and recounts the empirical evidence marshalled in connection with those claims. It then situates dual class within a broader evolving framework about the allocation of shareholder control in the corporation. Although dual class has captured most of the attention, corporations today face a variety of emerging control structures ranging from shareholder agreements to the emergence of institutional block holders.

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The emergent forms of shareholder control present two important challenges for corporate law. First, how does the presence of a controlling shareholder affect the fiduciary responsibilities of corporate officials? In particular, how should officers and directors balance their obligations to the corporation between those who exercise voting control and minority shareholders? Second, under what circumstances do controlling shareholders themselves owe fiduciary duties to the corporation and their fellow shareholders, and how should courts distinguish between a controlling shareholder's bargained-for right to act out of self-interest and conduct that potentially violates the duty of loyalty?

Ultimately, we conclude that the rise of dual class and its variants, including sunsets, has resulted in a number of heterogenous practices in terms of adoption of dual class, terms and scope of sunsets, sunset extensions and other features of dual class, including the number of votes and size of the wedge.[6] Many of these variations appear to be without explanation and bespoke, depend upon the choices of the founder, and lack alignment with the company itself. We conclude that as further empirical work is conducted, and dual class is better understood, there should be an attempt to put forth scopes of best practices within dual class in order to provide more certainty to capital markets and investors.

I. The History of Dual Class Common Stock

A. U.S. Origins

Corporate use of dual class voting structures dates back to the early 1900s.[7] Although the number of companies with dual class structures was relatively small at that time, the dual class structure was controversial, in part because some of these companies were issuing nonvoting stock to public investors to enable insiders to retain control. Two prominent examples were Dodge Brothers, Inc. and Industrial Rayon Corporation.[8] The decision by each to issue nonvoting stock in the 1920s attracted widespread public attention. As Professor Seligman describes it, a Harvard University professor, William Ripley, criticized these decisions, focusing in particular on the sale of nonvoting common stock. [9] The media, the Justice Department, and even President Calvin Coolidge expressed concern.[10] In response to these concerns, in 1926, the New York Stock Exchange (NYSE) adopted a one share one vote rule that prohibited dual class listings.[11] As a result of the rule, from 1926 until 1986, dual class capitalization was impermissible for corporations listed on the NYSE.[12]

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The move did not eliminate dual class stock, in large part because competitors to the NYSE, the American Stock Exchange (AMEX) and Nasdaq, allowed dual class listings.[13] Over the years, some corporations went public with dual class voting structures, including family-owned firms, which used dual class to preserve family control, and media corporations that saw dual class as a way to protect their journalistic mission from capital market pressure.[14] The New York Times Corporation (NYT) was an example of both. When NYT CEO and chairman Arthur Ochs Sulzberger decided to take the company public in 1967, he wanted to preserve the Sulzberger's family control over the company and its newspaper.[15] His solution was to retain high vote shares in a family trust while issuing low vote shares to the public. The NYT went public in 1967 and, from 1969 until 1997, its low vote publicly-traded shares were traded on the AMEX. Similarly, in 1976, the NYSE informed Wang Laboratories that it could not be listed with its proposed dual class recapitalization that was designed to retain control in the Wang family. Wang Laboratories chose instead to be listed on the AMEX.[16] Despite these options, the number of public companies with dual class stock remained small.[17]

The use of dual class grew in importance in connection with the takeover contests of the 1980s.[18] It rapidly became apparent that a dual class structure was a virtually impenetrable obstacle to a hostile takeover.[19] "In the midst of a burgeoning hostile takeover environment, many issuers wasted no time in recapitalizing their capital structures into dual class stock, as a means of takeover defense, so that managers and other insiders could maintain sufficient voting control to block takeovers even though outsiders were providing the majority of the equity capital."[20] An increasing number of companies beginning with General Motors, began issuing low vote common stock.[21] This in turn increased corporate pressure on the NYSE to change its prohibition of dual class listings out of concern that, if it maintained the prohibition, it would lose listings to its competitors.[22] As a result, the NYSE proposed changes to its listing requirements that would have eliminated the prohibition on dual class.[23] The rule changes required approval from the SEC and, instead of approving the proposal, the SEC adopted Rule 19c-4, which prohibited dual class recapitalizations (although not IPOs with dual class structures).[24] The DC Circuit Court of Appeals subsequently invalidated Rule 19c-4, enabling use of dual class structures to expand.[25]

It should be noted that up through the 1980s, much of the policy debate over dual class focused on recapitalizations, in which a company that previously had a one share/one vote structure modified its capital structure to reduce or eliminate the voting rights of public shareholders. Companies that conduct their IPOs with dual class structures present somewhat different issues because shareholders investing in an IPO know ex ante whether the company will have dual class stock and can price the shares accordingly whereas a dual class recapitalization is an unexpected event.[26] Both the NYSE's proposed amendment to its listing requirements and SEC rule 19c-4 focused on recapitalizations, in part because the move toward dual class structures in the 1980s involved existing public companies. The growth of dual class IPOs, and, in particular, the importance of dual class to the technology industry, did not occur until several decades later.

B. Google and Tech Companies

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Despite the invalidation of SEC rule 19c-4, dual class remained something of a fringe capital structure.[27] Things changed when Google conducted its IPO in 2004. "Google became the first technology company to adopt [dual class] structures for the purpose of retaining control in the hands of founders, and thereafter other technology companies have followed suit."[28] Google's founders, Larry Page and Sergey Brin, explained that the dual class structure would enable them to pursue their long term vision for the company without being pressured to meet short term financial results.[29] Google's IPO was highly successful, and its use of the dual class structure became a "turning point" for modern IPO companies.[30] Following Google, "[f]rom 2004 to 2020, 12.6% of companies went public with a dual class structure, with the highest percentage of such companies going public in 2019 and 2020 and the lowest in 2006."[31]

Dual class structures are common in the technology industry – companies that went public with dual class structures included Facebook, Pinterest and Dropbox.[32] Technology firms are not the only ones to employ dual class structures, however. Other companies that have completed IPOs with dual class structures included Allbirds, Chewy, Planet Fitness and Shake Shack.[33] In addition, a few companies adopted more extreme structures. SNAP, for example, went public with three classes of stock and offered only non-voting shares to public investors.[34]

Dual class structures also have implications for the emerging debate over corporate sustainability. An ongoing challenge to corporate commitments to sustainability or environmental, social, and governance (ESG) concerns is that such commitments can sacrifice economic value. Because shareholders ultimately control the management of the corporation through their power to elect the board of directors, managers cannot commit to a value-decreasing strategy in the absence of shareholder consent; shareholder turnover in the public markets means that such consent may not persist over time. Dual class structures, in contrast, can protect the founders' desire to preserve social value.[35] Delaware public benefit corporations may also be able to protect their public benefit by adopting a golden share model, in which the corporation "divides equity into multiple classes, vesting all control rights in management and all economic rights in investors, while empowering an independent 'golden shareholder' to veto sales of the company, changes in its social mission, and certain other transformations that could undermine that mission."[36] On the other hand, some commentators argue that dual class structures gives founders greater scope to impose externalities on society. Greg Shill terms these the "social" costs of dual class stock,[37] and some empirical evidence supports the conclusion that companies with dual class underperform on various measures of environmental or social responsibility.[38] These concerns lead Vittoria Battocletti, Luca Enriques & Alessandro Romano to argue that dual class structures should be limited in companies that able to impose substantial systemic externalities.[39]

II. Non-US Variations – Loyalty Shares

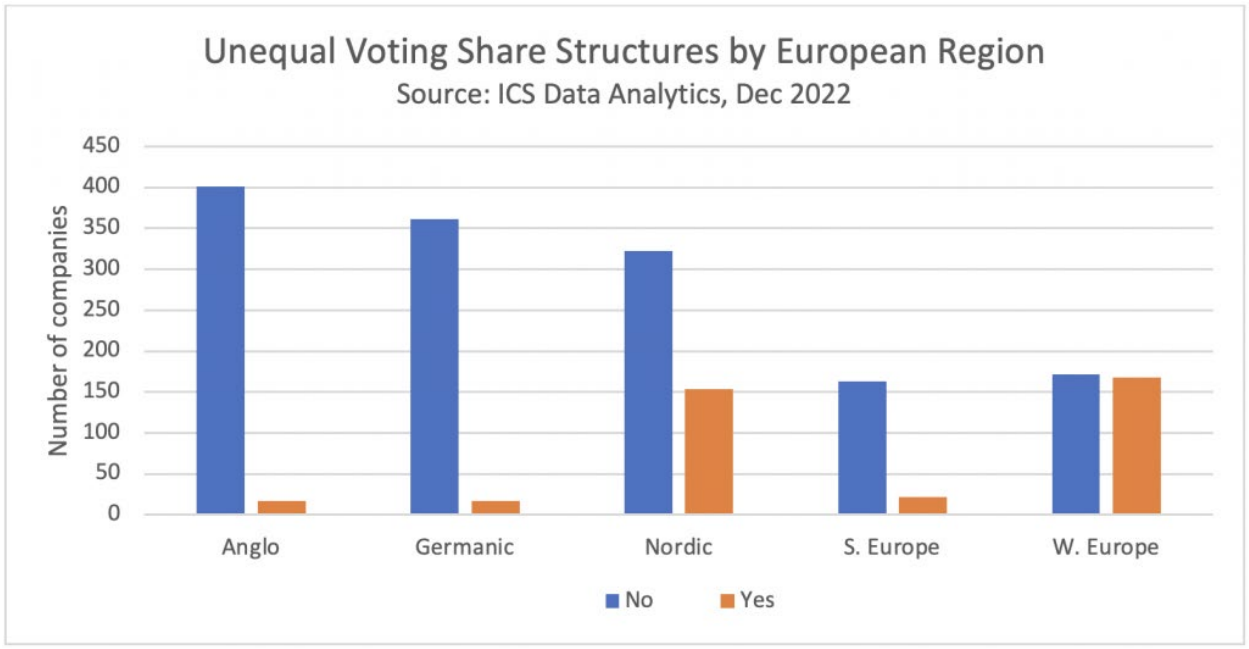
Outside the United States, the approach to companies with unequal voting structures varies. Most of the world's major stock exchanges allow dual class listings, including Hong Kong, Singapore, Shanghai, India and Tokyo.[40] Dual class structures are "gain[ing] traction" in the Asia Pacific Region.[41]

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The UK has been the exception; since 2014 listings on the premium tier of the London Stock Exchange have been required to have a one share/one vote structure.[42] However, weighted voting rights have long been permitted, with *Bushell v Faith* adjudicating that companies may validly incorporate weighted voting rights in their articles of association.[43] Subsequently, the courts have been lenient when scrutinising challenges against amendments to the articles implementing unequal voting rights. So long as there was an honest belief that the articles were altered for *bona fides* best interests of the company[44], and that "there are grounds on which reasonable men could come to the same decision,"[45] courts will uphold the alteration. Nevertheless, there are limits to the courts' generosity: (i) where some decisions are so unreasonable that no reasonable shareholder would consider that it benefits the company[46]; or (ii) where this is evidence of bad faith[47]. Yet, these narrowly construed limits, coupled with a predominantly subjective test, confer meagre protection on minority shareholders.

In 2021 HM Treasury Chair Jonathan Hill undertook a review of the competitiveness of the LSE's listing regime and, based on that review, proposed a variety of reforms, including the allowance of dual class structures.[48] In December 2021, these reforms were partially implemented; the listing requirements were revised to remove the prohibition on dual class structures. The reforms, however, did not go as far as to allow capital structures akin to those in the US – high vote stock can only be held by directors, can only be exercised with respect to specific voting issues and is subject to a mandatory five year sunset.[49] As such, although the high vote shares would be effective at blocking a hostile takeover, they would not enable a founder to retain board control.

In contrast to the United Kingdom, a number of European countries have used a different variation of capital structure with unequal voting rights – in the form of loyalty shares – as a tool for combatting short-termism. The following graph shows the dispersion of these rights as of 2023:



[50]

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France has perhaps the most extensive experience with loyalty shares, which it explicitly embraced as part of the *Loi Florange* in 2014.[51] Under the terms of the Act, investors who hold their shares for at least two years are automatically granted double voting rights unless a company specifically opts out of the regime.[52]

Several empirical studies examined the impact of the Loi Florange. They found that most of the companies that had previously had one share/one vote capital structures opted out of tenure voting, and those companies that retained tenure voting were either family firms or companies in which the French State was a large shareholder.[53] Tenure voting appears to have increased the ability of large blockholders to exercise control, but not to democratize the power of dispersed shareholders.[54]

Italy also adopted a similar tenure voting provision in 2014.[55] Unlike in France, Italy did not have a prior tradition of allowing unequal voting rights in listed companies. The provision was ostensibly adopted to encourage institutional investor engagement but, as with France, it did not have that effect and instead appeared "to further empower pre-existing long-term shareholders."[56] Other European countries allow unequal voting rights including the Netherlands, Denmark and Sweden.[57]

In the Netherlands, the concept of unequal voting rights and loyalty shares have primarily been addressed by the judiciary. This was first proposed in the *DSM* case, where DSM attempted to introduce a loyalty scheme, which was initially struck down by the Enterprise Chamber on the basis that it violates the principle of equal treatment of shareholders.[58] The Supreme Court reversed this decision by construing the equal treatment principle as requiring that shareholders who are in the same position to be treated in the same manner.[59] In the 2020 ruling of *Mediaset,* The Dutch Court of Appeal, for the first time, invalidated a loyalty share structure. Although the court found the loyalty share structure valid in principle, it concluded that the structure in this was "served solely to secure absolute control… while unreasonably prejudicing the position of [the minority shareholders]."[60]

European courts have also considered a variation on dual class - so-called "golden shares." Golden shares provide a shareholder (typically the state) with a veto over certain corporate decisions. The EU Commission has repeatedly sued Member States in the in the Court of Justice of European Union (CJEU) for implementation of golden shares. For example, in the seminal case involving Volkswagen, in Volkswagen the CJEU assessed a golden share which placed a voting cap on Volkswagen shares and certain majority requirements for major corporate actions. The Court found these measures to be incompatible with the EU Treaty.[61]

Loyalty shares can be distinguished from the US-style dual class structures in two important ways. First, the high vote shares are, at least nominally, available to all shareholders rather than being limited to insiders. This availability is more limited, however, than it initially appears. Many institutional investors cannot easily meet the recordkeeping criteria or holding period necessary to qualify for the higher voting rights.[62] Second, the higher voting rights expire automatically when the stock is transferred.

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Despite these differences, unequal voting rights are controversial in Europe. The European Union has engaged in extensive debate over whether to adopt one-share-one vote rules.[63] In 2007, the European Union after years of study decided not to adopt any plan to mandate one share one vote.[64] Since that time, the decision on differential voting has been at the country level and, as noted above, a number of companies have embraced differential voting rights. In December 2022, the EU put forth a proposal as part of the Listing Act package explicitly to permit differential voting for small and medium-sized companies (SMEs).[65]

III. The Policy Debate over Dual Class

The use of dual class stock continues to be heavily debated,[66] even though the policy arguments "have not changed much over the last 100 years."[67] The original concerns in the 1920s were that nonvoting stock disenfranchised minority public shareholders.[68] These concerns are reduced, but not eliminated, when the publicly-traded shares are low vote, as opposed to non-voting. For the most part, opponents of dual class stock argue that such structures are inimical to "corporate democracy"[69] and exacerbate agency costs,[70] while proponents argue that in protecting entrepreneurs from the pressures of the stock market, dual class structures provide for stability, long-term planning, and innovation.[71]

A. Opposition to Dual Class

Institutional investors have been at the forefront of the campaign against dual class stock. For example, the Council of Institutional Investors ("CII") supports "one share, one vote" on the basis that all shareholders, through their investments, should obtain a right to vote.[72] While CII ultimately believes "that stock with differential voting should [therefore] be barred," their recognition of the ubiquity of dual class structures has led them to advocate for time-based sunset charter provisions, rather than outright bans.[73] Institutional Shareholder Services ("ISS"), Blackrock, State Street Corporation, and T. Rowe price have all made similar shareholder-democracy-based arguments against the adoption of dual class structures.[74]

Institutional investors' distaste for dual class stock is starkly illustrated by Institutional Shareholder Services (ISS)'s 2023 voting guidelines, which mark a shift regarding companies with unequal voting rights. Since 2015, ISS's policy in the U.S. was to recommend votes against directors of newly-public companies with disfavored governance structures, such as unequal voting rights, but "ISS grandfathered companies that already had these provisions. "[75] ISS removed this carve-out in response to its 2021 benchmark policy survey, where 94% of investors and 57% of non-investors[76], advocated for a re-evaluation of this approach.[77] Accordingly, ISS will now generally recommend a withhold or against vote against directors from all covered companies with unequal voting rights.[78]

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Likewise, although ISS had not previously adopted a particular policy in continental Europe, it altered this stance in 2023. Starting February 1st, 2024, ISS will generally propose to "hold boards accountable for the existence of arrangements that allow for unequal voting rights through recommendations against specific directors or against the discharge of (non-executive) directors."[79] Although ISS has acknowledged the potential positive governance intentions, it emphasized that "equal treatment of shareholders is a key tenant of good governance"[80] and its commitment to adhering to the International Corporate Governance Network (ICGN)'s Global Governance Principle number nine.[81]

Investor opposition also reflects the concern that dual class stock exacerbates agency costs by entrenching management and preventing shareholders from holding directors accountable. Because voting rights in a dual class structure are severed from economic interest in the company, shareholders bear the financial burden of any decision making; consequently, directors, founders, and management may act in self-interest and shareholders "are less able to counteract [such] misalignment of interests."[82] The usual threats of a hostile takeover or removal are also neutralized as the typical "market monitoring function" is undermined.[83]

The concern over agency costs is heightened as the gap increases between the controlling shareholders' economic interests and their voting power, a gap that Bebchuk and Kastiel term the "wedge."[84] Bebchuk and Kastiel argue that companies "with a larger wedge between voting power and cash-flow rights are associated with more severe reductions in value and with larger agency problems."[85] They similarly argue that most companies with dual class stock have structures that enable controllers to retain control even when they reduce their economic stakes to less than 10% or 5%.[86] They argue that these companies are particularly vulnerable to "severe governance concerns and risks" and that such risks are not sufficiently transparent.[87]

The examples of Conrad Black and Sumner Redstone are often cited to illustrate these agency risks. Despite only owning minimal equity capital in Hollinger International, Conrad Black maintained voting control; this control helped him in illegally transferring thousands of the corporation's dollars to his own accounts.[88] Similarly, Sumner Redstone controlled eighty percent of Viacom's voting shares while public investors owned ninety percent of the company's equity capital; Redstone maintained this control even after concerns arose regarding his mental and physical health.[89] In both examples, shareholders were unable to wield their voting rights to rectify their concerns and minimize agency costs.

B. Support of Dual Class

The principal argument made by proponents of dual class structures is that they protect founders from the pressures of the market as they work on unique and visionary goals.[90] The leading advocates of this position are Goshen and Hamdani who argue that dual class enables entrepreneurs to realize the idiosyncratic vision that makes their companies most valuable.[91] Instead of worrying about appeasing investors who may lack expertise and information[92] and fending off activists who prioritize short-term results, founders can focus on long-term planning.[93]

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Proponents further argue that allowing founders to retain control through the use of dual class stock encourages them to go public—this not only reduces their cost of capital but it provides investors with unique investment opportunities.[94] In recent years, the number of public companies has declined by more than half and companies are staying private substantially longer.[95] As a result, Main Street investors, who are limited to investing in public companies, may miss out on valuable opportunities to participate in economic growth.[96]

Some commentators also question the value of enabling public shareholders to exercise voting rights. Commentators have expressed concerns about participation by many types of public shareholders in corporate governance.[97] As Lund explains, nonvoting stock can make corporate governance more efficient by limiting voting rights only to those shareholders who are sufficiently informed to exercise them appropriately.[98] In addition, some commentators question the claimed value of one share/one vote structures in reducing agency costs. In particular, they identify limits in the potential of shareholder democracy to produce efficient voting outcomes given heterogeneity in shareholder interests and expectations.[99] An article by Vittoria Battocletti, Luca Enriques and Alessandro Romano introduces another potential benefit, arguing that dual class shares can mitigate the potential anticompetitive effects of common ownership.[100]

IV. The Empirical Evidence

The rise of dual class stock has sparked a developing, yet to date inconclusive, body of empirical evidence. As an initial matter, some academics have argued that the IPO market offers a sufficient constraint on the inefficient use of the dual class structure. Under a traditional law and economics analysis, rational investors will take into account the potential costs and benefits of dual class at the time of the IPO.[101] In this scenario, investors will pay less for the stock at the time of the IPO if they deem dual class to be harmful. Alternatively, if they view it as beneficial, they will pay more. In either case, because dual class stock is "priced," policy prescriptions are unnecessary. And while a company's value may change over time, in a diversified market some will do better than others, meaning shareholders will earn a market return. Indeed, if market participants effectively price the potential costs associated with dual class at the IPO stage, dual class stock should be impervious to empirical analysis.

This argument assumes that markets are efficient in pricing dual class stock at the IPO stage, an assumption that is controversial. There is an extensive body of literature that argues that the IPO market is generally not efficient in pricing governance terms.[102] Moreover, this argument ignores any externalized effects of dual class stock caused by unanticipated actions by the founder or company at a later date. For example, CBS faced chaos in connection with a proposed merger with Viacom due to the conflict between Shari Redstone, who had effective control over CBS with her 10% ownership stake, and the CBS board of directors.[103] The conflict harmed employees, suppliers and other non-shareholder constituents. Even if the IPO market were efficient, the harm to non-shareholder stakeholders would go unpriced.

The uncertain theoretical basis for valuing dual class stock is matched by unclear evidence on the effect of dual class on value.[104] A number of studies of dual class firms in the era prior to Google found that dual class stock was value-decreasing.[105] These studies relied on basic agency theory as articulated by Professors Adolf Berle and Gardiner Means to understand the separation of ownership

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and control,[106] as well as a controller's theoretical motivation to take advantage of its differential voting and economic position to extract private benefits.[107] These findings also find further theoretical justification in numerous studies outside the dual class context which find that firm value and stock market returns decrease as the divergence between voting and cash flow rights increases.[108]

Another conflicting strand of research has identified potential value-increasing attributes of the dual class structure.[109] This literature attributes value to dual class in certain circumstances, including when there is information asymmetry between shareholders[110] or shareholders with a short term focus.[111] Others have found that dual class allows firms to cement long term relationships with other constituencies and to make long-term investments.[112] One working paper found that the bigger the wedge size between voting and cash flow rights, the higher the quality of financial reporting in order to attract lower vote shareholders.[113]

Lund argues that no-vote shares can "reduce agency and transaction costs" by reducing inefficiencies.[114] Many shareholders do not exercise their voting rights, so Lund argues that allowing "rationally apathetic investors" to sell their voting rights would distribute voting rights more optimally.[115] Additionally, Lehn, Netter, and Poulsen found that DCS companies have significantly higher growth in sales and number of employees, higher ratios of R&D expenditures, as well as higher increases in industry-adjusted operating income.[116] Such higher sales growth and R&D intensity is confirmed by other papers.

However, here too there is countervailing research. Masulis, Wang, and Xie found that the increased wedge between insiders' control and cash-flow rights results in lower firm valuation.[117] They identify four mechanisms for this result: "misusing corporate cash reserves, demanding excessive remuneration, engaging in shareholder value destroying acquisitions, and making poor capital expenditure decision . . . ."[118] And Lin, Shi, Tsai, and Yu argue that agency costs related to dual class ownership increase over the corporation's life cycle, as evidenced by dual class firms' cash holdings being lower than that of single class firms.[119] Hamid Beladi, May Hu, JinJin Yang, Ruicheng Zhu also argue that dual class structures exacerbate the principal-agent problem because it increases over-investment behavior.[120]

Most recently, an MSCI study found that issuers with unequal voting rights outperformed the market over a ten year period.[121] Relatedly, Ahn, Fisch, Patatoukas and Solomon created a new governance-based index, the Dual Index, which selected portfolio companies on the basis of a dual class voting structure. They then compared the performance of these corporations to various benchmarks and found that dual class companies created value in their early years.[122]

These studies are not only conflicting, but in many cases, they suffer from econometric limitations. The primary issue with finance studies of dual class stock is selection effects—namely that the companies that select into dual class structures differ, in important ways, from companies that adopt single class structures.[123] More specifically companies with value decreasing corporate governance or those otherwise prone to poor performance may select into dual class structures in order to insulate the board and executives from their poor performance. If this is the case, dual class stock is merely a symptom of poor governance or performance and not itself value reducing. Further, it would suggest that companies are able to implement these structures at the IPO stage due to inefficiencies in the IPO process itself. Relatedly, companies with strong governance and value creation mechanisms may

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prefer this structure in order to cement ties with other constituencies and truly plan for the long term. In either case, no finance study has to date adequately disentangled these effects and addressed this selection issue.

A second issue is time. Companies with dual class stock may have as life spans as long as public firms. Dual class stock may create value in the early years when the company is implementing its long-term agenda. However, dual class companies may suffer in later years as the founders become distracted or future generations take control of the company. In their paper, Cremers, Lauterbach, and Pajuste analyze this issue.[124] The authors find that in a sample of dual class firms matched with a single class sample from 1980-2015, dual class firms on average have a higher valuation at the IPO stage than single class firms, a premium which disappears over time.[125] These findings generally align with another study of the matter by Kim and Michaely, who also find that, in the early years, dual class firms have higher valuations, but in later years are less agile and dynamic.[126]

These studies address the time issue, but they too suffer from econometric issues. More specifically, in both studies the authors rely on matched pair analysis to address selection effects. In a matched pair analysis, a dual class company is matched with a similar non-dual class company to compare performance.[127] This yields a sample of comparable firms that can then be compared on an average basis. This is an accepted technique in econometrics,[128] however the quality and scope of the match always creates uncertainty. In the case of the Cremers and Kim papers we simply do not know the quality and fit of the match, particularly due to the selection issue.

In addition, most studies of time-based effects focus on firms prior to the Google IPO. The Google IPO, however, changed the mix and character of dual class stock. Post-Google, dual class structures became more wide-spread in growth companies in the technology industry but also in other industries.[129] Yet, most of the growth in dual class companies has occurred in the last several years, making the long term effect of these structures impossible to evaluate empirically.[130] For example, the Kim and Michaely study finds a turning point in the value of multi-class structures eleven years after the IPO,[131] but the vast majority of technology companies with dual class structures went public less than eleven years ago. Even if the econometric issues could be addressed, the use of dual class among modern companies and its widespread growth have yet to be fully examined.

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V. Reponses to Dual Class

A. Listings, Index Exclusions and Proxy Advisor Recommendations

Institutional investors have repeatedly requested the exchanges to ban dual class listings.[132] Exchanges have not implemented the requested restrictions, likely in response to concerns about the risk of losing clients to their competitors, analogous to the concerns that motivated the NYSE to abandon its one share/one vote requirement in 1986.[133]

An alternative regulatory approach is index exclusion.[134] In 2017, the Financial Times Stock Exchange ("FTSE") Russell, S&P Dow Jones Indices, and MSCI, adopted rules restricting the inclusion of dual class companies.[135] The rules applied only to prospective entities and grandfathered in companies that were in the index at the time of their adoption. When they were adopted, it was unclear whether the indexes would be able to maintain them if the excluded companies became growth companies similar to Google and Facebook.

The pressure index providers faced to modify the rules came to fruition in April 2023, when the S&P Dow Jones Indices (DJI) announced that it was changing its inclusion criteria to make all companies with multi-class structures eligible for inclusion in the S&P 1500 and its component indices.[136] The changes came in response to a consultation process that DJI initiated in October 2022 to solicit feedback from market participants.[137]

Finally, as noted above, proxy advisor ISS has consistently opposed dual class structures and recently extended the scope of its opposition to recommend against the election of directors at companies with dual class structures.[138]

B. Sunsets

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In response to the debate over dual class, many commentators have moved to endorse a middle ground solution: so-called "sunset provisions." These provisions offer a compromise position between an outright prohibition of dual class structures and allowing issuers to adopt freely a "perpetual" dual class structure. Sunset provisions provide that, under stipulated circumstances, an issuer's dual class structure automatically converts into a single class structure in which all shares have equal voting power. The inclusion of sunset provisions in the charters of dual class issuers can be understood as a way of balancing the protection of the founder's ability to innovate with the need to minimize agency costs. As CII explains in defense of its support of sunsets: "Since 2016 CII has supported sunset provisions if necessary to achieve alignment over a reasonable period of time."[139] SEC Commissioner Jackson stated that, unless the higher voting rights had a sunset provision, they were "antithetical to our values as Americans."[140] In support of his position that dual class companies should include sunset provisions, Commissioner Jackson reported the results of preliminary empirical analysis showing that the valuations of dual class IPO companies with sunset provisions diverged from and exceeded the valuations of those companies with perpetual dual class stock, beginning two years after the IPO.[141] Similarly, Professors Lucian Bebchuk and Kobi Kastiel present empirical evidence that the adverse effects of dual class stock increase over time and advocate sunset provisions as a response to this problem.[142]

The debate over sunset provisions has focused primarily on time-based sunset provisions that eliminate higher voting rights after a designated period of time—commonly seven to ten years. According to a study by Andrew Winden, of a sample of 139 companies with dual class stock, only two companies had time-based sunset provisions prior to 2010, but currently eighteen percent have time-based sunsets.[143] For companies that went public in 2010 or after, 35% of dual class companies have a time-based sunset.[144] Time-based sunsets are appealing, in part because they seem to offer a solution to the empirical findings reported by Commissioner Jackson and Professors Bebchuk and Kastiel (i.e., that the potential advantages of a dual class structure decline over time). However, Fisch and Solomon argue that this appeal is surface-driven.[145] Time based sunsets are arbitrary in their application—and they may take effect either too late or too early.[146] In other words, they often take effect before or after the founder is either economically disengaged or otherwise providing value to the enterprise through the use of dual class stock.

Instead of the noisy proxy of a term limit sunset for assessing the desirability of retaining the dual class structure, Fisch and Solomon suggest other more closely tailored sunset provisions—that is, issuer-specific developments that potentially erode the desirability of dual class.[147] They postulate that the most important of these developments are substantial dilution of the founder's stake; transfer of high voting stock to a non-founder; and death, incapacitation, or departure of the founder.[148] Regardless, it appears that sunset provisions are here to stay, and their form and adoption is idiosyncratic in nature. In other words, there is no uniform approach to which type of sunset a company adopts for dual class and its mechanisms, or whether such a sunset is even adopted.

C. Sunset Extensions

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The growth in both dual class IPOs and dual class structures that incorporate sunset provisions leads to a new conceptual problem—sunset extensions. In some cases, either the passage of time or a reduction in the controlling shareholder's economic interest may trigger a sunset provision, but corporation may wish to avoid the operation of that sunset and extend its dual class structure. In *City Pension Fund for Firefighters and Police Officers in the City of Miami v. The Trade Desk, Inc.*, the Trade Desk faced this issue and applied an MFW procedure to the decision to extend the sunset.[149] The Delaware Chancery Court found that the decision was appropriate.[150]

More difficult questions arise in cases in which a corporation is found not to have made a decision in accordance with the MFW standard. Does any decision to extend a dual class structure trigger entire fairness scrutiny? If so, how should a court apply the entire fairness standard to the decision?[151]

The flip side of sunset extensions are transactions that terminate a dual class structure prior to or in the absence of a sunset provision. Many companies with dual class structures include equal treatment provisions in their charters that limit the ability of a controlling shareholder to receive disparate compensation in such a transaction.[152] To the extent that a dual class structure has become inefficient, however, it may be desirable both to allow a controller to receive a premium in exchange for surrendering its superior voting rights and to limit the procedural obstacles to such transactions.

VI. Dual Class and Allocations of Control

Traditionally commentators have drawn a binary distinction between companies that have one share/one vote structures and companies with dual class structures. Recent research demonstrates, however, that this dichotomy is misleading. In addition to capital structures, corporations can use shareholder agreements to allocate control rights by contract.[153] As a practical matter, such shareholder agreements have the attributes of dual class voting structures in that shareholder control need not be proportionate to economic interest. Gladriel Shobe & Jarrod Shobe term these "de facto dual-class corporate-governance structures."[154] They collect data showing that a substantial number of companies that nominally have a single class of stock use contracts to give insiders disproportionate control. This can include the ability to approve or disapprove corporate decisions, appoint a majority of the board, and obtain non-public information.[155] Gabriel Rauterberg presents similar data, finding that fifteen percent of recently-public companies went public with shareholder agreements that commonly allocated control rights such as the power to vote for directors or veto corporate transaction.[156] These findings demonstrate that, as a practical matter, departures from the standard one share/one vote structure are more common than many commentators believe.

What explains the use of de facto dual class structures as opposed to traditional dual class structures? Rauterberg suggests that corporations may prefer the increased flexibility associated with allocating control rights by contract rather than through charter provisions.[157] Shareholder agreements can be modified without formal corporate action. In addition, because these corporations do not have formal multi-class capital structures, they generally escape the criticism aimed at dual class companies.

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A notable difference between contractual allocations of control and dual class is that contracts facilitate control-sharing among minority shareholders; indeed, contracts enable minority shareholders to wield powers beyond those conveyed by their economic stakes – most commonly, the power to obtain board representation. As Rauterberg observes, these allocations raise concerns both about shareholders' decisions to enter into these agreements, which are arguably not subject to fiduciary limitations, and whether the existence of these agreements subsequently imposes such duties on the contracting shareholders on the theory that they are part of a control group.[158]

VII. The Future of Dual Class

As the preceding section observes, dual class is not a binary concept – there are multiple ways to delink control from economic ownership. The range and persistence of mechanisms to allocate control rights differentially suggest that, despite the potential for increased agency costs, corporations realize value from customizing their control structures in ways that depart from the standard one share/one vote regime. Alternatively, market forces may operate effectively to limit those agency costs even in companies with dual class structures.[159] Moreover, as a structural matter dual class stock is unlikely to be prohibited – it is now a feature of the worldwide capital markets. This potential, however, raises several distinctive concerns from a traditional corporate law perspective.

First, delinking control and economic ownership foregrounds the analytical question of what it means to be a controlling shareholder. The issue is important both because controlling shareholders are, in some contexts, subject to fiduciary duties and because transactions involving a controlling shareholder may be subject to a higher level of judicial scrutiny.[160] The Delaware courts have explicitly recognized that one can be a controlling shareholder through a combination of share ownership and the contractual power to exercise certain shareholder rights such as controlling the composition of the board and the power to veto certain transactions.[161] What the courts have yet to address is the threshold level of control that triggers these obligations.[162] Similarly, the courts have not considered the extent to which these obligations should be extended to minority shareholders who act collectively pursuant to a dual class structure or voting agreement.[163]

Second, and relatedly, what is the impact of shareholder control on traditional fiduciaries, especially corporate directors? In *Trados,* the Delaware courts considered a capital structure in which preferred shareholders exercised control of the board, and the court viewed this control as problematic in that the board's primary obligation ran to common shareholders.[164] Dual class structures present a somewhat different situation, however, in that they involve a single class of common stock. Delaware law provides that director fiduciary duties run to the corporation and its shareholders, but when common shareholders have heterogeneous interests, does that obligation run to the majority of shareholders, those shareholders with a majority of voting interests, or to minority shareholders?

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Third, while we identify the empirical issues and conflicting evidence, we are optimistic about future empirical research. More specifically, as the number and type of companies adopting dual class continues to increase, the sample available for empirical analysis grows. We are also obtaining significant data in terms of operating performance of these companies. There is significant heterogeneity in the provisions of the sunsets of these companies. All of this will provide valuable data to researchers to analyze the effects of dual class and address the selection and other effects which pervade this research.

At the same time, the heterogeneity in dual class structures – both with respect to the terms of the dual class and the sunset provisions that may apply, raises, for us, several questions. Although the heterogeneity may be a product of firm-specific differences and variation in the extent to which insiders possess market power at the time of the IPO, we question whether the nature of the IPO process is reasonably calculated to lead to efficient governance structures or whether heterogeneity produces inefficient opacity about the extent and likely duration of insider control. Can investors evaluate the differences and price them at the IPO stage? Does the presence of an investment bank intermediary provide or preclude a robust negotiation? We also wonder about the failure to converge on more standardization in dual class structures.

Finally, to the extent that shareholders with high vote stock are treated as controlling shareholders, under what circumstances should decisions by the board trigger entire fairness review? Are decisions favoring founder preferences, particularly non-economic preferences such as sustainability, to be considered self-dealing?[165] Given the substantial number of corporations with dual class structures, identifying the scope of corporate decisions that merit heightened judicial oversight is particularly important because such decisions could, in principle, be subject to business judgment deference if the corporation employs an MFW procedure.[166] Compliance with the MFW conditions is demanding, however, and is unlikely to be standard operating practice. As a result, clear judicial guidance as to the circumstances under which it is warranted is particularly important.

VIII. Conclusion

Ultimately, we conclude that the rise of dual class and its variants, including sunsets, has resulted in substantial heterogeneity among companies in terms of adoption of dual class and its terms, the applicability and type of sunset provisions, sunset extensions, and equal treatment provisions in mergers and other transactions. Many of these variations appear to be without explanation and bespoke, depend upon the choices of the founder and lack alignment with the company itself. We conclude that as further empirical work is conducted and dual class is better understood there should be an attempt to develop best practices within dual class in order to provide more certainty to capital markets and investors.

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[1] For data on the percentage of Russell 3000 companies excluding the S&P 1500 with unequal voting rights between 2019 and 2022, see Subodh Mishra, "Dual Class Share Structures: Is the Sun Setting Too Slowly?", Harv. L. Sch. F. on

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Corp. Governance, Dec. 19, 2022, available at https://corpgov.law.harvard.edu/2022/12/19/dual-class-share-structures-is-the-sun-setting-too-slowly/#more-153402 (last visited Feb. 17, 2023).

[2] Our focus in this chapter is on public companies with dual class capital structures. We note that dual class structures are also used in private companies. See, e.g., "The Terms Behind Unicorn Valuations", Fenwick Insights, Feb. 10, 2016, available at https://www.fenwick.com/insights/publications/the-terms-behind-unicorn-valuations (reporting on the percentage of unicorn companies in 2014-2015 with dual class common stock).

[3] In the first half of 2021, 24% of U.S. company IPOs included a dual class structure. See Council of Institutional Invs., "Dual-Class Stock", available at https://www.cii.org/dualclass_stock (last visited Feb. 17, 2022).

[4] Paul Hodgson, "Dual Class Share Structures: The European Experience," Institutional Shareholder Services, Feb. 6, 2023, available at https://insights.issgovernance.com/posts/dual-class-share-structures-the-european-experience/.

[5] Id.

[6] See also Dhruv Aggarwal, Ofer Eldar, Yael V. Hochberg & Lubomir P. Litov, "The rise of dual-class stock IPOs", 144 J. Fin. Econ. 122 (2022) (observing that "not all dual-class firms are the same" and creating database allowing differentiation along several dimensions).

[7] For a cogent history of the shift from "democratic" to "plutocratic" voting in the nineteenth century and the development of other variations in shareholder voting rights see Sarah C. Haan, "Voting Rights in Corporate Governance: History and Political Economy", __ S. Cal. L. Rev. __ (forthcoming) available at https://ssrn.com/abstract=4299462.

[8] Joel Seligman, "Equal Protection in Shareholder Voting Rights: The One Common Share, One Vote Controversy", 54 Geo. Wash. L. Rev. 687, 694 (1985).

[9] Id.

[10] For a description of Congress and President Calvin Coolidge's threats about dual class capital structures, see, e.g., Louis Lowenstein, "Shareholder Voting Rights: A Response to Professor Gilson", 89 Colum. L. Rev. 979, 982 (1989).

[11] Id.

[12] Notably, however, the NYSE did not appear to apply its policies uniformly; in 1956, the NYSE allowed Ford Motor Co. to list its shares despite its dual class structure and by 1985, ten companies listed on the NYSE had dual class structures. See Seligman, *supra* note 8, at 694. For a list of the companies listed on the NYSE with a dual class structure, see Andrew Winden, "Sunrise, Sunset: An Empirical and Theoretical Assessment of Dual-Class Stock Structures", 2018 Colum. Bus. L. Rev. 852, 855 n. 31 (2018).

[13] For a brief description of AMEX's and Nasdaq's policies, see Winden, *supra* note 12, at 864.

[14] Ari Grinapell, "Dual-Class Stock Structure and Firm Innovation", 25 Stan. J.L. Bus. & Fin. 40, 47 (2020) ("Over the years, dual-class structure has been considered justified for certain types of firms, often on the grounds of their specific needs; for instance, family-owned firms have used dual-class structure to preserve control over their businesses, and the media sector has used it to allow media firms to concentrate on objective news coverage")

[15] Joe Nocera, "How Punch Protected the Times", The New York Times, Oct. 1, 2012, available at https://www.nytimes.com/2012/10/02/opinion/nocera-how-punch-protected-the-times.html (last visited Feb. 17, 2023).

[16] Winden, *supra* note 12, at 864.

[17] For data on the number of companies listed with dual class structures on the AMEX or Nasdaq in 1985, see Lowenstein, *supra* note 10, at 983.

[18] On the use of dual class structures as a takeover defense during the 1980s takeover wave, see, e.g., Min Yan, "A Control-Accountability Analysis of Dual Class Share (DCS) Structures", 45 Del. J. Corp. L. 1, 11 (2020).

[19] On this, see Paul A. Gompers, Joy Ishii & Andrew Metrick, "Extreme Governance: An Analysis of Dual-Class Firms in the United States", 23 Rev. Fin. Stud. 1051, 1052 (2010).

[20] Bobby V. Reddy, "More than Meets the Eye: Reassessing the Empirical Evidence on U.S. Dual-Class Stock", 23 U. Pa. J. Bus. L. 955, 964 (2021).

[21] See, e.g., Gladriel Shobe & Jarrod Shobe, "The Dual-Class Spectrum", 39 Yale J. on Regul. 1343, 1351 (2022).

[22] Zoe Condon, "A Snapshot of Dual-Class Share Structures in the Twenty-First Century: A Solution to Reconcile Shareholder Protections with Founder Autonomy", 68 Emory L.J. 335, 346 (2018).

[23] NYSE's Proposed Rule Changes on Disparate Voting Rights, 18 Sec. Reg. & L. Rep. (BNA) No. 34, at 1389 (proposed Sept. 19, 1986).

[24] Voting Rights Listing Standards; Disenfranchisement Rule, 53 Fed. Reg. 26376, 26380, 26394 (codified as amended in 17 C.F.R. § 240.19c-4 (1988)).

[25] *Bus. Roundtable v. SEC*, 905 F.2d 406, 417 (D.C. Cir. 1990).

[26] For a rejection of dual class recapitalization and comparison with companies with dual class at the IPO stage, see, e.g., Jeffrey Gordon, "Ties that Bond: Dual Class Common Stock and the Problem of Shareholder Choice", 76 Cal. L. Rev. 3 (1988).

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[27] "In 2005, only 1% of IPOs listed on U.S. exchanges had a dual-class structure, most of which were media firms wishing to ensure journalistic editorial independence, or other firms led by a team of insiders." Grinapell, *supra* note 1414, at 43-44.

[28] Yan, *supra* note 18, at 11. On Google as a trailblazer, see also Reddy, *supra* note 15, at 966-67.

[29] On this, see Google, Final Prospectus, U.S. Securities and Exchange Commission, Aug. 18, 2004, available at https://www.sec.gov/Archives/edgar/data/1288776/000119312504143377/d424b4.htm#toc59330_1.

[30] Shobe & Shobe, *supra* note 21, at 1354.

[31] Id.

[32] Thomas J. Egan, James Thompson, Ivy Wong, & Mark Bell, "The Revival of Dual Class Shares," Int'l Fin. L. Rev., Spring 2020, at 27.

[33] "Dual Class List, No Wedge," Jan. 24, 2023, available at https://councilofinstitutionalinv-my.sharepoint.com/:x:/g/personal/onedrive_cii_org/EZhCaASpEnJHmdnotaJvGQMBB9Q71bQ_sBPCBz-YBX_2ng?rtime=ue1FefsN20g (last visited Feb. 17, 2023).

[34] Non-voting shares are used by other companies such as CBS, Visa, and Blue Apron. See Shane Keenaghan, "S&P, Russell Indexes Push Back on Snap's Non-Voting Stock", Aug. 2, 2017, available at https://www.glasslewis.com/snap-multi-class-share-structures-suffer-rebuke-major-indices/ (last visited Feb. 17, 2023). Similarly, at the time of its IPO, Airbnb had four classes of common stock. David Trainer, "Investors Can Rest Well with Airbnb's IPO", Forbes, Dec. 3, 2020, available at https://www.forbes.com/sites/greatspeculations/2020/12/03/investors-can-rest-well-with-airbnbs-ipo/?sh=38977482179d ("Airbnb is going public with 4 separate share classes, each with different voting rights.").

[35] See, e.g., Jill Fisch & Steven Davidoff Solomon, "The 'Value' of a Public Benefit Corporation", 83 n. 81 in RESEARCH HANDBOOK ON CORPORATE PURPOSE AND PERSONHOOD (Elgar, Elizabeth Pollman & Robert Thompson eds., 2021) ("Notably the increasing tendency of at least some founders to use dual class stock to retain voting control after taking a company public offers a potential way to insulate a PBC's social purpose from some of this vulnerability."). Veeva's decision to convert to a public benefit corporation was reportedly a response to the perception that the sunset of founder and CEO Peter Gassner's super voting rights would impair its continued commitment to its social purpose. With the Sunset of Its Dual Class Arriving, Veeva Systems (VEEV) Decides to Embrace Stakeholder Governance and Become a Public Benefit Corporation, Transactional Delights, Oct. 28, 2021, available at https://www.transactionaldelights.com/content/with-the-sunset-of-its-dual-class-arriving-veeva-systems-veev-decides-to-embrace-stakeholder-governance-and-become-a-public-benefit-corporation (last visited Apr. 26, 2023). See also Emilie Aguirre, "Beyond Profit", 54 U.C. Davis L. Rev. 2077, 2130 (2021).

[36] Naveen Thomas, "Golden Shares and Social Enterprise", 12 Harv. Bus. L. Rev. 157, 161 (2022). Thomas cites two examples of corporations with golden share structures -- Ziel and Creative Action Network. See id. at 171.

[37] Gregory H. Shill, "The Social Costs (and Benefits) of Dual-Class Stock", 75 Ala. L. Rev. __ (forthcoming 2023).

[38] See, e.g., Barry Hettler, Arno Forst, James Cordeiro & Stacy Chavez, "Excess insider control and corporate social responsibility: Evidence from dual-class firms", J. Acct'g & Pub. Policy 106877 (2021) (reporting a negative association between insider control and firms' CSR performance); Paul Seaborn, Tricia D. Olsen & Jason Howell, "Is Insider Control Good for Environmental Performance? Evidence From Dual-Class Firms", 59 Bus. & Soc. 716 (2020)(reporting that "on average, dual-class firms underperform their single-class peers on environmental measures and that the discrepancy comes from dual-class firms where insiders have more voting control, relative to their equity stake").

[39] Vittoria Battocletti, Luca Enrique & Alessandro Romano, "Dual Class Shares in the Age of Common Ownership" (April 1, 2022). Available at https://ssrn.com/abstract=4046244.

[40] Bobby V. Reddy, "Up the Hill and Down Again: Constraining Dual-Class Shares", 80 Cambridge L.J. 515 (2021).

[41] CFA Institute, "Dual-Class Shares: The Good, The Bad, and The Ugly: A Review of the Debate Surrounding Dual-Class Shares and Their Emergence in Asia Pacific", 39 (2018), https://www.cfainstitute.org/-/media/documents/survey/apac-dual-class-shares-survey-report.pdf.

[42] Bobby V. Reddy, "Finding the British Google: Relaxing the Prohibition of Dual-Class Stock from the Premium-Tier of the London Stock Exchange", 79 Cambridge L.J. 315 (2020).

[43] *Bushell v Faith* [1970] AC 1099.

[44] *Allen v Gold Reefs of West Africa Ltd* [1900] 1 Ch 656.

[45] *Shuttleworth v Cox Bros and Co (Maidenhead)* [1927] 1 Ch 154.

[46] *Re Charterhouse Capital Ltd* [2015] EWCA Civ 536.

[47] *Citco Banking Corporation NV v Pusser's Ltd* [2007] UKPC 13.

[48] Reddy, *supra* note 40.

[49] Bobby Reddy, "The UK's Dual–Class Shares Reforms – Failing to Throw off the Shackles", Oxford Bus. L. Blog, Jan. 30, 2022, https://blogs.law.ox.ac.uk/business-law-blog/blog/2022/01/uks-dual-class-shares-reforms-failing-throw-shackles#:~:text=Dual%E2%80%93class%20shares%20structure%20is,different%20levels%20of%20voting%20rights.

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[50] Institutional Shareholder Services, "Dual Class Share Structures: The European Experience," Feb. 6, 2023.

[51] Prior to 2014, tenure voting was permitted in France, and more than half of French companies used it, but the default voting system was one share/one vote, and companies were required explicitly to opt into tenure voting. Marco Becht, Yuliya Kamisarenka & Anete Pajuste, "Loyalty Shares with Tenure Voting: Does the Default Rule Matter? Evidence from the Loi Florange Experiment", 63 J.L. & Econ. 473, 475 (2019)

[52] Id.

[53] Id. at 495.

[54] Id. This finding is in accord with at least one study of the potential effect of tenure voting adoption in the United States. Paul H. Edelman, Randall S. Thomas, and Wei Jiang, "Will Tenure Voting Give Corporate Managers Lifetime Tenure?", 97 Tex. L. Rev. 991 (2019).

[55] Emanuele Bajo, Massimiliano Barbi, Marco Bigelli & Ettore Croci, "Bolstering Family Control: Evidence from Loyalty Shares", 65 J. Corp. Fin. (2020).

[56] Gaia Balp & Giovanni Strampelli, "Empowering Institutional Investors in Concentrated Ownership Contexts: The Case of Italy", 17 S.C. J. Int'l L. & Bus. 1, 30 (2020).

[57] Becht et al., *supra* note 51, at 495.

[58] Carolyn Bandel, "Dutch court bans DSM loyalty bonus" IPE Magazine, Mar. 29, 2007, https://www.ipe.com/dutch-court-bans-dsm-loyalty-bonus/21700.article. Technically, the DSM proposal was a loyalty dividend. Id.

[59] "Dutch court says DSM could pay loyalty dividend," Reuters, Dec. 14, 2007, https://www.reuters.com/article/dsm-dividend/dutch-court-says-dsm-could-pay-loyalty-dividend-idUSL1434689920071214.; Loyens Loeff, Trend Report Recent developments in Dutch loyalty share schemes, 2020, https://www.loyensloeff.com/globalassets/02.-publications-pdf/01.-internal/2020/trend-report-loyalty-schemes-in-the-netherlands.pdf.

[60] Loyens Loeff, *supra* note 59.

[61] Case C-112/05 Commission v Germany [2007] ECR I-8995. See also WG Ringe. 'Case C-112/05, Commission v. Germany ("VW law"), Judgment of the Grand Chamber of 23 October 2007' (2008) 45 CML Rev 537.

[62] BlackRock, "Key considerations in the debate on differentiated voting rights", Investment Stewardship Commentary, https://www.blackrock.com/corporate/literature/whitepaper/blackrock-the-debate-on-differentiated-voting-rights.pdf (last visited Feb. 20, 2023).

[63] This debate is chronicled in Wolf-Georg Ringe, "Deviations from Ownership-Control Proportionality—Economic Protectionism Revisited", U Bernitz and WG Ringe (eds), Company Law and Economic Protectionism (Oxford Univ. Press, 2010).

[64] C McCreevy, Speech at the European Parliament's Legal Affairs Committee, 3 October 2007, Speech/07/592.

[65] Proposal for a Directive of the European Parliament and of the Council on multiple-vote share structures in companies that seek the admission to trading of their shares on an SME growth market, Brussels, 7.12.2022 COM(2022) 761 final 2022/0406 (COD).

[66] This debate is spurred, in part, by the increase in companies with dual class stock. While the majority of U.S. companies have a single-class structure, nearly "one in four (24%) U.S. companies that went public in the first half of 2021 did so with a dual class structure." *Dual-Class Stock*, **Council of Institutional Invs.,** https://www.cii.org/dualclass_stock (last visited Feb. 9, 2023).

[67] Shobe & Shobe, *supra* note 21, at 1351-52.

[68] See, e.g., Egan, Thompson, Wong, & Bell, *supra* note 32, at 27.

[69] Robert Jackson, "Perpetual Dual-Class Stock: The Case Against Corporate Royalty", Feb. 15, 2018, available at https://www.sec.gov/news/speech/perpetual-dual-class-stock-case-against-corporate-royalty (last visited Feb. 17, 2023). For an argument that dual class structures are inherently undemocratic, see Kara M. Stein., Comm'r, Sec. & Exch. Comm'n, "Remarks at Stanford University: Mutualism: Reimagining the Role of Shareholders in Modern Corporate Governance", Feb. 13, 2018, available at https://www.sec.gov/news/speech/speech-stein-021318#_ednref45) (last visited Feb. 17, 2023).

[70] On this, see Yan, *supra* note 18, at 15.

[71] Id. at 19 ("[S]uch insulation can provide visionary entrepreneurs and founders the freedom to pursue and implement their idiosyncratic business ideas without worrying unduly about stock market performance."). There can be an economic benefit to a founder's vision being realized. See Zohar Goshen & Assaf Hamdani, "Corporate Control and Idiosyncratic Vision", 125 Yale L.J. 560, 560, 565-67 (2016).

[72] Council of Institutional Invs., *supra* note 3.

[73] Jill E. Fisch & Steven Davidoff Solomon, *The Problem of Sunsets*, 99 B.U. L. Rev. 1057, 1075 (2019).

[74] *See* id.

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[75] Cydney Posner, "ISS Issues Benchmark Policy Updates for 2023", December 23, 2022. Harvard Law School Forum on Corporate Governance, https://corpgov.law.harvard.edu/2022/12/23/iss-issues-benchmark-policy-updates-for2023/#:~:text=ISS%20has%20previously%20observed%20that,have%20unequal%20voting%20rights%20structures.%E2%80%9D.

[76] Id.

[77] Id.

[78] Institutional Shareholder Services, United States Proxy Voting Guidelines Benchmark Policy Recommendations, Dec. 13, 2022, https://www.issgovernance.com/file/policy/active/americas/US-Voting-Guidelines.pdf?v=1. The ISS recommendation does not apply to newly-public companies with a time-based sunset provision of no more than seven years or companies that provide sufficient protection for minority shareholders "such as allowing minority shareholders a regular binding vote on whether the capital structure should be maintained."

[79] Institutional Shareholder Services, "Proposed ISS Benchmark Policy Changes for 2023", https://www.issgovernance.com/file/policy/2022/2023-Benchmark-Policy-Changes-For-Comment.pdf.

[80] Id. Some European investors have been highly critical of the policy change. See, e.g., Richard Milne, "Sweden's Jacob Wallenberg hits out at ISS over dual-class share attack", Fin. Times, Apr. 10, 2023.

[81] International Corporate Governance Network, "CGN Global Governance Principles", 2021, https://www.icgn.org/sites/default/files/2021-11/ICGN%20Global%20Governance%20Principles%202021.pdf

[82] Shobe & Shobe, *supra* note 21, at 1352.

[83] Yan, *supra* note 18, at 18. It should be noted that the extent to which dual class insulates a controller from market pressure may be overstated. Yifat Aran and Elizabeth Pollman find that a significant number of controllers are "ousted" despite the seeming protection of dual class for reasons that include economic underperformance, regulatory pressure or corporate scandals. Yifat Aran & Elizabeth Pollman, "Ousted", Theoretical Inquiries in Law (forthcoming 2024)

[84] Lucian A. Bebchuk & Kobi Kastiel, "The Untenable Case for Perpetual Dual-Class Stock", 103 Va. L. Rev. 585, 591 (2017) ("When the wedge between the interests of the controller and those of the public investors grows over time, the agency costs of a dual-class structure can also be expected to increase.").

[85] Lucian A. Bebchuk & Kobi Kastiel, "The Perils of Small-Minority Controllers", 107 Geo. L.J. 1453, 1473 (2019).

[86] Id. at 1457.

[87] Id. at 1499.

[88] Condon, *supra* note 22, at 353.

[89] Id. at 353-54.

[90] Shobe & Shobe, *supra* note 21, at 1353.

[91] Goshen & Hamdani, *supra* note 71, at 565-67.

[92] For an argument about the costs associated with an investor's lack of expertise and self-interested conduct, see Yan, *supra* note 18, at 21.

[93] See Daniel R. Fischel, "Organized Exchanges and the Regulation of Dual Class Common Stock", 54 U. Chi. L. Rev. 119, 137-38 (1987).

[94] For an argument that dual class stock helps reduce the cost of capital and provides unique investment opportunities, see Grinapelli, *supra* note 14, at 82.

[95] Jay Clayton, Chairman, U.S. Sec. Exch. Comm'n, Remarks to the Economic Club of New York, Sept. 9, 2019, available at https://www.sec.gov/news/speech/speech-clayton-2019-09-09 (last visited Feb. 17, 2023). ("On the other hand, (i) we have roughly half the number of public companies we had twenty years ago; (ii) growing companies are staying private substantially longer;")

[96] Id.

[97] For an argument that index and passive funds lack adequate incentives to vote intelligently, see, e.g., Dorothy S. Lund, "The Case Against Passive Shareholder Voting", 43 J Corp L 493, 506-20 (2018); Kobi Kastiel & Yaron Nili, "In Search of the 'Absent' Shareholders: A New Solution to Retail Investors' Apathy", 41 Del. J. Corp. L. 55, 99 (2016) (warning that "uninformed retail investors could also support proposals that are not beneficial to the corporation.").

[98] Dorothy S. Lund, "Nonvoting Shares and Efficient Corporate Governance", 71 Stan. L. Rev. 687 (2019).

[99] Yan, *supra* note 18, at 8-9.

[100] Battocletti, et al., supra note 39.

[101] For an argument that corporate governance issues are priced into transactions, see Frank H. Easterbrook & Daniel R. Fischel, The Corporate Contract, in THE ECONOMIC STRUCTURE OF CORPORATE LAW, 17-19 (1991).

[102] On this, see, e.g., Robert Daines & Michael Klausner, "Do IPO Charters Maximize Firm Value? Antitakeover Protection in IPOs", 17 J.L. Econ. & Org. 83, 86-113 (2001).

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[103] Chloe Aiello, "CBS fight is 'the beginning of the end' of dual-share structures, says former NBCUniversal CEO", CNBC, May 18, 2018, https://www.cnbc.com/2018/05/18/ex-nbc-ceo-cbs-fight-is-the-beginning-of-the-end-of-dual-share-structures.html.

[104] For a summary of the empirical literature on the effects of dual class structure, see, e.g., Anita Anand, "Governance Complexities in Firms with Dual Class Shares", 3 Annals of Corp. Governance 184, 203-07 (2018).

[105] See, e.g., Henry DeAngelo & Linda DeAngelo, "Managerial Ownership of Voting Rights: A Study of Public Corporations with Dual Classes of Common Stock", 14 J. Fin. Econ. 33 (1985); Ronald C. Lease, John J. McConnell & Wayne H. Mikkelson, "The Market of Control in Publicly-Traded Corporations", 11 J. Fin. Econ. 439 (1983); Tatiana Nenova, "The Value of Corporate Voting Rights and Control: A Cross-Country Analysis", 68 J. Fin. Econ. 325 (2003); Luigi Zingales, "Insider Ownership and the Decision to Go Public", 62 Rev. Econ. Stud. 425 (1995). Notably, however, these studies focused primarily on family-owned and media companies, which are very different from the technology companies that have adopted dual class structures more recently.

[106] See Adolf A. Berle & Gardiner C. Means, The Modern Corporation and Private Property (1932).

[107] See, e.g., Alexander Dyck & Luigi Zingales, "Private Benefits of Control: An International Comparison", 59 J. Fin. 537, 540 (2004) ("The use of a company's money to pay for perquisites is the most visible but not the most important way in which corporate resources can be used to the sole (or main) advantage of the controlling party.").

[108] For data on a firm's value being negatively associated with the wedge between insiders' cash-flow rights and voting rights, see, e.g., Paul A. Gompers, Joy Ishii & Andrew Metrick, "Extreme Governance: An Analysis of Dual-Class Firms in the United States", 23 Rev. Fin. Stud. 1051, 1084 (2010); see also Michael L. Lemmon & Karl V. Lins, "Ownership Structure, Corporate Governance, and Firm Value: Evidence from the East Asian Financial Crisis", 53 J. Fin. 1445, 1447 (2003); Karl V. Lins, "Equity Ownership and Firm Value in Emerging Markets", 38 J. Fin. & Quantitative Analysis 159, 181 (2003).

[109] For an argument as to how dual class structures may increase firm value, see Lucian Arye Bebchuk, "Why Firms Adopt Antitakeover Arrangements", 152 U. Pa. L. Rev. 713, 714-17 (2003).

[110] Armen A. Alchian & Harold Demsetz, "Production, Information Costs, and Economic Organization", 62 Am. Econ. Rev. 777, 783 (1972).

[111] Jeremy C. Stein, "Takeover Threats and Managerial Myopia", 96 J. Pol. Econ. 61, 61-64 (1988); Jeremy C. Stein, "Efficient Capital Markets, Inefficient Firms: A Model of Myopic Corporate Behavior", 104 Q.J. Econ. 655, 661-65 (1989).

[112] For an argument that reduced exposure to competition may encourage investments in innovation, see Henry DeAngelo & Linda DeAngelo, "Managerial Ownership of Voting Rights: A Study of Public Corporations with Dual Classes of Common Stock", 14 J. Fin. Econ. 33, 35 (1985). For efficiency justifications for defensive tactics, including dual- class structures, see Jean-Jacques Laffont & Jean Tirole, "Repeated Auctions of Incentive Contracts, Investment and Bidding Parity, with an Application to Takeovers", 19 RAND J. Econ. 516, 530-31 (1988). For an argument that incumbent managers are successful because of the relationships of trust they build with stakeholders, see Andrei Shleifer & Lawrence H. Summers, "Breach of Trust in Hostile Takeovers", in Corporate Takeovers: Causes and Consequences 33, 40-41 (Alan J. Auerbach ed., 1988).

[113] Rimona Palas, Dov Solomon, Dalit Gafni & Ido Baum, , "Does Wedge Size Matter? Financial Reporting Quality and Effective Regulation of Dual-Class Firms", Sept. 13, 2022, available at https://ssrn.com/abstract=4217935.

[114] Lund, *supra* note 98, at 694.

[115] Id. at 695.

[116] Kenneth Lehn, Jeffry Netter & Annette Poulsen, "Consolidating Corporate Control: Dual-class Recapitalizations Versus Leveraged Buyouts", 27 J. Fin. Econ. 557, 559 (1990).

[117] Ronald W. Masulis, Cong Wang, & Fei Xie, "Agency Problems at Dual-Class Companies", 64 J. Fin. 1697, 1698 (2009).

[118] Id. at 1699-1700.

[119] James Juichia Lin, Wei-Zhong Shi, Li-Fang Tsai & Min-Teh Yu, "Corporate Cash and the Firm's Life-cycle: Evidence from Dual-class Firms," 80 Int'l Rev. Econ. & Fin. (2022).

[120] Hamid Beladi, May Hu, JinJin Yang, & Ruicheng Zhu, "Dual-class Stock Structure and Firm Investment", Fin. Rsch. Letters, June 2022, at 1.

[121] For research indicating that dual class structured corporations outperformed other stocks from November 2008 to August 2017, see Dimitris Melas, "Putting the Spotlight on Spotify: Why Have Stocks with Unequal Voting Rights Outperformed?", MSCI (Apr. 3, 2018), available at https://www.msci.com/www/blog-posts/putting-the-spotlight-on/0898078592 (last visited Feb. 19, 2023).

[122] Byung Hyun Ahn, Jill E. Fisch, Panos N. Patatoukas, & Steven Davidoff Solomon, "Synthetic Governance", 2021 Colum. Bus. L. Rev. 476, 482 (2022).

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[123] For a discussion of the problem of selection effects in the study of dual class firms, see, e.g., Martjin Cremers, Beni Lauterbach, & Anete Pajuste, "The Life-Cycle of Dual Class Firm Valuation", Rev. Corp. Fin. Stud. (2022).

[124] Id.

[125] Id.

[126] For data showing that dual class firms have higher valuations initially but decline in value as they mature, see Hyunseob Kim & Roni Michaely, "Sticking Around too Long? Dynamics of the Benefits of Dual-Class Voting", ECGI Finance Working Paper No. 590/2019, available at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3145209, at 19.

[127] For an example of this, see Cremers, Lauterbach & Pajuste, *supra* note 123, at 15-16.

[128] For an overview of matching methodologies in empirical research, see, e.g., Elizabeth A. Stuart, "Matching Methods for Causal Inference: A Review and a Look Forward", 25 Stat. Sci. 1 (2010).

[129] See *supra* notes ?? and accompanying text.

[130] For data on the growth of Russell 3000 companies with dual class structures between 2015 and 2016, see, e.g., Rob Kalb & Rob Yates, "Snap, Inc. Reportedly to IPO with Unprecedented Non-Voting Shares for Public", Harv. L. Sch. F. on Corp. Governance & Fin. Reg. (Feb. 7, 2017), available at https://corpgov.law.harvard.edu/2017/02/07/snap-inc-reportedly-to-ipo-with-unprecedented-non-voting-shares-for-public/ (last visited Feb. 19, 2023).

[131] Kim & Michaely, *supra* note 126, at 18.

[132] Daniel Wells, "Shareholder Inequity in the Age of Big Tech: Public Policy Dangers of Dual-Class Share Structures and the Case for Congressional Action", 13 Ne. U. L. Rev 41, 57 (2021).

[133] Id. See also Scott Hirst & Kobi Kastiel, "Corporate Governance by Index Exclusion", 99 B.U. L. Rev. 1229, 1241 (2019) ("A long debate regarding state competition for incorporations has shown that competition for incorporations and listings will lead states and exchanges to follow the preferences of those that make incorporation and listing decisions - in this case corporate insiders").

[134] See generally Hirst & Kastiel, *supra* note 133 (evaluating index exclusion as a response to dual class).

[135] Shobe & Shobe, *supra* note 21, at 1355. For an explanation of these index and listing exclusions see Fisch & Solomon, *supra* note 73, at 1076.

[136] Wilson Sonsini Goodrich & Rosati, "S&P Dow Jones Indices Opens Door for Multi-Class Share Companies", JDSupra, Apr. 21, 2023, available at https://www.jdsupra.com/legalnews/s-p-dow-jones-indices-opens-door-for-3292064/.

[137] Id.

[138] See notes 75 through 81*, supra* and accompanying text. We note the limited impact of ISS recommendations at companies with dual class structures in light of the controlling shareholders' inherent power to elect the board.

[139] Fisch & Solomon, *supra* note 73 at 1062.

[140] Jackson, *supra* note 69.

[141] Id.

[142] Bebchuk & Kastiel, *supra* note 84, at 590.

[143] Winden, *supra* note 12, at 870.

[144] Id. at 871.

[145] Fisch & Solomon, *supra* note 73.

[146] Id.

[147] Id.

[148] Id.

[149] Kahn v. M & F Worldwide Corp., 88 A.3d 635 (Del. 2014).

[150] *City Pension Fund for Firefighters & Police Officers in City of Miami v. The Trade Desk, Inc.*, No. CV 2021-0560-PAF, 2022 WL 3009959 (Del. Ch. July 29, 2022).

[151] See David Berger, Jill Fisch & Steven Davidoff Solomon, "Extending Dual Class Stock: A Proposal", Theoretical Inquiries in Law (forthcoming 2023).

[152] See Caley Petrucci, "Equal Treatment Agreements: Theory, Evidence & Policy", Yale J. Reg. (forthcoming 2023).

[153] Gabriel Rauterberg, "The Separation of Voting and Control: The Role of Contract in Corporate Governance", 38 Yale J. on Reg 1124, 1128.

[154] Shobe & Shobe, *supra* note 21, at 1361.

[155] Id. at 1347, 1368.

[156] Rauterberg, *supra* note 153, at 1129.

[157] Id. at 1128.

[158] Id. at 1130.

[159] See Aran & Pollman, *supra* note 83.

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[160] See e.g., *In re CNX Gas Corp. S'Holders Litig.*, 4 A.3d 397 (Del. Ch. 2010).

[161] In re KKR Fin. Holdings LLC S'holder Litig., 101 A.3d 980 (Del. Ch. 2014), aff'd, Corwin v. KKR Fin. Holdings LLC, 125 A.3d 304 (Del. 2015).

[162] See Tornetta v. Musk, 250 A.3d 793, 801 (Del. Ch. 2019) (holding that, for purposes of motion to dismiss, plaintiff adequately pled that Elon Musk, who owned 21.9% of Tesla's stock as well as serving as Chairman, CEO and Chief Product Architect, was Tesla's controlling stockholder).

[163] A related concern is the extent to which other shareholders might be subject to fiduciary duties, particularly when they act collectively to influence corporate decisions. For an argument that minority activist shareholders should be subject to fiduciary duties when they exercise "ad hoc control") see Iman Anabtawi & Lynn Stout, "Fiduciary Duties for Activist Shareholders", 60 Stan. L. Rev. 1255 (2008).

[164] In re Trados Inc. S'holder Litig., 2009 Del. Ch. LEXIS 128.

[165] See eBay Domestic Holdings, Inc. v. Newmark, 16 A.3d 1 (Del. Ch. 2010).

[166] See, e.g., Tornetta v. Musk, 250 A.3d 793, 810 (Del. Ch. 2019) ("MFW provides a roadmap that allows fiduciaries to engage in conflicted controller transactions worthy of pleadings stage business judgment deference.").

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