Dual-Class Contracting

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Dual-class companies are often touted as an example of contractual customization of corporate governance, based on the view that they deviate from the default rule of "one share, one vote" to fit the specific characteristics of individual companies. But voting inequality is a spectrum, not a binary choice, and we know little about how different dual-class companies choose their level of voting inequality along this spectrum.

In this Article, I seek to shed light on this phenomenon by presenting and discussing quantitative and qualitative data on dual-class IPOs, including a comprehensive sample of dual-class charters and a survey of capital markets lawyers with expertise in dual-class IPOs. The corporate charters analyzed span 27 years, from 1996 to 2022, and the survey respondents include more than three dozen partners of law firms that have represented over two-thirds of the U.S. dual-class companies that have gone public in the past decade.

This Article has three main goals. The first is to map the dual-class landscape and to document standardization and customization of voting inequality across almost 300 companies and three decades. The second is to reconstruct the "contracting process" that shapes dual-class charters and the role of key market players in this process. The third is to situate this real-world picture within the standard framework of the "classic contractarian theory," the richer and more nuanced insights of "modern contractarian theories," and the work of sociologists and economists on the emergence and evolution of social norms.

The resulting picture shows that, despite a broad spectrum of possible tailor-made options, most dual-class companies choose similar or identical levels of

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voting inequality, innovation in market practice happens quite rapidly after long periods of equilibrium, and lawyers perceive themselves as playing a much more important role than investment bankers in shaping the "dual-class contract." I suggest that both the traditional account of contractual optimization and the more nuanced theories of learning externalities and agency problems are insufficient to explain some peculiarities of dual-class contracting. I propose an alternative conjecture in which "market norms" play an important role alongside atomistic contracting, lawyers serve a crucial sociological function as transmitters of these norms, and "norm innovation" happens less through rational design than through random mutation and the deliberate action of "norm entrepreneurs."

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INTRODUCTION

The default voting rule in corporate law is "one share, one vote."[1] At Amazon, for example, founder and CEO Jeff Bezos owns 11% of the shares and may cast 11% of the votes.[2] At Walmart, the Walton family owns 46% of the shares and may cast 46% of the votes.[3] The voting power of controlling or influential shareholders is thus proportionate to the size of their investment.

A growing number of large and innovative companies, however, especially in the technology sector and in the platform economy—such as Alphabet, Meta, Airbnb, Lyft, and Zoom—go public with a dual-class structure, in which founders and other insiders have greater voting power than public investors.[4] In these companies, some shareholders can cast a majority of votes with only a minority of shares. This is the case, for example, at Meta Platforms (formerly Facebook), where founder and CEO Mark Zuckerberg has 14% of the shares and 61% of the votes;[5] at Alphabet (formerly Google), where founders Sergey Brin and Larry Page have 6% of the shares and 52% of the votes;[6] and at Ralph Lauren Corp., where the eponymous founder has 39% of the shares and 86% of the votes.[7]

Dual-class structures are one of the most controversial topics in corporate governance. Many find them objectionable, on the grounds that they violate fundamental principles of shareholder democracy, reduce accountability of managers, and distort the controller's incentives to create value for all shareholders. Others, in contrast, believe that dual-class structures protect the founders' entrepreneurial vision from myopic market pressures, improve the controller's incentives with respect to risk-taking, and strengthen the managers' bargaining power vis-à-vis buyers of the company.[8] The debate remains unresolved.[9]

The choice between dual-class and single-class structures has been the subject of academic and policy debates for many years. But voting inequality is a spectrum, not a binary choice. A dual-class structure that allows the controller to have a majority of votes with only 4.8% of the shares (such as the one chosen by Pinterest, for example) is much more unequal than a dual-class structure that requires the majority shareholder to have at least

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1. DEL. CODE ANN. tit. 8, § 212 (2020) ("Unless otherwise provided in the certificate of incorporation . . . each stockholder shall be entitled to 1 vote for each share of capital stock held by such stockholder."); MODEL BUS. CORP. ACT § 7.21(a) (AM. BAR. ASS'N 2023) ("[U]nless the articles of incorporation provide otherwise, each outstanding share, regardless of class or series, is entitled to one vote on each matter voted on at a shareholders' meeting.").

2. Amazon.com, Inc., 2024 Proxy Statement (Form 14A) 84 (May 22, 2024). More precisely, Bezos owns 938,251,817 shares and has sole voting power on an additional 184,282,131 shares, likely due to an irrevocable proxy or a shareholder agreement. *Id.*

3. Walmart, Inc., 2024 Proxy Statement (Form 14A) 119 (Apr. 25, 2024). Family members have direct or indirect ownership and shared voting power on 3,654,717,654 shares and individual ownership and voting power on an additional 58,796,471 shares. *Id.*

4. *See* Jill E. Fisch & Steven Davidoff Solomon, *Dual Class Stock* 2 (Univ. of Penn. Inst. for L. & Econ., Rsch. Paper No. 23-21, 2023) ("The incidence of corporations with disparate voting structures . . . continues to increase.").

5. Facebook, Inc., 2024 Proxy Statement (Form 14A) 66 (Apr. 19, 2024).

6. Alphabet, Inc., 2024 Proxy Statement (Form 14A) 38 (Apr. 26, 2024).

7. Ralph Lauren Corp., 2023 Proxy Statement (Form 14A) 50, 115 (June 22, 2023).

8. *See infra* Part I.A.

9. *See* Jill Fisch & Steven Davidoff Solomon, *The Problem of Sunsets*, 99 B.U. L. REV. 1057, 1061 (2019) ("The debate over whether dual-class structures increase or decrease corporate value is, to date, unresolved.").

35% of the shares (such as the one adopted by Cognizant).[10] In fact, by this measure, Cognizant's dual-class structure is closer to a single-class structure such as Amazon's (where a majority shareholder must own 50% plus one shares) than to Pinterest's dual-class structure. If the choice between a single-class structure like Amazon's and a dual-class structure like Cognizant's is significant and worthy of careful analysis, so must be the choice between a dual-class structure like Cognizant's and a dual-class structure like Pinterest's.

Similarly, a dual-class structure that may last for the entire life of the founders (such as the one chosen by Google, for example) or in perpetuity (such as the one chosen by Facebook) is much more unequal than a dual-class structure that expires after five years (such as the one chosen by Groupon).[11] Once again, if voting inequality matters, then the choice between temporary inequality or lifelong or perpetual inequality must be taken seriously.

Unlike the "categorical" choice between dual-class and single-class structures, however, the "continuous" choice of specific levels of voting inequality remains little studied. How much variation and customization are there within dual-class structures? What is the contribution of the various market players to the final shape of these structures? Do real-world dual-class arrangements adapt to different characteristics of companies and controllers, as the textbook model predicts? How do dual-class structures evolve and what might explain the patterns of change or persistence?

This Article sheds light on these questions by examining both quantitative and qualitative evidence on initial public offerings (IPOs) of U.S. dual-class companies. I analyze and discuss a hand-collected sample of dual-class charters adopted at the IPOs by U.S. nonfinancial companies, as well as the findings from a survey of more than three dozen law firm partners with expertise on dual-class IPOs. The charters included in this study represent a comprehensive sample of all dual-class IPOs by U.S. nonfinancial companies from 1996 to 2022, totaling 293 corporate charters. Respondents to the survey and the follow-up interviews are senior IPO lawyers, working at elite law firms that have assisted more than two-thirds of dual-class issuers between 2013 and 2022.

The Article has three goals. The first goal is to map the dual-class landscape and to document variation and customization of voting inequality and dual-class charters across almost 300 companies and three decades. To this end, I have built a comprehensive sample of dual-class structures and will focus on the levels of voting inequality contracted for at the IPO, rather than measuring voting inequality at the time of the IPO (as is instead customary in the finance literature). As I will show, voting inequality may and does change after the IPO; hence, identifying the level of voting inequality accepted in the charter is, I believe, a better measure of what shareholders have bargained for.[12] In addition to

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10. Unless otherwise indicated, throughout the Article all the references to the voting structure of specific dual-class companies derive from the dataset built for this Article (and on file with the *Journal of Corporation Law*). *See infra* Part I.C.1.

11. *See* Lucian A. Bebchuk & Kobi Kastiel, *The Untenable Case for Perpetual Dual-Class Stock*, 103 VA. L. REV. 585, 589 (2017) (exploring problems that stem from perpetual dual-class stocks such as a founder's health declining or losing touch with the fast-moving technology sector).

12. Previous research, by Professors Andrew Winden, Professors Lucian Bebchuk and Kobi Kastiel, and Professors Dhruv Aggarwal, Ofer Eldar, Yael Hochberg, and Lubomir Litov, has tackled the specific question of variation across dual-class charters. *See generally* Andrew W. Winden, *Sunrise, Sunset: An Empirical and*

quantitative evidence based on the review of IPO charters, I also collect and analyze qualitative evidence from senior practitioners in the attempt of understanding the dynamics of real-world "contracting" in dual-class IPOs.

I measure voting inequality in two dimensions: *degree* and *duration*. I measure the *degree* of voting inequality by calculating, for each dual-class charter, the smallest percentage of common stock that a high-vote shareholder must own to have 50% of the votes.[13] I call this metric the "control lock."[14] I measure the *duration* of voting inequality by calculating the combined effect of charter provisions that allow high-vote shareholders to keep a dual-class structure in place over time.

One important finding is that, despite a broad spectrum of possible tailor-made options, most dual companies choose similar or identical levels of voting inequality. In theory, dual-class companies can choose a control lock from slightly above 0% (extreme inequality) to slightly below 50% (very low inequality). Furthermore, they can choose whatever duration of voting inequality they think is most appropriate for their company, from a few months to the entire life of the corporation. But in practice most companies conform to strikingly similar patterns.

Over the entire 27-year period, 62% of companies chose a control lock in the very narrow range between 9% and 10%, and less than 7% chose a control lock greater than 20%. Furthermore, between 1996 and 2010, 96% of dual-class structures had a potentially lifelong (27%) or perpetual (69%) duration; then the landscape changed dramatically, and between 2011 and 2022 only 58% of dual-class companies chose lifelong or perpetual structures. Perpetual structures became quite infrequent (21% in the 2011–2022 period, 13% in 2021–2022). Interestingly, with limited exceptions, *degree* and *duration* of voting inequality are not statistically associated with characteristics that, according to the previous literature, predict the categorical choice between dual-class and single-class structures. In other words, it seems that the continuous choice is largely unanchored from the characteristics that affect the categorical choice.

The second goal is to reconstruct the "contracting process" that shapes dual-class charters. In a 2006 article, Professor Michael Klausner observed that the fact that "corporate contracts reflect a high degree of uniformity" rather than "fulfilling their contractarian role as the locus of innovative and customized corporate contracting" warrants "at least

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Theoretical Assessment of Dual-Class Stock Structures, 2018 COLUM. BUS. L. REV. 852 (analyzing the IPO charters of 139 dual-class companies and identified a variety of charter provisions); Lucian A. Bebchuk & Kobi Kastiel, *The Perils of Small-Minority Controllers*, 107 GEO. L.J. 1453 (2019) (examining 170 dual-class charters (adopted at the IPO or at a later stage) and found that many dual-class controllers were potentially able to maintain control with small or very small fraction of common stock); Dhruv Aggarwal et al., *The Rise of Dual-Class Stock IPOs*, 144 J. FIN ECON. 122 (2022) (examining the effect of outside funding options on the degree of voting inequality in dual-class companies, measured by the "wedge" of the controller at the IPO).

13. This methodology was first proposed by Professors Lucian Bebchuk and Kobi Kastiel. *See* Bebchuk & Kastiel, *supra* note 12, at 1493–95.

14. This way to measure voting inequality is different from the one typically found in the finance literature, which is the so-called "wedge" (that is, the difference) between cash flow rights and voting rights. The wedge is typically measured at the IPO (or at another reference date) and therefore is only a snapshot of voting inequality at a given point in time. As I will show, the wedge almost always varies significantly across time, with many companies with a smaller wedge ending up having a larger one, or vice versa. By contrast, the control lock measures the maximum degree of voting inequality that investors have agreed to and therefore is a more accurate measure of the degree of voting inequality "bargained for" between insiders and public investors. For more details, see *infra* Part I.B.2.

some rethinking of the contractarian theory . . . ."[15] Even Klausner, however, considered dual-class structures as an exception to such a uniform landscape and one of the very few instances of "deliberate contracting. . . in the drafting of corporate charters."[16]

But what counts as "deliberate contracting"? The picture emerging from the experience of top IPO lawyers shows that "norms" and "precedents" play a crucial role in the shaping of dual-class structures. The textbook story is that corporate insiders "bargain" with the investment banker, who acts as representative of the public investors, and the governance features ultimately chosen by the company tend to maximize the joint surplus of insiders and public investors, given the individual characteristics of the company. However, the real-world picture painted by the senior lawyers who participated in the survey and the follow-up interviews shows that the pricing of dual-class features is surrounded by high uncertainty, and companies tend to comply with "market norms" rather than tailoring the levels of voting inequality to their specific circumstances. Indeed, neither investment bankers nor investors are perceived to play an important role in designing dual-class structures, whereas founders, venture capitalists (VCs) and—surprisingly—issuer lawyers are believed to play a significant role. Both issuer lawyers and investment bank lawyers perceive the role of issuer lawyers as crucial in shaping or reshaping the founders' preferences based on the existing "market practice." This story is at odds with the textbook model: contrary to this model, in the real world, the main preoccupation of IPO insiders has less to do with optimizing dual-class features and more with conforming to prevailing norms, and lawyers seem to play the very important role of conservators and transmitters of these norms.

The third goal is to try to reconcile this picture with the standard theories of corporate contracting. The "classic contractarian theory" of the corporation argues that pre-IPO owners internalize the effects of charter provisions on firm value, and therefore corporate charters will tend to include value-maximizing provisions.[17] Under this view, the level of voting inequality should be a function of company characteristics and founder characteristics. It is plausible, however, that company and founder characteristics vary significantly across firms; therefore, the low variation in voting inequality among real-world dual-class companies is puzzling. It is possible, in theory, that the 9%–10% control lock and an unlimited duration (before 2011) or a mix of lifelong and 7–to–10-year duration (from 2011) are optimal for most dual-class companies. However, the fact that companies with different characteristics do not choose tailor-made solutions more frequently is suspicious.

More recent work has provided richer and more nuanced versions of the contractarian theory. I call them "modern contractarian theories."[18] On the topic of standardization and customization in corporate governance, the main insights of the modern contractarian theories concern the role of learning and network externalities and of agency problems. But do these mechanisms persuasively explain dual-class norms? I will argue that, with respect to dual-class structures, these models are much less compelling than in other cases.

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15. Michael Klausner, *The Contractarian Theory of Corporate Law: A Generation Later*, 31 J. CORP. L. 779, 782 (2006).

16. *Id.* at 790–91; *see also* Jill E. Fisch, *Stealth Governance: Shareholder Agreements and Private Ordering*, 99 WASH. U. L. REV. 913, 919 (2021) (using "dual or multiclass voting structures" as an example of private ordering "tailoring a corporation's structure and governance mechanism to meet firm-specific needs").

17. *See* sources cited *infra* note 82.

18. I thank Marcel Kahan for this label.

The learning externalities hypothesis relies on the assumption that companies that adopt standard terms save on drafting and other advisory costs and reduce legal uncertainty. But customizing dual-class structures does not seem to require significant drafting efforts or to add legal uncertainty. Dual-class companies can very easily alter the degree or duration of voting inequality with very little cost and virtually no risk of ambiguity or legal uncertainty, yet, in most cases, they choose not to do so.

The agency problem hypothesis relies on the assumptions that the lawyers' work is assessed based on good or bad outcomes rather than on its intrinsic quality; that a bad outcome has a disproportionately larger cost for the lawyer's reputation when the lawyer chooses a customized contract term rather than a standard contract term; and, therefore, lawyers choose standard terms even when they are not in the best interest of their client. In the case of dual-class structures, however, the "standards" concern substantive features—such as how large the voting power asymmetry will be and for how long this asymmetry can persist—rather than mere technical legal terms. Agency theories of contractual standardization typically deal with technical legal language, which is not easily understood and assessed by the clients. Here, by contrast, founders, VCs, company directors, and institutional investors can accurately observe the level of voting inequality chosen in the IPO charter and act accordingly.

Given the limits of classic and modern contractarian theories in explaining the real-world dynamics of dual-class contracting, we need a richer story. At the end of the Article, I will sketch a conjecture that draws from different literature on social norms (by sociologists, economists, and legal scholars). Briefly stated the conjecture is as follows. In dual-class contracting, "market norms" play an important role alongside individualized contracting. Indeed, the market practice in dual-class IPOs possesses certain essential characteristics of social norms: compression (i.e., low variation), stickiness (i.e., persistence over time), and the so-called punctuated equilibrium (i.e., long period of stasis followed by rapid change). Furthermore, the key insiders surveyed and interviewed for this Article seem to treat dual-class market practice as norms—standards that one *ought* to comply with even if the underlying price-maximization rationale is unclear. Finally, the emergence of these norms resembles random mutation rather than rational design, with some important innovations appearing to have been spurred by the deliberate actions of individuals and organizations, akin to the role of "norm entrepreneurs" in changing social norms.

If the market norms conjecture is, as I believe, an accurate explanation of an important part of dual-class contracting, the policy debate on dual-class companies should focus on understanding the process shaping these norms, starting from the recognition that some aspects of this process might be different from what classic and modern contractarianism predict. To begin with, contrary to the classic contractarian theory and the learning externalities theory, we should not dismiss the possibility that the prevailing dual-class norms may be bad for investors. Furthermore, contrary to the agency theory, the lawyers are not to be blamed for this phenomenon: market norms exist because the dual-class IPO process is embedded in business and social relationships, particularly those among VCs, founders, early-stage investors, incubators, tech experts, and advisors within the start-up ecosystem. Finally, we should envisage the role of the regulator in this space neither as a passive spectator (as standard contractarian accounts suggest) nor as an active designer of optimal voting structures (as anti-contractarian accounts suggest), but rather as a facilitator of tailor-made contracting and norm innovation.

The Article contributes to the literature on dual-class companies and corporate contractarianism by providing a systematic analysis of voting inequality levels across nearly three decades, which documents the persistence and evolution of recurring patterns in dual-class structures. This analysis challenges the view that dual-class charters are a textbook example of "deliberate contracting" and suggests a rethinking of this standard narrative. Additionally, it highlights the limits of learning externalities and agency problems in explaining certain peculiarities of dual-class contracting and outlines an alternative conjecture with potential implications for future research.

The rest of the Article proceeds in four Parts. Part I identifies the problem of the "continuous choice" of voting inequality and illustrates the methodology employed to study it. Part II maps the dual-class landscape by presenting evidence on the degree and duration of voting inequality across the 293 dual-class companies in the sample and across the 27 years of the sample period. Part III reconstructs the "contracting process" in dual-class IPOs as experienced by senior lawyers involved in the process. Part IV situates the findings within the frameworks of classic and modern contractarian theories, discusses the limits of these theories, and outlines an alternative conjecture drawing on different literature on social norms. The last part concludes.

I. PROBLEM, DATA, AND METHODOLOGY

A. The "Categorical" Problem of Dual-Class Structures

Dual-class structures are one of the most controversial topics in corporate governance. Critics believe that they are "inherently undemocratic,"[19] and aimed at perpetuating "corporate royalty."[20] Supporters, in contrast, argue that giving insiders superior voting power protects companies from market short-termism and encourages managers to focus on creating long-term value.[21]

19. Kara M. Stein, Comm'r, SEC, Remarks at Stanford University: Mutualism: Reimagining the Role of Shareholders in Modern Corporate Governance (Feb. 13, 2018), https://www.sec.gov/news/speech/speech-stein-021318 [https://perma.cc/SHZ4-6MNH].

20. Robert J. Jackson, Jr., Comm'r, SEC, Address at the University of California Berkeley School of Law: Perpetual Dual-Class Stock: The Case Against Corporate Royalty (Feb. 15, 2018), https://www.sec.gov/news/speech/perpetual-dual-class-stock-case-against-corporate-royalty [https://perma.cc/958P-3285].

21. *See, e.g.*, Google, Inc., IPO Prospectus (Form 424B4) 29 (Aug. 18, 2004) ("This [dual-class] structure will also make it easier for our management team to follow the long term, innovative approach emphasized earlier."); Opening Pretrial Brief of Defendants Larry Page and Sergey Brin at 2, In re Google, Inc. Class C Shareholder Litigation, 2013 WL 2728581 (Del. Ch. June 10, 2013) (arguing that Google's dual-class capital structure "had the effect of concentrating voting power in Google's longest-term stockholders, and particularly the Founders" and that the company "[g]uided by its Founders' vision . . . made big long-term bets on revolutionary products and services, and pursued its ambitious mission"); Facebook, Inc., Preliminary Proxy Statement (Form PRE 14-A) 55 (May 2016) (arguing that a, later abandoned, proposal of reclassification to create a class of nonvoting stock would have "allow[ed] the company to maintain focus on Mr. Zuckerberg's long-term vision for the company").

The controversy over dual-class companies is not novel.[22] However, whereas in the past dual-class structures were used quite rarely,[23] in the last two decades they have become a very familiar way to allocate voting rights in the technology sector, one of the fastest-growing sectors of the U.S. economy.[24]

In 2004, Google (now Alphabet) made the decision, then unusual for tech companies, to adopt a dual-class structure.[25] Since then, many large and visible tech IPOs have followed Google's example, including Facebook (now Meta Platforms), LinkedIn, First Data, Snap, Lyft, Airbnb, DoorDash, Zoom, and many others.[26] Today, there is a widespread perception that dual-class IPOs have become the norm in Silicon Valley.[27]

As happened in the past, commentators disagree on the advantages and disadvantages of dual-class structures. On the one hand, tech founders and their advisers argue that dual-class structures allow entrepreneurs to focus on innovation and long-term value creation, thanks to the insulation from the pernicious short-term pressure of the stock market.[28] On the other hand, many commentators believe that dual-class structures violate the fundamental principle of "one share, one vote," reduce managerial accountability, and undermine the trust of investors in the market.[29]

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22. For a brief overview of past controversies on dual-class structures, see generally Joel Seligman, *Equal Protection in Shareholder Voting Rights: The One Common Share, One Vote Controversy*, 54 GEO. WASH. L. REV. 687 (1985). *See also* Jeffrey N. Gordon, *Ties That Bond: Dual Class Common Stock and the Problem of Shareholder Choice*, 76 CALIF. L. REV. 1, 4–5 (1988) (documenting the wave of dual-class recapitalizations in the 1980s); Stephen M. Bainbridge, *The Short Life and Resurrection of SEC Rule 19C-4*, 69 WASH. U. L.Q. 565 (1991).

23. Robert Daines & Michael Klausner, *Do IPO Charters Maximize Firm Value? Antitakeover Protection in IPOs*, 17 J.L., ECON., & ORG. 83, 96 (2001) (finding that only 6.4 percent of companies that went public between January 1, 1994, and July 1, 1997, chose a dual-class structure). For decades, dual-class structures were most often associated with media companies—including The New York Times Co., The Washington Post Co., and Dow Jones & Co. (publisher of The Wall Street Journal). *See* Johnnie L. Roberts & Linda Sandler, *Washington Post Seeks to Strengthen Graham Family's Control of Company*, WALL ST. J., Apr. 14, 1988, at 36 (reporting that "many media concerns . . . [use dual-class structures] to ensure continued control by founding family members"). Corporate leaders of dual-class media companies argued that, by insulating the insiders' control of the company from shareholder interference, dual-class stock ensured editorial independence against the whims of the stock market. *See, e.g.*, Johnnie L. Roberts, *Media General Case Likely to Spotlight Any Cracks in the Dual Stock Defense*, WALL ST. J., Apr. 1, 1988, at 16 (quoting Ray Shaw, President of Dow Jones, arguing that dual-class structures are aimed to "insure journalistic independence").

24. Andrew DePietro, *U.S. Industries with the Biggest Growth in GDP from 2000 to 2020*, FORBES (Aug. 23, 2021), https://www.forbes.com/sites/andrewdepietro/2021/08/23/us-industries-with-the-biggest-growth-in-gdp-from-2000-to-2020 (on file with the *Journal of Corporation Law*).

25. Google, IPO Prospectus, *supra* note 21, at 30 (reporting the founders' observation that "[w]hile [a dual-class] structure is unusual for technology companies, similar structures are common in the media business and has had a profound importance there").

26. *See, e.g.*, Eliot Brown, *IPO Demands Tilts Power to Tech Founders*, WALL. ST. J., Dec. 23, 2020, at B1.

27. *Id.* (reporting that "[dual-class] share structures . . . [once] reserved for a tiny number of startups . . . ha[ve] effectively become the norm" and presenting data from Professor Jay Ritter showing that more than 40 percent of tech IPOs in 2020 had a dual-class structure).

28. *See* sources cited *supra* note 21.

29. *See, e.g.*, Letter from Elizabeth Warren, U.S. Senator, to John Carey, Vice President, NYSE Regulation, Inc., and Edward Knight, Exec. Vice President & Gen. Couns., NASDAQ OMX (June 5, 2013), https://www.warren.senate.gov/files/documents/Senator%20Warren%20letter%20to%20NYSE,%20Nasdaq%20-%206-5-2013.pdf [https://perma.cc/H794-MAZE] ("If a company goes to the public markets to raise money, long-term

Legal and finance scholars are similarly divided on the virtues and vices of dual-class structures. As some studies have made clear, by creating a wedge between insiders' cash-flow rights and control rights, dual-class structures increase managerial agency costs.[30] Consistent with this hypothesis, empirical studies have found that the valuation of dual-class companies is lower relative to the valuation of comparable single-class companies.[31] More recently, some scholars have hypothesized,[32] and others have documented empirically,[33] that the advantage of dual-class companies relative to single-class companies tends to dissipate in the long run.

Other scholars, in contrast, have proposed arguments as to why dual-class structures might be good for shareholders. One traditional argument is that takeover defenses (including dual-class structures) give managers more bargaining power vis-à-vis buyers in case of a sale of the company, and therefore managers, using such enhanced bargaining power, can obtain a higher premium for shareholders.[34]

Another argument is that dual-class structures allow CEO-controllers to diversify their investment portfolio without losing control of the company, thus making them less risk-averse when making business decisions.[35] According to this view, a CEO-controller with

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ordinary common stock investors – a category that includes directly or indirectly millions of retirees and workers – should be entitled to certain basic rights. One of the most basic of those rights is one-share-one-vote."). Letter from the Council of Institutional Investors to Evan Thomas Spiegel, CEO, Snap, Inc., Robert Murphy, Chief Tech. Officer, Snap, Inc., & Michael Lynton, Chairman-Designate, Snap, Inc., on the Proposed Multi-Class Structure for Post-IPO Snap, Inc. (Feb. 3, 2017), https://www.cii.org/files/issues_and_advocacy/correspondence/2017/02_03_17_SNAP_IPO.pdf [https://perma.cc/AQN6-S73W] ("[W]e believe a decision by Snap to go public with the reported dual-class structure will undermine the quality and confidence of public shareholders in the market").

30. For a discussion of how the misalignment between cash-flow rights and voting rights increase agency costs, see generally Bebchuk & Kastiel, *supra* note 11 (highlighting the "perils of small-minority controllers" which include higher governance costs and risks). *See also* Lucian A. Bebchuk, Reinier Kraakman & George G. Triantis, *Stock Pyramids, Cross-Ownership, and Dual Class Equity: The Mechanisms and Agency Costs of Separating Control from Cash-Flow Rights*, *in* CONCENTRATED CORPORATE OWNERSHIP 296 (Randall K. Morck ed., 2000) (demonstrating that controlling shareholders with minority cash-flow rights create agency costs "an order of magnitude" higher than controlling shareholders that have a majority of cash-flow rights).

31. *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, 1054 (2010) (finding that insider voting rights are negatively associated with firm value); Ronald W. Masulis, Cong Wang & Fei Xie, *Agency Problems at Dual-Class Companies*, 64 J. FIN. 1697, 1698 (2009) ("[W]e find four distinctive sets of evidence supporting the hypothesis that managers with greater control rights in excess of cash flow rights are more likely to pursue private benefits at the expense of outside shareholders."); Scott B. Smart, Ramabhadran S. Thirumalai, & Chad J. Zutter, *What's in a Vote? The Short- and Long-Run Impact of Dual-Class Equity on IPO Firm Values*, 45 J. ACCT. & ECON. 94, 96 (2008) (finding that dual-class firms are valued by the market lower than non-dual class firms).

32. Bebchuk & Kastiel, *supra* note 11, at 612.

33. Martijn Cremers, Beni Lauterbach & Anete Pajuste, *The Life-Cycle of Dual Class Firm Valuation*, 13 REV. CORP. FIN. STUD. 459, 460 (2024). These authors also find that dual-class companies have an initial valuation premium, but "this initial valuation premium of dual-class firms dissipates in the years after the IPO, and on average dual-class firms start trading at a discount relative to comparable single-class firms about 7 to 9 years after the IPO." *Id.* at 461.

34. *See, e.g.*, René M. Stulz, *Managerial Control of Voting Rights: Financing Policies and the Market for Corporate Control*, 20 J. FIN. ECON. 25, 26 (1988) (arguing that the expansion of managerial control on voting rights can lead to better outcomes for shareholders and the company alike).

35. *See generally* Scott W. Bauguess, Myron B. Slovin & Marie E. Sushka, *Large Shareholder Diversification, Corporate Risk Taking, and the Benefits of Changing to Differential Voting Rights*, 36 J. BANKING & FIN. 1244 (2012).

a very large fraction of her wealth invested in the company would take much fewer risks than optimal.

A further argument is that entrepreneurs may have peculiar perspectives that are difficult to convey to shareholders, either because they are based on private information that cannot be disclosed to the public or because they are part of an idiosyncratic vision with which uninformed or short-term-oriented shareholders might disagree. Therefore, dual-class structures protect the entrepreneur's vision from such disruptive market pressure and allow the company to innovate and produce long-term value for shareholders.[36]

Theoretical and empirical studies on the effects of dual-class structures on shareholder value leave us with limited evidence[37] and conflicting conclusions. The debate remains unresolved.[38]

In this Article, I will take an agnostic view on the costs and benefits of dual-class structures. Dual-class structures may be bad for shareholders in some companies but good in other companies. Furthermore, some of these positive and negative effects may coexist in the same company, but to different degrees. Therefore, dual-class structures may produce *both* increased agency costs *and* increased shareholder value, but for some companies the net effect will be positive and for other companies, the net effect will be negative.[39] Hence, the voting structure that is good for one company is not necessarily good for another company.[40] Importantly, even a value-decreasing voting structure does not necessarily result in the exploitation of shareholders, as long as shareholders can price the effect of the structure and therefore pay a correspondingly lower price for the company's stock.

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36. *See* Zohar Goshen & Assaf Hamdani, *Corporate Control and Idiosyncratic Vision*, 125 YALE L.J. 560, 579–81, 590–91 (2016) (arguing that asymmetric information between public shareholders and insiders, as well as differences of opinion, can disrupt the entrepreneur's idiosyncratic vision, whereas insulating mechanisms such as dual-class structures can correct this effect). A related argument has been subsequently proposed by Dorothy S. Lund, *Nonvoting Shares and Efficient Corporate Governance*, 71 STAN. L. REV. 687 (2019) (arguing that dual-class structures can be used to separate informed and non-informed shareholders in an efficient way).

37. For a discussion of the limits of dual-class empirical studies, see Fisch & Solomon, *supra* note 9, at 1073–75.

38. *Id.* at 1061.

39. For example, a highly innovative company is likely to be more vulnerable to information asymmetry and short-termism and, in this company, the value-increasing effects of a dual-class structure might outweigh its value-decreasing effects. *See, e.g.*, Bronwyn H. Hall & Josh Lerner, *The Financing of R&D and Innovation*, *in* HANDBOOK OF THE ECONOMICS OF INNOVATION 614 (Bronwyn H. Hall & Nathan Rosenberg eds., 2010) ("In the innovation setting, the asymmetric information problem refers to the fact that an inventor frequently has better information about the likelihood of success and the nature of the contemplated innovation project than potential investors."). By contrast, in a company with significant amounts of free cash flow, there are more opportunities for insiders to waste resources on pet projects and other private goals and therefore the value-decreasing effects of a dual-class structure might outweigh its value-increasing effects. *See, e.g.*, Michael C. Jensen, *Agency Costs of Free Cash Flow, Corporate Finance, and Takeovers*, 76 AM. ECON. REV. 323, 326–27 (1986) (describing high agency costs of free cash flow experienced by the oil industry in the late 1970s).

40. For a defense of this view, see Goshen & Hamdani, *supra* note 36, at 586–87 ("[A]ny contract between entrepreneurs and investors . . . represents a different balance between idiosyncratic vision and agency costs."). *See also* Zohar Goshen & Assaf Hamdani, *Corporate Control, Dual Class, and the Limits of Judicial Review*, 120 COLUM. L. REV. 941, 962 (2020) ("Through the negotiation [between insiders and investors at the IPO], the parties are able to reach an acceptable balance between idiosyncratic vision and agency costs that fits their preferences and the nature of the business activity.").

B. The "Continuous" Problem of Voting Inequality

1. The Voting Inequality Spectrum

As discussed in the previous Part, the choice between dual-class and single-class structures has been the subject of academic and policy debates for many years. But voting inequality is a spectrum, not a binary choice.[41] Corporate charters can choose different levels of voting inequality, and in some cases the difference in voting inequality between a dual-class company and a single-class company can be smaller than the difference between two dual-class companies.

Consider the following example. Amazon went public as a single-class company. If its founder and CEO Jeff Bezos wants to exercise a majority of votes, he must own a majority of shares. By contrast, Pinterest and Cognizant went public as dual-class companies. Based on their IPO voting structures, high-vote shareholders in Pinterest and Cognizant can have a majority of votes with less than 50% of shares. At Pinterest, however, owners of Class B shares can reduce their equity holding down to 4.8% and still have a majority of votes; at Cognizant, founder Kumar Mahadeva can potentially reduce his equity stake down to 35% and keep a majority of the votes. If he goes below 35% of common stock, he loses the voting majority.

Whatever effects voting inequality has on public companies, good or bad, it is clear that Pinterest has greater voting inequality than Cognizant. In fact, if we measure voting inequality by this metric—the smallest percentage of common stock needed to keep a majority of votes—Cognizant's dual-class structure is closer to Amazon's single-class structure than to Pinterest's dual-class structure. Therefore, the division of voting structures into single class and dual class gives us a very partial picture. We should pay attention to the different levels of voting inequality within dual-class structures, not just to a binary division between single-class and dual-class structures.

The problem of customization and innovation within dual-class structures is important in and of itself because, as explained above, voting inequality is, from a logical, legal, and economic standpoint, a continuous phenomenon, not a categorical one. However, this problem is also relevant for its implications on the traditional "categorical" debate. As we will see in Part IV, the "classical contractarian theory" of the corporations argues that pre-IPO owners internalize the effects of charter provisions on firm value, and therefore corporate charters will tend to include value maximizing provisions. Critics, by contrast, argue that low variation across corporate charters warrants some rethinking of the contractarian theory.[42] Dual-class structures, however, have been usually considered, even by critics of contractarianism, as an example of "deliberate contracting."[43] But little attention has been paid to how deliberate this contracting process exactly is: How much variation and

41. This point has already been made, quite emphatically, by Professors Gladriel Shobe and Jarrod Shobe. Gladriel Shobe & Jarrod Shobe, *The Dual-Class Spectrum*, 39 YALE J. REG. 1343 (2022). In this Article, however, I use the concept of "spectrum" to study a different phenomenon. Professors Shobe and Shobe find that single-class companies give insiders control rights by contract, thus blurring the line between single-class and dual-class structures. Here, I focus on the variation of voting inequality within actual dual-class companies. *See also infra* note 44.

42. *See* Klausner, *supra* note 15, at 789 (discussing a lack of deliberate contracting in drafted corporate charters).

43. *Id.* at 790–91. *See also* Fisch, *supra* note 16, at 933.

customization are there within dual-class structures? What is the contribution of the various market actors to the final shape of these structures? Do real-world dual-class arrangements adapt to different characteristics of companies and controllers? How do dual-class structures evolve and what might explain the patterns of change or persistence?

2. Degree of Voting Inequality

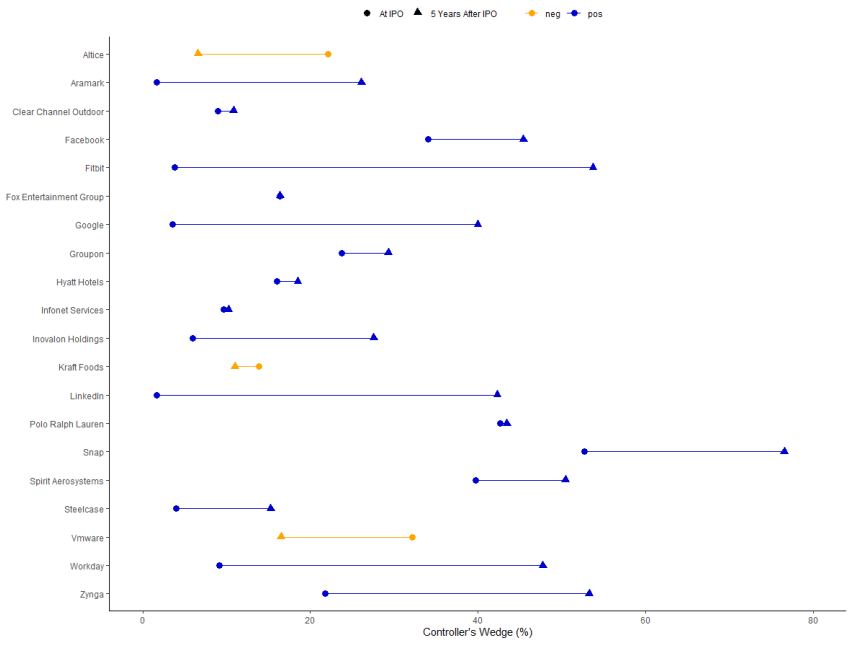
To take account of the differences among dual-class structures, I will consider two dimensions of voting inequality. The first is the *degree* of voting inequality. A dual-class structure that enables the founder to control the company with only 4.8% of shares (such as the one chosen by Pinterest) has a greater degree of voting inequality than a dual-class structure that enables the founder to control the company with at least 35% of shares (such as the one adopted by Cognizant).

In the corporate governance literature, this aspect is often measured by the difference between cash-flow rights and voting rights of the controller (the so-called *wedge*) at a given point in time, usually at the time of the IPO. However, the controller's wedge may and does vary over time, and companies with different wedges at the IPO may end up having very similar wedges after a few years, whereas companies with similar wedges at the IPO may end up having very different wedges after a few years. To illustrate this point, I will draw a subsample of dual-class structures from the dataset of dual-class IPOs that I will analyze in detail in Part II.

Figure 1 Figure 1. Controller Wedge at the IPO and 5 Years After the IPOreports, for the twenty largest dual-class IPOs in my dataset,[44] the controller's wedge at the IPO and five years after the IPO. As the Figure shows, with only a few exceptions, the controller's wedge five years after the IPO is significantly different from what it was at the IPO, and in most cases it is much larger. At Facebook, for example, Zuckerberg had 24% of shares and 58% of voting rights at the IPO (34% wedge) and 14% of shares and 60% of voting rights five years after the IPO (45% wedge). At Google, Brin and Page had 28% of shares and 32% of voting rights at the IPO (4% wedge) and 18% of shares and 58% of voting rights five years after the IPO (40% wedge). Furthermore, companies with similar wedges at the IPO had very different wedges five years after the IPO, and vice versa. For example, at Aramark and Fitbit, the controller wedges at the IPO were quite close (2% and 4%, respectively), but they were very different five years later (26% and 54%, respectively). By contrast, at Zynga and DreamWorks, the wedges at the IPO were very different (22% and 45%, respectively) whereas five years after the IPO they were very close (53% and 55%, respectively).

44. I excluded companies that, after five years from the IPO, had been acquired or had become single-class companies.

Figure 1. Controller Wedge at the IPO and 5 Years After the IPO



The Figure reports the size of the "controller's wedge" (i.e., the difference between the controller's voting rights and common shares as a percentage of the total) at the time of the IPO and five years after the IPO for the twenty largest dual-class companies in my dataset (at the time of the IPO), excluding companies that did not exist or had become single-class companies five years after the IPO.

The controller's wedge increases, for example, when other dual-class controllers sell their shares, and the sale triggers an automatic conversion provision in the charter, or when the company issues more nonvoting shares authorized in the charter. These mechanisms (automatic conversions, authorized nonvoting shares) are present in the charter at the time of the IPO but are actioned only later.

Hence, measuring the controller's wedge at the IPO (or at any other specific point in time) reveals the degree of voting inequality only at that specific time, but it tells us nothing about the potential degree of inequality that public investors accepted with the "corporate contract." By accepting a certain dual-class structure, public shareholders accept that voting inequality can increase over time, including by unilateral decision of the controller, and therefore the instantaneous measure of such inequality at a given point in time does not capture the substance of the arrangement agreed upon by insiders and public investors.

Therefore, to measure the degree of voting inequality in dual-class structures I will measure the *maximum* degree of voting inequality that investors have accepted in the charter. Building on a methodology introduced by Professors Bebchuk and Kastiel,[45] I calculate, for each dual-class company in my sample, the minimum percentage of shares with

45. *See* Bebchuk & Kastiel, *supra* note 12, at 1493–95 (describing the application of the methodology to measure the degree of inequality to dual-class stock structure).

which high-vote shareholders could keep a majority of votes if they unilaterally used all the potential tools built in the IPO charter to their fullest extent. I will refer to this metric as the "control lock."

3. Duration of Voting Inequality

The second dimension of voting inequality is its *duration* over time. At Google, for example, the dual-class structure can potentially last for the entire life of the founders, whereas at FitBit the dual-class structure will convert into a single-class structure ten years after the IPO. Other things being equal, a dual-class structure that lasts for ten years will have different effects, both on shareholder value and private benefits, than a dual-class structure that lasts for a lifetime. Whatever the costs and benefits of a dual-class arrangement, they accrue year after year, and therefore the present value of these effects, when estimated at the time of the IPO, heavily depends on how long these structures will last.

As I will show in Part II, different contractual mechanisms affect the duration of voting inequality over time. Longer-lasting structures create larger private benefits for the founder and may create larger benefits or larger costs for public investors, depending on the specific circumstances.

To be sure, degree and duration of voting inequality, as measured here, are the most extreme outcomes allowed by the charter. In practice, however, companies with different contractual degrees and durations of voting inequality may end up having the same actual degrees and durations, and vice versa. However, since the actual degree and duration are not observable ex-ante, at the time of the IPO, the fact that the charter allows greater or lower voting inequality should affect the value of the shares for outside investors and insiders alike.

C. Data and Methodology

1. The Charter Dataset

To study the problem of dual-class customization and innovation, I constructed a novel dataset of dual-class charters.[46] The dataset consists of all dual-class IPOs by U.S. nonfinancial companies completed between 1996 and 2022. To build the dataset, I started from the database of multi-class IPOs compiled by Professor Jay Ritter,[47] and then I excluded non-U.S. companies, companies in the financial, insurance, real estate, and utility sectors (consistent with the finance literature on dual-class companies), and legal entities other than corporations. For each of the remaining companies, I manually reviewed the

46. Professors Gladriel and Jarrod Shobe have recently documented the existence of shareholder agreements in single-class companies that give minority shareholders control over the board of directors, thus making these companies functionally equivalent to dual-class companies. Shobe & Shobe, *supra* note 41. They report that 252 single-class IPOs out of their sample of 1,870 single-class IPOs have agreements in place that give some insiders the right to nominate a majority of the board. Professors Shobe and Shobe do not analyze whether these agreements introduce, from outside the charter, higher variation in the degree and duration of voting inequality. Therefore, their important findings warrant further analysis.

47. Jay Ritter, *A List of IPOs from 1975-2020 With Multiple Share Classes Outstanding*, UNIV. OF FLA. WARRINGTON COLL. BUS., https://site.warrington.ufl.edu/ritter/ipo-data/ [https://web.archive.org/web/20210330210649/https://site.warrington.ufl.edu/ritter/ipo-data/]. The list used for constructing the sample was downloaded in October 2021.

final IPO prospectus, filed pursuant to Rule 424 at the completion of the IPO, and the proposed charter as enclosed with the company's registration statement (Form S-1). All these documents were collected from the Securities and Exchange Commission (SEC)'s Electronic Data Gathering, Analysis, and Retrieval (EDGAR) system. Based on this review, I excluded companies for which the prospectus or the charter was not available on EDGAR, as well as the companies that were mistakenly coded as dual-class in Ritter's database but were in fact single-class companies.

Finally, I excluded all the companies that adopted a multi-class structure for other purposes than enhancing insiders' control. The focus of this Article—and of the scholarly and policy debate on dual-class companies—is on legal structures aimed at preserving the insiders' control (or influence) on the company. However, multi-class structures are also used for other purposes, including tax and regulatory reasons, sometimes only for a short transitory period.

To this end, I excluded: (a) multi-class structures with equal voting rights; (b) multi-class structures in which low-vote shares had privileged dividend rights; (c) so-called "Up-C" structures in which the unequal voting rights at the level of the publicly traded issuer are part of a more complex, multi-company structure designed for tax reasons;[48] (d) multi-class structures in which public investors receive high-vote shares (often because some pre-IPO shareholders may not exercise voting rights, or more than a certain number of voting rights, for regulatory reasons); (e) multi-class structures in which high-vote stock has superior voting rights only on specific matters (typically, a charter amendment) but not on the election of directors; (f) dual-class structures mentioning the possibility of a subsequent spin-off or split-off, if the spin-off or split-off occurred within three years of the IPO.[49]

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48. In an "Up-C" structure, a holding company goes public with an unequal voting structure, but the voting inequality often disappears when one considers the combination of cash flow rights and voting rights in the holding company and in the subsidiary partnership or limited liability company. *See, e.g.*, Joshua Ford Bonnie & Andrew B. Purcell, *The Up-C Structure Employing the Umbrella Partnership–C-Corporation Structure in an IPO*, SIMPSON THATCHER (Dec. 17, 2019), https://www.stblaw.com/docs/default-source/related-link-pdfs/up-c-slides.pdf?sfvrsn=6 [https://perma.cc/67DC-WCAP]. In some Up-C IPOs examined for the construction of the dataset, there is also some voting asymmetry even after considering the combined equity interest in the holding and the operating subsidiary. However, given the peculiarity of these structures, I decided to exclude them from the final dataset. In any event, they would constitute a very small fraction of the total and they do not show major differences compared to the most common dual-class structure found among regular IPOs.

49. Some charters mention the possibility of a spin-off or split-off, that is, the distribution of the company stock owned by its parent corporation to the shareholders of the latter. The parent company (controller) chooses a dual-class structure, but in many of these cases, it plans to relinquish control shortly after the IPO, upon completion of the aforesaid spin-off. In these cases, the dual-class structure does not seem aimed at strengthening the control of the parent company on strategic and managerial issues, but only to facilitate the execution of the spin-off or split-off.

The reason for this type of structure seems to be a statutory requirement that the "distributing" company must own at least 80% of the total voting power of the controlled company, for the spin-off to be tax-free. *See* 26 U.S.C. §§ 355, 368 (requiring, for a tax-free spin-off, that the parent company distributes to its stockholders "an amount of stock in the controlled corporation constituting control . . . ." and defining control as "the ownership of stock possessing at least 80 percent of the total combined voting power of all classes of stock entitled to vote and at least 80 percent of the total number of shares of all other classes of stock of the corporation"). Therefore, high-vote shares are issued to the parent company to artificially keep the voting power of the latter above the threshold of 80% until the completion of the spin-off. This goal is occasionally acknowledged by the issuer. In other instances, by contrast, a future spin-off is mentioned only as one of the potential scenarios that the controller

The final dataset, so constructed, includes 293 dual-class IPOs. For each charter and prospectus, I manually reviewed and coded the provisions affecting voting inequality and information regarding certain company characteristics, pre-IPO shareholders, CEO, and legal advisers. I also collected additional information from CRISP-Compustat, SDC New Issues, and news sources. Table 1 presents some descriptive statistics of the companies included in the sample.

envisages for the future. In these cases, the dual-class structure might be motivated by the intention to insulate the controller, not to facilitate the spin-off.

In our case, however, we have the benefit of hindsight. We know which parent companies have completed a spin-off and canceled the dual-class structure shortly after the IPO and which did not. Thus, I exclude from the analysis those charters that explicitly mention the tax-free distribution of the parent company's holding to the extent that this distribution occurred within three years of the IPO. Although highly imperfect, this criterion seems better than a qualitative inquiry into the undisclosed intentions of the corporate planners.

Table 1. Dual Class IPOs 1996-2022

	% of Sample
Number of IPOs	
- 1996-2004	41.0%
- 2005-2013	14.7%
- 2014-2022	44.4%
State of incorporation	
- Delaware	86.0%
- Other states	14.0%
Industries	
- Computer and data services	40.6%
- Communications	11.3%
- Retail	8.2%
- Entertainment	5.1%
- Pharmaceutical products	3.1%
- Personal services	2.7%
- Transportation	2.4%
- Restaurants & hotels	2.4%
- Apparel	2.0%
- Wholesale	1.7%
- Industries with fewer than 5 dual-class IPOs	20.5%
Tech companies*	
- 1996-2004	17.2%
- 2005-2013	12.9%
- 2014-2022	69.8%
Market cap at IPO (2020 USD)	
- > $10 billion	11.3%
- $2 - $10 billion	29.0%
- $250 million - $10 billion	46.4%
- < $250 million	13.0%
Ownership structure	
- Founder control**	60.8%
- Sub of controlled company	10.2%
- Family control***	8.9%
- PE control	7.8%
- Sub of non-controlled company	6.1%
- Other	6.1%

The Table reports some characteristics of the dual-class companies included in the dataset built for this Article.

*Tech companies are companies with the following 3-digit SIC codes as reported in their IPO prospectus: 357, 366, 367, 382, 737, 873.

**Founder control means companies in which, at the IPO or following the full divestment of VC investors, (a) the founder (or co-founder) is CEO or executive director, and nobody has more than 30% of the votes at the IPO or (b) the founders have more than 30% of the votes at the IPO.

***Family control means companies in which at the IPO the CEO or Chairman is a member of the founding family and/or the founding family has more than 30% of the votes.

2. Survey and Interviews

To supplement the quantitative data discussed above and study the real-world dynamics of dual-class contracting, I conducted a survey of elite law firm partners and senior lawyers with expertise on dual-class IPOs. The survey was conducted between September 6 and October 15, 2023, and consisted of multiple-choice questions, open questions, and matrix questions with multiple sub-questions. In the aggregate, survey recipients were asked to answer 137 questions.[50]

The survey was sent to law firm partners, of counsel, senior counsel (and similar senior titles) in the capital markets group of the nine law firms most represented in my charter dataset as counsel to dual-class issuers. The survey was specifically directed at the relatively small number of senior lawyers with expertise on dual-class IPOs and therefore screened out those without this expertise.

Of the 502 lawyers initially contacted, 110 responded, and 46 of them said that they had "some" or "significant" expertise on dual-class IPOs. The final survey dataset includes the responses of the 37 respondents who completed at least 50% of the survey: 28 respondents answered all 137 questions, 6 respondents answered between 60% and 94% of the questions, and 3 respondents answered between 51% and 57% of the questions. Table 2 presents some descriptive statistics of the final respondents.

The final respondents (the "survey respondents" or just the "respondents") are partners, counsel, or senior counsel at eight different law firms that have worked as issuer law firms in more than two-thirds of the dual-class IPOs in my dataset between 2013 and 2022. The respondents have between 8 and 50 years of experience as IPO lawyers, with an average (and median) of 24 years of experience. The average (median) respondent worked on 13 (7) dual-class IPOs, of which 8 (5) IPOs as counsel to the issuer and 9 (5) IPOs as counsel to the underwriters. Compared to my sample, the dual-class IPOs on which the respondents have worked on are larger (unsurprisingly, as the respondents are among the top IPO lawyers in the country). Given the significant variation in terms of expertise, all responses will be weighted by the total number of dual-class IPOs on which the respondent has worked. Hence, when I say that "most" or "the vast majority of" or a certain percentage of the survey respondents gave a certain answer, I will refer to an experience-weighted percentage of respondents.

Finally, to collect more qualitative evidence regarding the process through which market actors make certain choices in dual-class charters, I conducted follow-up interviews with nine survey respondents from six different law firms. Each interview was conducted on Zoom and lasted approximately 30-40 minutes. In one case, the interview was followed by some follow-up questions and answers by email.

All interview respondents have expertise on dual-class IPOs. However, to give more context to their comments, I will refer to interview respondents with above-median experience as "experienced," and those with experience above the top quartile as "very experienced." All the participants in the survey and the interviews will remain anonymous.

50. The survey and all the responses are on file with the *Journal of Corporation Law*.

Table 2. Survey of Senior IPO Lawyers

Panel A: Survey	
Survey requests	502
Initial responses	110
- "Some" or "significant" experience with dual-class IPOs	46
- "Never worked on dual-class IPOs"	64
Survey completion	
- 100% completed	22
- 71%-99% completed	8
- 51%-70% completed	7
- Less than 50% completed	9
Panel B: Final respondents	
Years of experience as IPO lawyer	
- Min-max	8-50
- Average	23.6
- Median	24
Experience as issuer counsel on dual-class IPOs	
- # of respondents	36
- # of dual-class IPOs (min-max)	1-40
- # of dual-class IPOs (average)	7.9
- # of dual-class IPOs (median)	5
Experience as underwriter counsel on dual-class IPOs	
- # of respondents	26
- # of dual-class IPOs (min-max)	1-50
- # of dual-class IPOs (average)	8.6
- # of dual-class IPOs (median)	5
Market cap of dual-class issuers	
- > $10 billion	22.1%
- $2 - $10 billion	44.3%
- $250 million - $10 billion	29.6%
- < $250 million	3.9%

The Table reports some characteristics of the survey of senior IPO lawyers conducted between September 6 and October 15, 2023, and of the final respondents included in the analysis.

II. VOTING INEQUALITY IN DUAL-CLASS STRUCTURES

In this Part, I will examine the variation in voting inequality across the 293 companies and 27 years examined in my sample. Part II.A explains how dual-class charters regulate voting inequality. Parts II.B and II.C examine degree and duration of voting inequality, across charters and across time.

A. Dual Class Features

Many provisions of dual-class charters deal with the voting rights of shareholders. I have identified eight contractual mechanisms (consisting of one or more charter provisions)

that affect voting inequality.[51] They all contribute to the particular design of each company's dual-class structure.

Each of these mechanisms can be set up in different ways. For example, one mechanism is the authorization and issuance of multiple classes of shares with different voting rights. Most companies issue two classes of shares, but others issue three or more. Another example is the right of high-vote shareholders to transfer their super-voting power to third parties (which affects the duration of voting inequality). Most charters authorize high-vote shareholders to transfer their super-voting power only to affiliated entities or family members, but some charters authorize the transfer to unrelated buyers, and others prohibit the transfer even when it is in favor of family members. For brevity, I will refer to the specific setup of each mechanism as a "feature" of that particular dual-class design.

(a) Classes of common stock. As explained above, dual-class structures can have two or more classes of common stock. While most charters authorize two different classes of stock with different voting rights, some charters authorize three or more classes of stock.[52] In particular, the degree of voting inequality is affected by the presence of authorized but unissued no-vote shares. which if issued would dilute high-vote shareholders' ownership rights but not their voting rights, thus increasing the size of the control lock. Warby Parker, for example, has a voting ratio of 10:1 (corresponding to a 9.09% control lock), but also 150 million authorized no-vote shares. This means that Warby Parker's controllers can issue no-vote shares and keep a 50% voting power with less than 9.09% of common stock. (More precisely, they can reduce their participation down to 3.87%).

(b) Voting ratio. It is the ratio between the number of votes per share attached to high-vote shares and the number of votes per share attached to low-vote shares.[53] CarGurus, for example, has a voting ratio of 10:1 (high-vote shares have 10 votes per share, whereas low-vote shares have 1 vote per share). AirBnB, by contrast, has a voting ratio of 20:1 (high-vote shares have 20 votes per share, whereas low-vote shares have 1 vote per share). Other things being equal, a voting ratio of 10:1 corresponds to a control lock of 9.09% (high-vote shareholders can have 50% of the votes with 9.09% of common stock), whereas a voting

51. The dual-class mechanisms discussed here are largely consistent with what Professor Winden and Professors Bebchuk & Kastiel found in smaller samples. *See* Winden, *supra* note 12, at 863–86 (focusing on sunrise and sunset provisions in dual-class stock companies); Bebchuk & Kastiel, *supra* note 12, at 1474–87 (analyzing mechanisms that allow controllers to reduce their equity stake without relinquishing control).

52. In some cases, the classes of common stock are formally more than two, but the various high-vote classes are effectively sub-classes with identical rights. SAIC, Inc., for example, has two classes of common stock—Common Stock and Class A Preferred Stock (which, despite the name, has the same economic rights as the Common Stock class and therefore I consider common stock)—but the Class A Preferred Stock is in turn divided into four different "series": Series A-1 Preferred Stock, Series A-2 Preferred Stock, Series A-3 Preferred Stock, and Series A-4 Preferred Stock. SAIC, Inc., Annual Report (Form 10-K) 4 (May 1, 2006). All four series of high-vote stock have the same voting power, namely ten votes per share; therefore, I consider them (and other structures of similar kind) as two-class structures.

53. When there are three or more classes of shares, I measure the voting ratio of the highest-vote class to the lowest-vote class. There are some exceptions, where the third or fourth class of stock is clearly meant for a very limited and special use and therefore, I exclude them from the calculation of the voting ratio. In the IPO of Nexstar Broadcasting Group, for example, one-vote shares are issued to public investors, ten-vote shares are kept by pre-IPO owners, and nonvoting shares are given to a banking investor (Banc of America Capital Investors) for regulatory reasons. In these types of cases, I calculate the voting ratio between the ten-vote shares and the one-vote shares, ignoring the special-purpose class.

ratio of 20:1 corresponds to a control lock of 4.76%. When the low-vote shares have no voting rights, the voting power differential is virtually infinite.

(c) Ownership-based sunset. Some charters contain an automatic conversion mechanism whereby all high-vote shares convert into low-vote shares if and when the equity interest of high-vote shareholders falls below a certain threshold. This provides for the automatic conversion of all high-vote shares into low-vote shares if and when high-vote shareholders (or specific high-vote shareholders, such as the founders or other key decision-makers) cease to hold a minimum fraction of shares or votes. Such threshold is calculated in different ways. Sometimes it is a fraction of total common stock, other times it is a fraction of total voting rights, or a fraction of the original number of high-vote shares outstanding immediately after the IPO.

Sometimes the ownership-based sunset does not affect the control lock, because the threshold is set at a lower level than the one sufficient to keep 50% voting power. Many times, however, ownership-based sunsets increase the size of the control lock, thus making the structure less unequal. At Internet Brands, for example, a voting ratio of 20:1 (and no authorized no-vote shares) would normally correspond to a 4.76% control lock, but an ownership-based sunset triggers the conversion of the shares into single-class shares if high-vote shares cease to represent at least 20% of common stock. Hence, the control lock is 20%.

(d) Time-based sunset. Some charters provide for the winding down of the dual-class structure after a certain number of years after the IPO. In these cases, the company will become a single-class company after the expiration of the time-based sunset.

(e) Event-based sunset. Some dual-class structures have a sunset provision linked not to a fixed period but to specific future events that may happen at an unspecified time. Most event-based sunsets are linked to the death, disability, or departure of the founders or key executives from the company. A handful of charters link the sunset to other kinds of events, such as the spin-off of the high-vote participation by the parent company or the sale by a private equity controller.

(f) Transfer. Dual-class charters usually regulate what happens to the high-vote power when shares are sold or donated to someone else. Some structures allow high-vote shareholders to transfer their superior voting rights to buyers, while other structures limit this possibility only to specific categories of transferees, such as affiliated entities or family members. In some cases, transfer of high-vote power is outright prohibited.

(g) Voluntary conversion. Most dual-class charters allow high-vote shareholders to convert their own shares into low-vote shares voluntarily.

(h) Special control rights. Some dual-class charters give high-vote shareholders the power to appoint the majority of directors regardless of their actual voting power. In these cases, voting inequality does not arise from multiple voting rights per share, but from built-in special rights that do not depend on the number of high-vote shares owned.

Table 3 reports the frequency of the most common dual-class features in my sample. For each charter mechanism, there is one dominant feature, which is often found in the majority or the vast majority of charters. Note, however, that different combinations of these features create a significant degree of contractual diversity across companies. The most common contractual design, which is the combination of all the dominant features, is chosen by only 12.3% of dual-class companies, whereas almost half of the companies (46.1%) choose a unique contractual design, which no other company has adopted. There

seems to be, therefore, a significant degree of customization in the choice of dual-class features. Yet, as I will show in the following parts, when we measure the combined effect of these contractual features on the degree and duration of voting inequality, much of the heterogeneity disappears and most companies are shown to choose similar or identical levels of voting inequality.

Table 3. Dual-Class Features

Features	% of sample
Classes of common stock	
- 2 classes	89.1%
- 3 classes	9.9%
- 4 classes	1.0%
Voting ratio	
- 10x	74.4%
- 20x	6.5%
- 5x	4.4%
- Other	14.7%
Ownership-based sunset	
- No sunset	49.8%
- 10% common stock	17.1%
- 20% common stock	4.8%
- 5% common stock	4.1%
- 15% common stock	3.1%
- 10% votes	0.7%
- 20% of high-vote shares at IPO	0.3%
- Other	20.1%
Time-based sunset	
- No sunset	76.5%
- 7 years after IPO	8.5%
- 10 years after IPO	8.5%
- 5 years after IPO	3.1%
- 20 years after IPO	1.0%
- Other	2.4%
Event-based sunset	
- No sunset	57.7%
- Death, disability, departure	38.9%
- Sale, board resolution etc.	2.0%
- Spin-off, split-off	1.4%
Transferability of super-voting power	
- To family and affiliated entities	38.8%
- To affiliated entities only	37.9%
- To any third parties	9.9%
- To nobody	3.4%
Voluntary conversion	
- Permitted	98.0%
- Not permitted	2.0%
Special control rights	
- Not included	94.5%
- Included	5.5%
Dual-class designs	
- Most common (most common features)	12.3%
- Unique design	46.1%

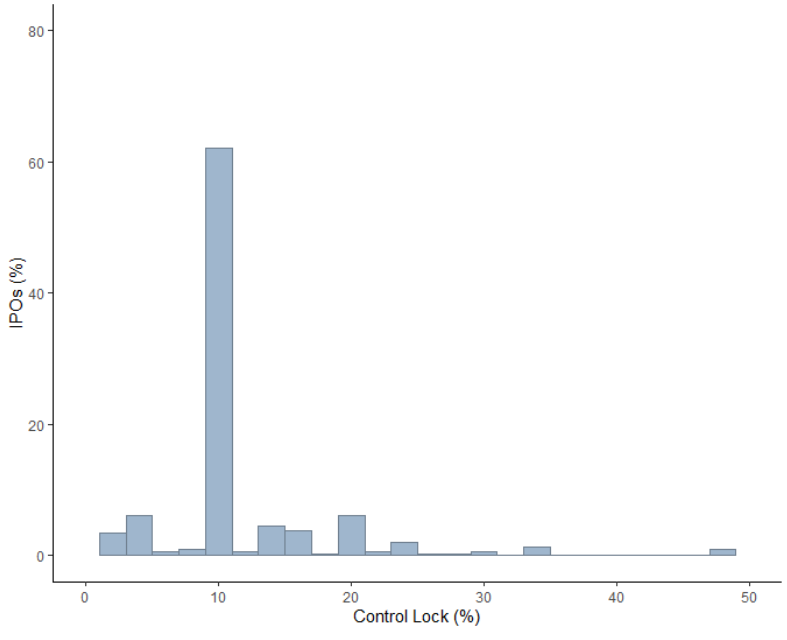
The Table reports the frequency of the most common dual-class features in the sample and the frequency of certain dual-class designs (i.e. combinations of features).

B. Degree of Voting Inequality

1. Across Companies

To examine the effects of charter features on the degree of voting inequality, I measured the control lock for each of the 293 dual-class structures. The control lock is the combined result of some of the charter mechanisms discussed in the previous Parts: the *voting ratio* (which directly affects the relative voting power of different classes of shares), the presence of authorized but unissued *no-vote shares* (which, if and when issued, increase the wedge between the controller's voting power and her equity interest), *ownership-based sunsets* (which set a minimum fraction of equity for the high-vote shareholders, therefore limiting the potential degree of voting inequality), and the *voluntary conversion* of high-vote shares into low-vote shares (which allow high-vote shareholders to sell high-vote shares after stripping them of their super-voting power, thus avoiding a dilution of their voting power).[54] Figure 2 reports the distribution of the size of the control lock for the entire sample.

Figure 2. Degree of Voting Inequality



Distribution of the size of the control lock in the sample. The control lock is the smallest percentage of common stock that high-vote shareholders must own to have 50% of votes, assuming that high-vote shareholders use all the tools available to them under the charter adopted at the IPO.

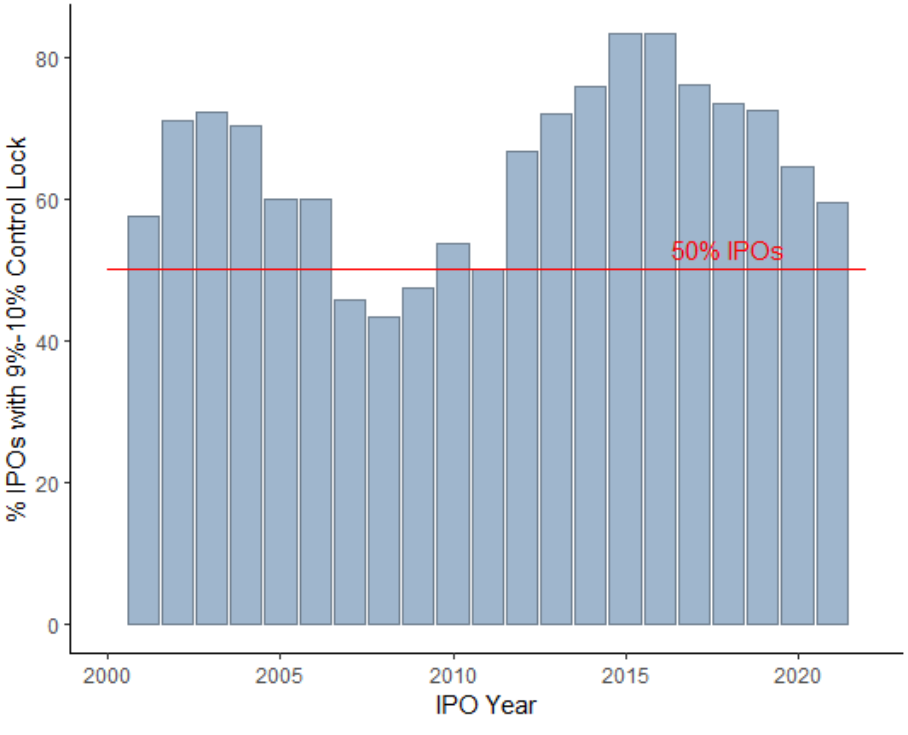
54. When high-vote shareholders sell shares to third parties, the dilution of their voting power is heavily affected by whether the transferred shares keep or lose their high-vote rights. Voluntary conversion allows a seller, in the absence of a transfer conversion provision, to convert their high-vote shares into low-vote shares right before transferring them, thus reducing the vote dilution effect.

Strikingly, of all possible degrees of voting inequality that insiders and public investors can agree upon, from a control lock of slightly more than 0% (extreme inequality) up to a control lock of slightly less than 50% (very low inequality), most companies (62%) choose structures with a control lock in the very narrow range between 9% and 10%. Only 15% of companies choose structures with a control lock between 10% and 20%, and less than 7% of companies choose structures with a control lock greater than 20%. There is therefore an unmistakable concentration of choices in a very small segment of the potential spectrum of voting inequality. A very high degree of homogeneity dominates the choice of voting inequality in dual-class contracting.

2. Across Time

The 9%–10% control lock dominates dual-class charters across the entire sample period. Figure 3 shows that, throughout the 27 years analyzed in my sample, a substantial majority of dual-class structures have a 9%–10% control lock, with the only exception being the period of the 2008-2010 financial crisis, characterized by very few IPOs.

Figure 3. 9%–10% Control Lock across Time



The figure reports the percentage of dual-class IPOs with a control lock between 9%–10% in each year and the four preceding years (5-year moving period). The red line indicates the 50% level on the vertical axis.

Indeed, historical evidence suggests that the 9–10% control lock has been the "norm" for decades. One empirical study of dual-class recapitalizations between 1976 and 1987 mentions in passing that the dual-class structures examined for the study assigned low-vote shares "one vote per share and/or [the right] to elect a minority of the board of directors" and high-vote shares "ten votes per shares and/or [the right] to elect a majority of the board."[55] Other articles in the 1980s refer to a voting ratio of 10:1, as the "typical scheme" of dual-class companies.[56] In the absence of no-vote shares and ownership-based sunsets, a 10:1 voting ratio corresponds to a 9.09% control lock; therefore, it is possible that a 9%-10% control lock was already the norm in the 1970s and 1980s.

3. Individual Characteristics

Interestingly, the size of the control lock does not seem significantly affected by factors that are believed to be connected to the categorical choice between dual-class and single-class structures. The empirical literature on dual-class companies has found that companies with an active founder, family firms, and larger companies are more likely to choose a dual-class structure; whereas companies backed by venture capitalists (VCs) and companies with an independent chair are less likely to choose a dual-class structure.[57]

A plausible explanation for these statistical associations is that founders and family members receive larger psychological benefits if the company they founded or the company that belongs to their family remains under their control. Similarly, larger companies and companies with poorer corporate governance (e.g., overlapping roles of CEO and chair) allow controllers to extract more pecuniary private benefits.[58] In all these cases (psychological or pecuniary private benefits), insiders will be willing to accept a lower firm value to keep control over the company and extract those benefits. By contrast, companies with stronger investor oversight (VC backing) or stronger board monitoring (independent chair) tend to limit the extraction of private benefits and therefore make the choice of dual-class structure less appealing for the insiders.[59]

However, these characteristics do not seem to affect the prevalence of the 9%-10% control lock across dual-class companies. As Figure 4 shows, in each subset of the sample built by selecting one of those characteristics (companies with founder control vs other companies; family firms vs other firms; companies in the top quartile of market

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55. Gregg A. Jarrell & Annette B. Poulsen, *Dual-Class Recapitalizations as Antitakeover Mechanisms: The Recent Evidence*, 20 J. FIN. ECON. 129, 136 (1988).

56. *See, e.g.*, Louis Lowenstein, *Shareholder Voting Rights: A Response to SEC Rule 19c-4 and to Professor Gilson*, 89 COLUM. L. REV. 979, 989 (1989) ("In a typical scheme . . . the public shareholders wind up with Class *A* shares, the insiders get Class *B* shares, and each Class *B* share has as much as ten times as many votes as a Class *A*.").

57. For the correlation between dual-class structures and family firms and firms with an active founder, see Gompers, Ishii & Metrick, *supra* note 31, at 1084 (finding that "[t]he most powerful predictor is whether a person's name appears in the company's name at the time of the IPO."). For the correlation between dual-class structures and the presence of an independent chair, see Laura Casares Field & Jonathan M. Karpoff, *Takeover Defenses of IPO Firms*, 57 J. FIN. 1857, 1860 (2002). For the correlation between dual-class structures and size of the firm and venture capital backing, *see* Scott B. Smart & Chad J. Zutter, *Control as a Motivation for Underpricing: A Comparison of Dual and Single-Class IPOs*, 69 J. FIN. ECON. 85, 95 (2003).

58. *See, e.g.*, Ronald J. Gilson, *Controlling Shareholders and Corporate Governance: Complicating the Comparative Taxonomy*, 119 HARV. L. REV. 1641, 1649 (2006).

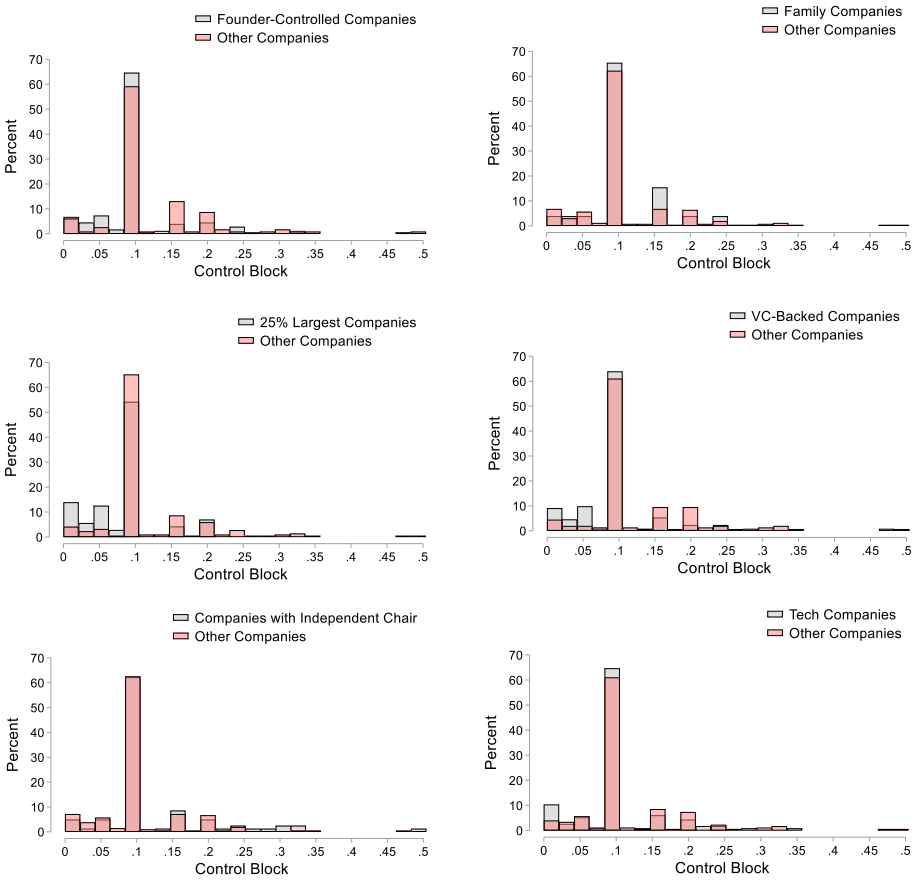
59. *Id.*

capitalization vs other companies; VC-backed companies vs other companies; and companies with an independent chair vs other companies) most companies choose a 9%-10% control lock. Even in the subsets of tech companies, on the one hand, and companies in other industries on the other hand, most firms choose a 9–10% control lock.

In the multivariate regression model presented in Table 4, only one of these variables (market capitalization) is statistically significant at the 5% level: larger companies are more likely to choose a smaller control lock. But even in this case, the magnitude of the effect is very small: one billion dollars of greater market capitalization are associated with a control lock that is smaller by 0.11%.

As Table 5 shows, dual-class companies that deviate from the 9–10% norm (contrarians), whether in the direction of greater voting inequality (high-inequality contrarians) or lesser voting inequality (low-inequality contrarians), are somewhat different from the other dual-class companies. For example, high-inequality contrarians are more likely to be founder-controlled, larger, backed by VCs, and without an independent chair. But even in this case, when we use these variables as predictors of whether the company will be conformist, high-inequality contrarian, or low-inequality contrarian, as in Table 6, only market capitalization is statistically significant for high-inequality contrarians, and only founder control is statistically significant for low-inequality contrarians. The former effect is quite small (one billion dollars of greater market capitalization are associated with a greater likelihood that the company is a high-inequality contrarian by approximately 8%), whereas the latter effect is large (companies with founder control are about 61% less likely to be low-inequality contrarians).

Figure 4. Control Lock and Firm Characteristics: Subsamples



Each histogram in this Figure reports the frequency of different sizes of the control block in certain subsets of dual-class companies in the sample. From the top left quadrant and proceeding clockwise, the histograms compare the frequency of control blocks in (1) companies with founder control vs other companies, (2) companies with family control vs other companies, (3) companies in the top quartile of the market capitalization vs other companies, (4) VC-backed companies vs other companies, (5) companies with an independent chair vs other companies, and (6) tech companies vs other companies.

Table 4. Control Lock and Firm Characteristics: Multivariate Regression

	Coefficient	**P-value**
Control Lock		
Founder control	-0.0196271	0.104
Family control	-0.0301149*	0.053
Market capitalization	-0.001089**	0.041
VC backing	-0.0174936	0.076
Independent chair	0.0127153	0.197
Tech industry	0.0003591	0.971
IPO Year FE	YES	
Observations	293	
R-squared	0.1804	

The Table reports the coefficients and p-values of a linear regression model in which the size of the control lock is the outcome variable and the characteristics indicated in the first column are the predictor and control variables.

*** p-value ≤0.01, ** p-value ≤0.05, * p-value ≤0.10

Table 5. Dual-Class Conformists and Contrarians: Subsamples

	Conformists	**High-Inequality Contrarians**	**Low-Inequality Contrarians**
Total companies	183	47	63
Founder control	62.8%	76.6%	42.9%
Family control	9.3%	6.4%	9.5%
Market cap	4.0 BB	10.4 BB	2.0 BB
VC backing	46.7%	68.1%	25.4%
Independent chair	27.9%	19.1%	34.9%
Tech companies	41.0%	46.8%	30.2%
Firm age	19.8 years	17.5 years	26.5 years
CEO age	49.1 years	45.9 years	50.6 years
Size of the board	6.9 directors	7.0 directors	7.0 directors

The table reports the total number of companies and means of certain variables in each of the following three subsamples: (a) conformists (companies with a 9%-10% control), (b) high-inequality contrarians (control lock < 9%), and (c) low-inequality contrarians (control lock >10%).

Table 6. Dual-Class Conformists and Contrarians: Multivariate Analysis

	Coefficient	**P-value**
High-inequality contrarians vs conformists		
Founder control	0.342257	0.556
Family control	0.146642	0.868
Market capitalization	0.076777***	0.003
VC backing	0.552521	0.205
Independent chair	-0.29351	0.559
Tech industry	-0.37676	0.376
Low-inequality contrarians vs conformists		
Founder control	-0.94665**	0.03
Family control	-1.0685	0.107
Market capitalization	-0.06358	0.315
VC backing	-0.70519	0.125
Independent chair	0.195444	0.611
Tech industry	-0.00123	0.998
IPO Year FE	YES	
Observations	293	
R-squared	0.1804	

The Table reports the coefficients and p-values of a multinomial logistic regression model in which the outcome variable is whether a company is a conformist, high-inequality contrarian, or low-inequality contrarian. "Founder control" means companies in which, at the IPO or following the full divestment of VC investors, (a) the founder (or co-founder) is CEO or executive director, and nobody has more than 30% of the votes at the IPO or (b) the founders have more than 30% of the votes at the IPO. "Family control" means companies in which at the IPO the CEO or Chairman is a member of the founding family and/or the founding family has more than 30% of the votes. "Tech industry" are companies with the following 3-digit SIC codes as reported in their IPO prospectus: 357, 366, 367, 382, 737, or 873.

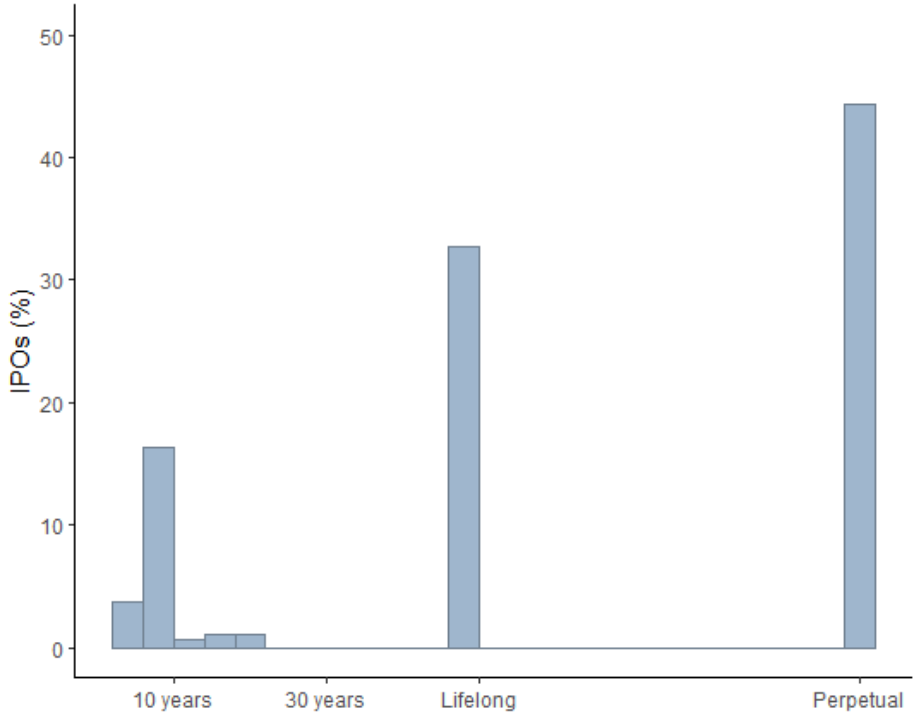
*** p-value ≤0.01, ** p-value ≤0.05, * p-value ≤0.10

C. Duration of Voting Inequality

1. Across Companies

A similar pattern of convergence on a "norm" can be observed for the duration of voting inequality. Despite the potentially broad spectrum of customization (from a few months to the entire life of the corporation), the vast majority of dual-class structures in the sample (77%) choose an unlimited duration, whether for the entire life of the founder or key controller (lifelong duration) or the entire life of the corporation (perpetuity). Figure 5 reports the relative frequency of different durations of voting inequality.

Figure 5. Duration of Voting Inequality

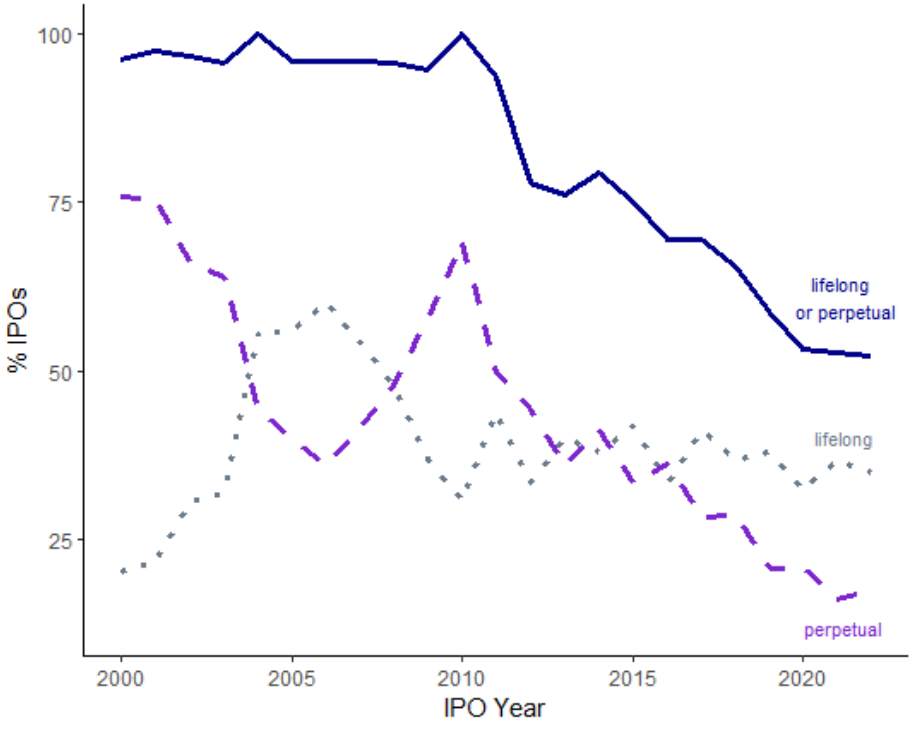


Distribution of duration of voting inequality in dual-class IPOs. Perpetual dual-class structures are structures with no time-based sunsets, no conversion upon death, disability, or departure, and either (a) the right to transfer high-vote power to family members or third-party buyers; or (b) a corporate controller (excluding private equity firms). Lifelong dual-class structures are structures with no time-based sunsets, and either (a) conversion upon death, disability, or departure or (b) conversion upon transfer to family members. Time-based structures are structures with a time-based sunset or a private equity controller with an explicit change-of-control conversion clause.

2. Across Time

In this case, however, market practice has changed dramatically over time. Before 2011, more than 96% of dual-class structures have lifelong (27%) or perpetual (69%) durations. From 2011 onwards, by contrast, the percentage of lifelong or perpetual structures went down to 58%, and perpetual structures became quite infrequent (21% in the 2011–2022 period, 13% in 2021–2022). Figure 6 shows the relevant trends.

Figure 6. Duration of Voting Inequality Across Time



Percentage of dual-class IPOs with a lifelong or perpetual duration in each year and the four preceding years (5-year moving period). Perpetual dual-class structures are structures with no time-based sunsets, no conversion upon death, disability, or departure, and either (a) the right to transfer high-vote power to family members or third-party buyers; or (b) a corporate controller (excluding private equity firms). Lifelong dual-class structures are structures with no time-based sunsets, and either (a) conversion upon death, disability, or departure or (b) conversion upon transfer to family members.

3. Individual Characteristics

Interestingly, the decision to adopt a time-limited duration does not seem to be associated with the age of the CEO. Similarly, the decision does not seem to be associated with the other characteristics that are believed to predict the categorical choice between dual-class and single-class structures, except for VCs backing.

Table 7 reports some descriptive statistics and Table 8 reports the results of a multinomial regression for the period 2011-2022 (in the previous period, virtually all dual-class structures were either lifelong or perpetual structures). In this period, VC-backed firms are about 73% less likely than other firms to have a lifelong structure and about 91% less likely to have a perpetual structure.[60] All the other predictor variables are not statistically significant.

60. This finding is consistent with Aggarwal et al., *supra* note 12, at 147. None of the four family firms, by contrast, have a time-limited structure.

Table 7. Duration and Company Characteristics: Subsamples

	(a) Time Limited	**(b) Lifelong**	**(c) Perpetual**
1996-2010			
Total companies	5	39	98
Founder control	40.0%	46.1%	40.8%
Family control	20%	5.1%	19.4%
Market cap	1.4 BB	2.4 BB	2.5 BB
VC backing	0%	25.6%	18.4%
Independent chair	80%	33.3%	30.6%
Tech companies	20%	25.6%	16.3%
CEO age	53	52.5	50.7
Size of the board	9.2 directors	6.5 directors	6.4 directors
2011-2022			
Total companies	62	57	32
Founder control	91.9%	82.5%	43.7%
Family control	0	17.5%	9.4%
Market cap	6.1 BB	6.9 BB	7.6 BB
VC backing	90.3%	68.4%	31.2%
Independent chair	19.3%	21.0%	34.4%
Tech companies	72.6%	52.6%	43.7%
CEO age	45.3	45.5	51.6
Size of the board	7.6 directors	7.3 directors	6.8 directors

The table reports the total number of companies and mean of certain variables in each of the following subsamples: (1) time limited, (b) lifelong, and (c) perpetual dual-class structures, before 2011 and from 2011 onwards.

Table 8. Duration and Company Characteristics: Multivariate Analysis

	Coefficient	**P-value**
Time-limited structures vs other structures		
Founder control	0.28	0.659
Family control	-13.74***	0.000
Market capitalization	-0.02*	0.089
VC backing	1.87***	0.002
Independent chair	-0.01	0.990
Tech industry	0.70	0.069
CEO age	-0.00	0.833
IPO Year FE	YES	
Observations	151	
Pseudo R-squared	0.1804	

The Table reports the coefficients and p-values of a logistic regression model in which the outcome variable is whether a company has a time-limited structure or a lifelong/perpetual structure. "Founder control" means companies in which, at the IPO or following the full divestment of VC investors, (a) the founder (or co-founder) is CEO or executive director, and nobody has more than 30% of the votes at the IPO or (b) the founders have more than 30% of the votes at the IPO. "Family control" means companies in which at the IPO the CEO or Chairman is a member of the founding family and/or the founding family has more than 30% of the votes. "Tech industry" are companies with the following 3-digit SIC codes as reported in their IPO prospectus: 357, 366, 367, 382, 737, or 873.

*** p-value ≤0.01, ** p-value ≤0.05, * p-value ≤0.10

* * *

This Part has mapped the dual-class landscape by reporting data on the variety of contractual features, as well as the variation of degree and duration of voting inequality within dual-class companies and across time. Such analysis has shown three main characteristics of this landscape.

First, dual-class companies do adopt a variety of charter provisions, and although most features are clearly "dominant" (i.e., they are found in most dual-class charters), there is a significant degree of variation in how these features are combined in any given charter.

Second, despite such contractual variation, most dual-class companies end up having a very similar or identical degree of voting inequality, measured by the control lock, which is the minimum percentage of common equity needed to have a majority of votes. In theory, dual-class structures can choose a control lock from slightly above 0% to slightly below 50%; in practice, most companies (62%) choose structures with a control lock in the very narrow range between 9% and 10%, and such a pattern has been in place at least since 1996 (and possibly for decades before then). Furthermore, before 2011 almost all dual-class companies had lifelong or perpetual duration, whereas from 2011 onwards perpetual structures have become rare, and time-limited structures have been on the rise.

Third, degree and duration of voting inequality seem to be only modestly affected by certain characteristics traditionally associated with the categorical dual-class choice, with very few exceptions. Founder-controlled companies are much less likely to be low-inequality contrarians compared to companies without founder control; and, starting from

2011, VC-backed companies are much less likely than other dual-class companies to have a lifelong or perpetual structure.

In sum, the dual-class landscape presents striking patterns of recurring choices, both across companies with different characteristics and across time. Although some firm characteristics—such as founder control for low-inequality contrarians and VC backing for time-limited structures—seem to have some significant effects, the overall structure of dual-class contracting reveals two strong trends: most companies, including in subsamples with potentially relevant characteristics, choose a 9%-10% control lock, and virtually all companies used to choose lifelong or perpetual duration before 2011 and now choose either lifelong duration or time-limited duration.

But how do these choices get made and why do they tend to converge on certain recurring patterns? In Part III, I will examine the dual-class contracting process through the eyes of senior IPO lawyers who are key players in it.

III. DUAL-CLASS CONTRACTING AS SEEN BY IPO LAWYERS

In Part II, we saw that most dual-class companies choose similar or identical degrees of voting inequality, that virtually all dual-class companies chose lifelong or perpetual structures before 2011, and that, starting from 2011, perpetual structures have become rare, and time-limited structures have been on the rise. But what is the process through which these design choices are made? In this Part, I will examine how senior lawyers with expertise in dual-class IPOs experience the process of dual-class contracting.

Lawyers tell a largely consistent story, which is different from the textbook model of an IPO. According to the textbook story, the founder and investment banker negotiate the most appropriate governance features to maximize the joint surplus for insiders and outsiders. In this interaction, founders want to maximize the sum of firm value and private benefits, whereas investment bankers, as representatives of the public investors, care only about firm value. In addition, venture capitalists are also expected to care exclusively about firm value. The result should be a tailor-made voting structure that fits the specific characteristics of the founder and the company.

According to the lawyers' experience, by contrast, value maximization is surrounded by high uncertainty and the identification of a company-specific optimal level of voting inequality is not a central concern of the various players. On the contrary, there is a strong pressure to conform to "standard" structures, rather than to design a customized one. The role of ensuring conformity with market practice is primarily played by the issuer lawyers, who, in this account, have a much more consequential role than investment bankers.

In the following Parts, I will discuss how senior lawyers view the process leading to the final charter as well as the role of the various market players in influencing the final decisions. All the observations about the dual-class IPO process that are not otherwise qualified or specified are based on what the respondents said in the survey or in the follow-up interviews.[61]

61. Anonymized survey response data and interview notes are on file with the *Journal of Corporation Law*.

A. The Players

The IPO pricing process is an intricate exercise where different players, with different information and incentives, interact with one another to discover the correct price for the stock. According to the standard story, the crucial role is played by the underwriters, and particularly the lead underwriter (which I will simply call the "investment banker"), who acts as the representative of the public investors.[62] Although insiders and public investors do not negotiate directly, insiders and investment bankers do, to some extent. It is the investment banker who is supposed to warn the company against any charter provisions that might negatively affect the IPO price.[63] Investment bankers play a triple role—adviser to the issuer, buyer of the new shares, and re-seller to the public.[64] They have an incentive to set a high price (because its fees are calculated as a fraction of the offer price) but not so high that investors might decide not to buy the stock (because they bear the risk of not being able to re-sell it). They organize the "roadshow," where corporate managers present their company to the investor community, allocate the offer among interested investors, and price the offer based on the manifestations of interests received.

Other players too, however, play an important role in the process. Corporate insiders are not a monolith: founders typically have different preferences and goals than VCs, executives, and employee-shareholders;[65] independent directors, where present, are supposed to have a yet different set of goals.[66] Lawyers are supposed to perform a merely technical function, by explaining the legal implications of possible options and translating the final choices into legal language; yet we will see that they do not perceive their role in such a narrow way. Finally, investors may provide feedback to the investment banker, thus influencing the design of the dual-class charter. In the following Parts, I will examine how senior lawyers perceive and interpret the process leading to the choice of a given dual-class structure and the role that each of the above actors plays in this process.

B. The Process

1. The Choice of the Precedent

What does the process leading to a dual-class charter look like? According to some interview respondents, lawyers are the first, most important, and most trusted advisers to corporate insiders during the IPO process. In many cases, the IPO lawyer is the same lawyer who has advised the founder and the company since the start-up stage, and who advises the founder on other legal matters, both personal and professional. This kind of self-

62. *See, e.g.*, Frank H. Easterbrook & Daniel R. Fischel, *The Corporate Contract*, 89 COLUM. L. REV. 1416, 1429 (1989) ("[Corporate] contracts usually are negotiated by representatives . . . . [I]nvestment banks [negotiate] on behalf of equity investors").

63. *Id.*

64. RICHARD A. BREALEY, STEWART C. MYERS & FRANKLYN ALLEN, PRINCIPLES OF CORPORATE FINANCE 371 (10th ed. 2011)

65. For a discussion of the "vertical and horizontal tensions between founders, investors, executives, and employees," see generally Elizabeth Pollman, *Startup Governance*, 168 U. PA. L. REV. 155 (2019). For a discussion of "interinvestor conflicts" among VCs, see Robert P. Bartlett, III, *Venture Capital, Agency Costs, and the False Dichotomy of the Corporation*, 54 UCLA L. REV. 37 (2006).

66. For an analysis of the role of independent directors in start-ups, see Brian J. Broughman, *The Role of Independent Directors in Startup Firms*, 2010 UTAH L. REV. 461.

perception may well be biased, of course, but it largely reflects a widespread view in the IPO industry.[67]

Company's managers and the founder (or other key decision makers)[68] meet with the lawyers to understand what the IPO process entails, and which decisions need to be made to make progress. The choice between dual-class and single-class structure is one such decision; another important, more technical decision is the choice of the specific dual-class features. Lawyers initially discuss these issues with the founder, with the company's general counsel, and with other key managers; at a later stage, they discuss them with the entire board.

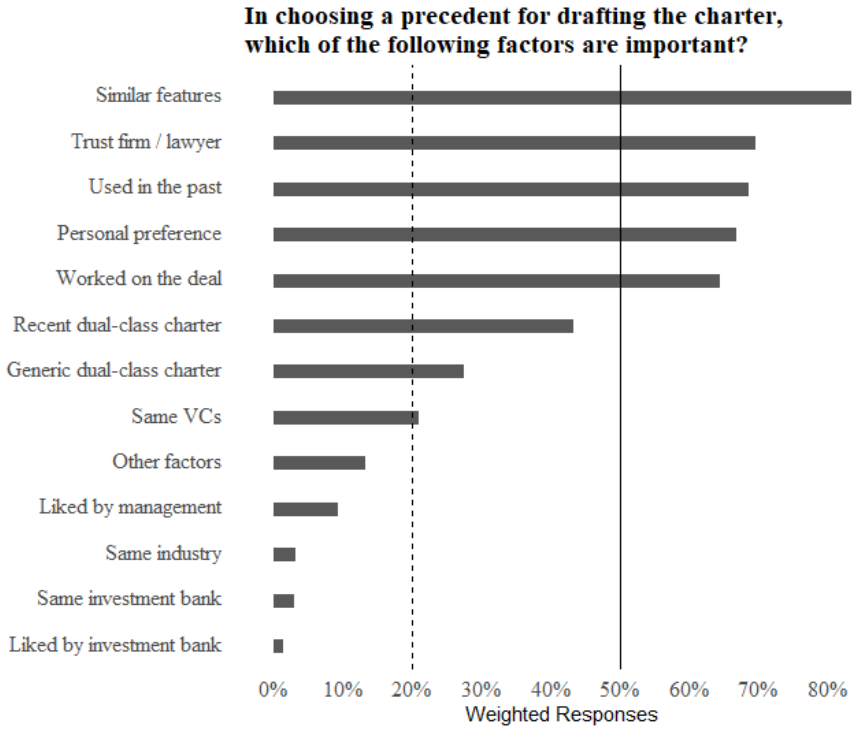
How are these decisions made? According to the respondents, the issuer lawyer explains to the founder and other key managers the dual-class design of recent or comparable companies. Law firms have standard slide decks to explain what a dual-class structure is and how the most important or relevant dual-class companies have structured their voting mechanisms. This basic presentation does not focus on the details of a dual-class structure, but only on its key features, such as voting ratio and time-based sunsets. It is the lawyer who typically chooses the most pertinent precedent to use as a model. Bankers, according to a very experienced interview respondent, do not participate in this choice, as they believe that "unless you have a weird structure" the market will not penalize you.

When choosing a previous dual-class charter to use as a "precedent" for the new IPO, lawyers tend to favor dual-class charters prepared by their firms "unless there is a very good reason to start from another precedent" (100% of respondents confirmed this). Furthermore, as Figure 7 shows, when selecting the most appropriate precedent, lawyers tend to choose charters with features like those they plan to use in the new IPO and charters they have personally worked on in the past or that have been used by lawyers or firms they trust. By contrast, they do not give much weight to the fact that the charter has been used by a company in the same industry, or in an IPO in which the same VCs or investment banks were involved. The fact that corporate managers or the investment bank "likes" the precedent seems to be irrelevant as well. In short, the choice of the "precedent" seems to be firmly within the purview of the lawyers.

67. *See, e.g.*, PWC, ROADMAP FOR AN IPO: A GUIDE TO GOING PUBLIC 70, https://explore.pwc.com/c/intro?x=nmqemH [https://perma.cc/P43L-TTPU] ("A company's attorney will become the quarterback of the [IPO] process.").

68. I will generally refer to the "founder" as many dual-class companies are founder-led, but the same considerations apply to other key decision makers and controllers. For a recent study of founder control in tech IPOs, see Brian Broughman & Jesse M. Fried, *Do Founders Control Start-up Firms That Go Public?*, 10 HARV. BUS. L. REV. 49 (2020).

Figure 7. How Issuer Lawyers Choose a Dual-Class Precedent

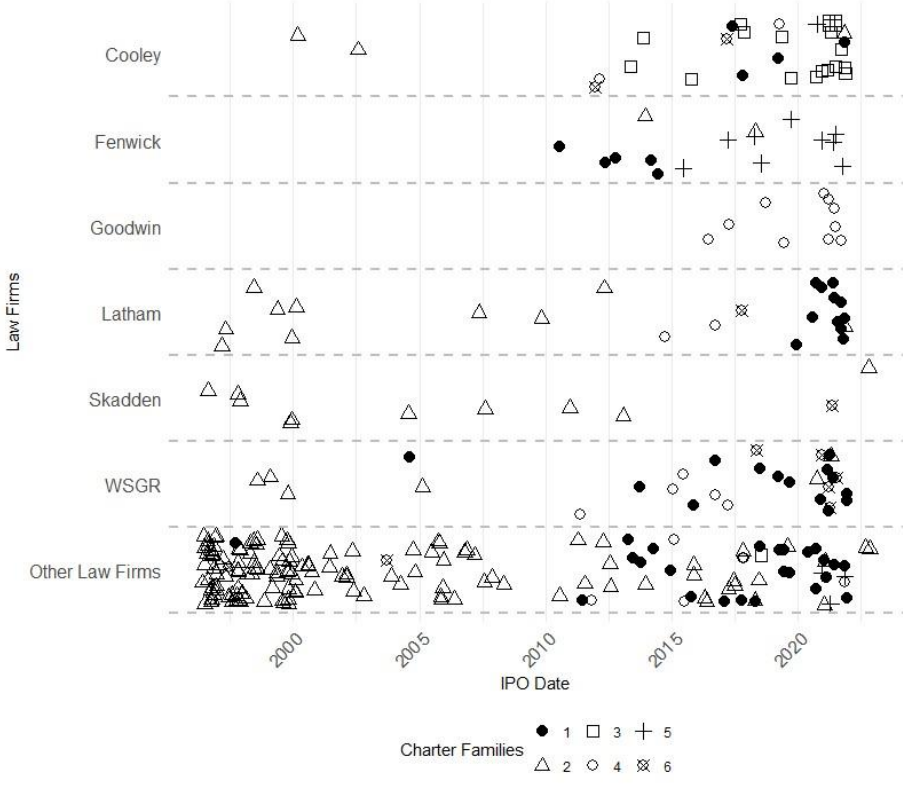


The Figure reports the percentage of respondents (weighted by overall experience with dual-class IPOs) who answered "Important" to the question "In choosing a precedent for drafting the dual-class IPO charter, how important are the following factors?" The results are based on 37 responses.

Indeed, a computational textual analysis of the 293 charters in my sample confirms that law firms tend to rely on internal precedents, but occasionally some precedent "travels" from one law firm to other law firms. Figure 8 plots the use of dual-class charter "precedents" by issuer law firms over the entire sample period. To identify the use of "precedents," I applied standard techniques in natural language processing to transform each of the 293 charters in my sample into a vector of three-word strings (tri-grams) and then compare all these vectors according to a metric of text similarity called "cosine similarity." In this way, I identify six "charter families," each of which includes dual-class charters with a high degree of text similarity, thus suggesting that all the charters in the same family probably descend from the same precedent.[69]

69. To identify the "charter families" I used the following procedure. First, I created a corpus with the texts of all the 293 charters. Second, I tokenized the text, removing punctuation, numbers, symbols, URLs, stop-words, and separators, and converting the tokens into lowercase. Third, I converted the tokens into tri-grams

Figure 8. Law Firms and Charter Models



The Figure plots the use of charters belonging to one of six different "families" by the five major law firms in dual-class IPOs and by other law firms, from 1996 to 2022. Each shape represents one charter adopted by a dual-class company at the IPO, with different shapes representing different "charter families" identified with NLP techniques. The horizontal axis indicates the date of the IPO. The vertical axis indicates the law firms drafting the charter, separated by dashed lines.

(combinations of three tokens), to capture phrases. Fourth, I created a document-term matrix (DTM) from the preprocessed tokens, and I weighted the DTM using the standard method of term frequency-inverse document frequency (TF-IDF) to account for the importance of terms. Fifth, I computed a cosine similarity matrix to measure the similarity between documents, and I converted the matrix into a distance matrix (the inverse of a similarity matrix). Sixth, I performed hierarchical clustering using the Ward D2 method, and I plotted a dendrogram to visualize the clusters. Finally, to identify the individual "families," I "cut" the dendrogram at a certain "height" based on a visual inspection of the dendrogram, with the assistance of the so-called "elbow method," which consists in plotting the total within-cluster sum of squares against a range of cluster numbers. This plot helps to identify the number of clusters that minimizes the sum of squares within clusters. Once I identified a plausibly "optimal" number of clusters, I assigned the various charters to the different clusters, which I termed "charter families." This method of hierarchical clustering and identification of the optimal number of clusters inevitably involves some degree of subject judgment. For an overview of these natural language processing (NLP) techniques, see DANIEL JURAFSKY & JAMES H. MARTIN, SPEECH AND LANGUAGE PROCESSING (3d. ed. draft 2024), https://web.stanford.edu/~jurafsky/slp3/ed3bookfeb3_2024.pdf [https://perma.cc/E8HS-KG6T].

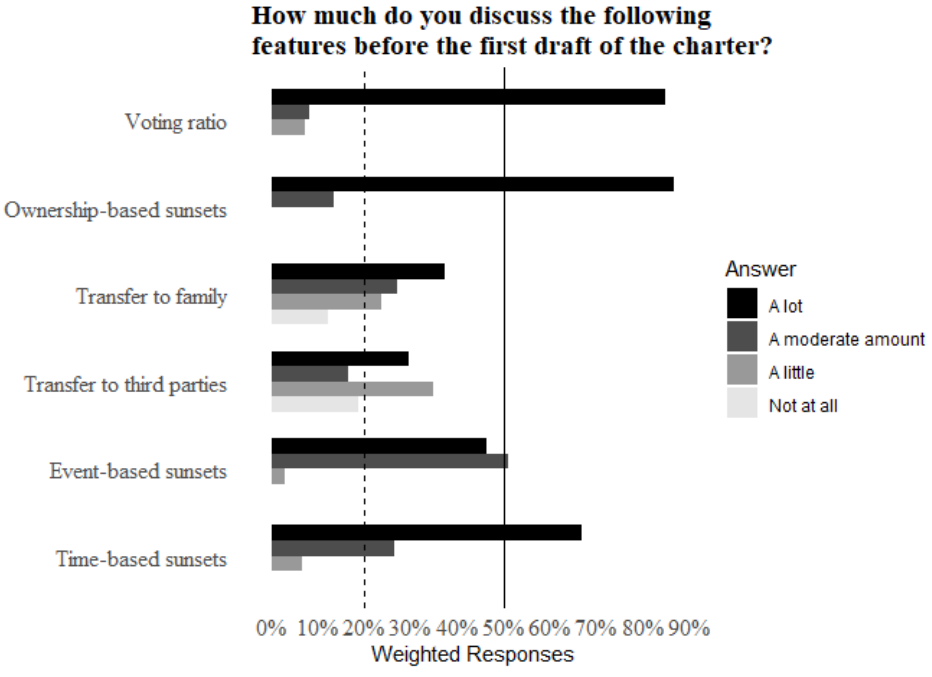
As the Figure shows, before 2011, almost all dual-class companies used a Family 2 charter (represented in the Figure by empty triangles), and most companies were assisted by law firms other than the six major law firms that came to dominate the dual-class IPO market in the second half of the sample period. Around 2011, however, the landscape changed. Goodwin, Fenwick, and Cooley emerged as the three top players in dual-class IPOs; WSGR and Latham consolidated and expanded their influence, whereas Skadden and other law firms lost market share.

As already observed, law firms tend to reuse their precedents. Survey respondents acknowledge this phenomenon. Successful new precedents, however, tend to travel from one law firm to others. For example, after Google went public with a Family 1 charter drafted by WSGR (in Figure 8, the solitary full circle with an IPO in 2004), Family 1 charters started being adopted by companies assisted by other law firms (first Fenwick, then Cooley and Latham). Similarly, after LinkedIn went public with a Family 4 charter drafted by WSGR (in Figure 8, the solitary empty circle with an IPO in 2011), Family 4 charters started being adopted by other law firms. These two "templates" were very uncommon when these visible and large companies adopted them; afterward, they spread rapidly. In other cases, the contagion is limited or nonexistent. Family 5 charters (represented in Figure 8 by a plus sign) appeared in 2015 with FitBit's IPO, but the use of this template remains mostly confined to Fenwick. Family 3 charters (represented in Figure 8 by an empty square) appeared in 2013 with Tableau Software's IPO, but Cooley remained the only user of this template throughout the sample period.

2. Discussing Dual-Class Features

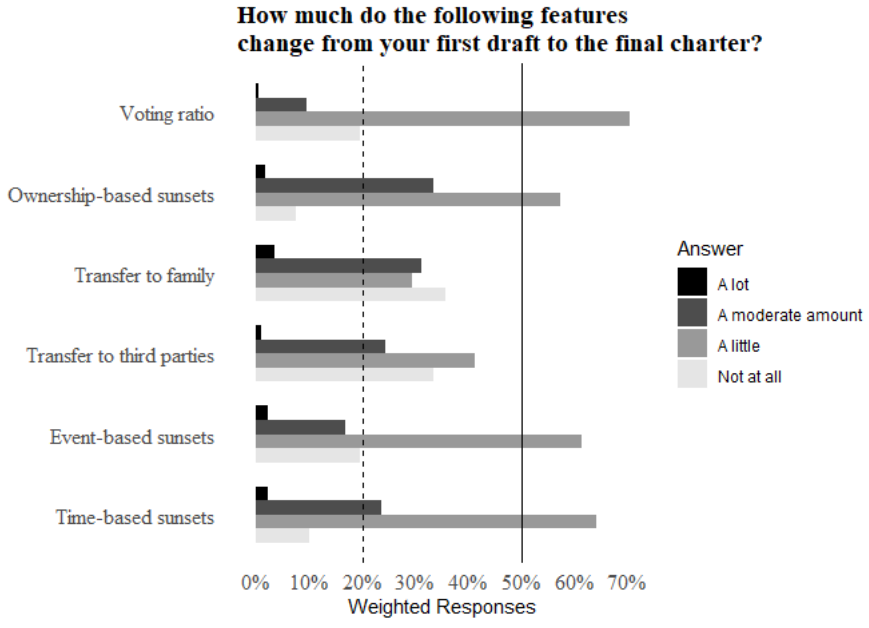
Before finalizing the first draft of the charter, lawyers discuss the most important dual-class features with their clients and the other advisors. Voting ratio and ownership-based sunsets are almost invariably discussed "a lot," and time-based sunsets receive significant attention too. By contrast, event-based sunsets and transfer mechanisms receive much less attention. After the first draft is finalized, these features rarely change in a significant way, although some of them are slightly or moderately revised. Figures 8 and 9 report the relevant answers.

Figure 9. Discussion of the Dual-Class Features Before the First Draft



The Figure reports the percentage of responses (weighted by overall experience with dual-class IPOs) to the question "How much are the following features of a dual-class IPO charter discussed with the client and other advisors before the first draft of the charter?" The results are based on 37 responses.

Figure 10. Change of the Dual-Class Features After the First Draft

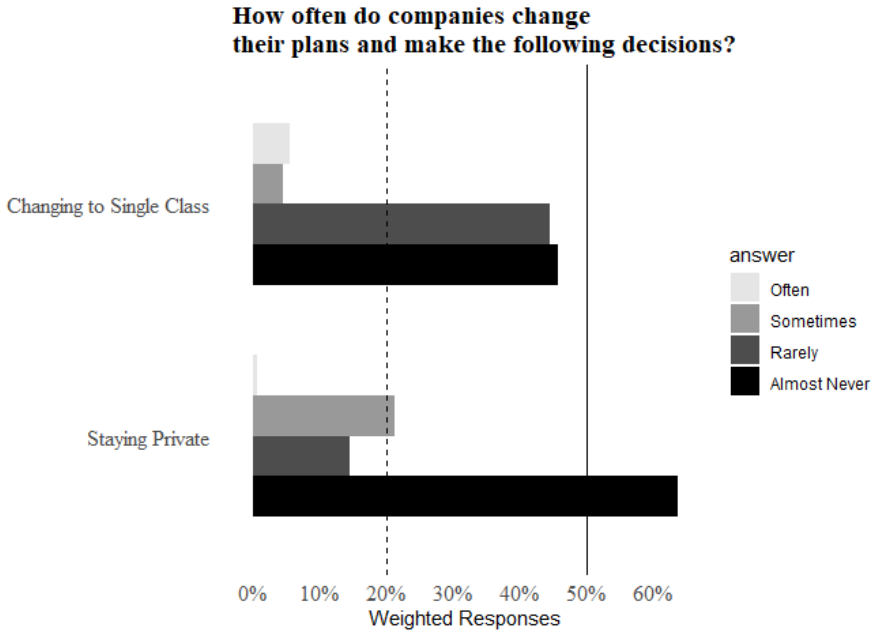


The Figure reports the percentage of responses (weighted by overall experience with dual-class IPOs) to the question "How much do the following features of a dual-class IPO charter change from your first draft to the final charter?" The results are based on 37 responses.

Similarly, the categorical decision to go public with a dual-class structure rarely changes during the process. Whereas a significant minority of respondents (21.8%) have experienced the decision to abandon an IPO altogether ("often" or "sometimes"), much fewer (9.9%) have seen companies revising the decision from a dual-class to a single-class structure with similar frequency.[70] Figure 11 reports the relevant responses.

70. This finding is consistent with the view that "a key alternative for dual-class firms is not necessarily to opt for a single-class IPO, but rather to remain private." Ofer Eldar, *Dual-Class IPOs: A Solution to Unicorn Governance Failure* 9 (Eur. Corporate Gov. Inst. Law Working Paper No. 741/2023, 2023), http://ssrn.com/abstract_id=4647143.

Figure 11. Revising the Categorical Decision



The Figure reports the percentage of responses (weighted by overall experience with dual-class IPOs) to the questions "How often does a company that would like to go public as a dual-class company decide to stay private rather than going public as a regular single-class company?" and "How often does a company that initially wants to go public as a dual-class company end up going public as a regular single-class company?" The results are based on 37 responses to the first question and 36 responses to the second question.

3. Marketing the IPO

Once the company has decided to go public, the investment bankers normally begin conversations with the investor community to assess the interest in the company.[71] During this phase, called in jargon "testing the waters," bankers use materials prepared together with the management and other advisers to present the company and the structure of the IPOs.[72] According to the interview respondents, these materials might mention that the company will choose a dual-class structure but do not typically include information on specific dual-class features.

The next stage, the "roadshow," happens after the filing of the preliminary prospectus.[73] According to the interview respondents, dual class features are not typically presented or discussed in the roadshow, either. The dual-class structure is mentioned, and some key features such as voting ratio and time-based sunsets might be mentioned in some

71. PwC, *supra* note 67, at 6.
72. *Id.* at 86.
73. *Id.*

cases, but as long as these key features are "standard," investors would not typically ask questions about the dual-class structure. As one experienced interviewee put it, investment bankers believe that the details of the dual-class structure are a "distraction" and they do not want to draw attention to them. The best strategy to avoid questions on the structure is to choose the most standard features, which is what bankers strongly recommend.

A draft of the charter adopted at the IPO is included in the registration statement as an exhibit. In some cases, it is filed together with the preliminary prospectus; in other cases, it is filed only with an amendment to the preliminary prospectus. Some but not all features of the dual-class structure are also summarized in the body of the prospectus.

C. The Role of Market Players

As we saw in the previous Part, according to the participants in the survey and the follow-up interviews, founders and key managers are educated about dual-class structures primarily by the lawyers, who choose the most appropriate precedent mostly based on their professional judgment. Furthermore, the details of the dual-class structure do not seem to be salient during the marketing phase, and they tend to remain unchanged throughout the IPO process. Similarly, the categorical decision between dual-class and single-class structures, once made, is very rarely revised. In other words, the initial decisions about adopting a dual-class structure and choosing specific dual-class features tend to be sticky.

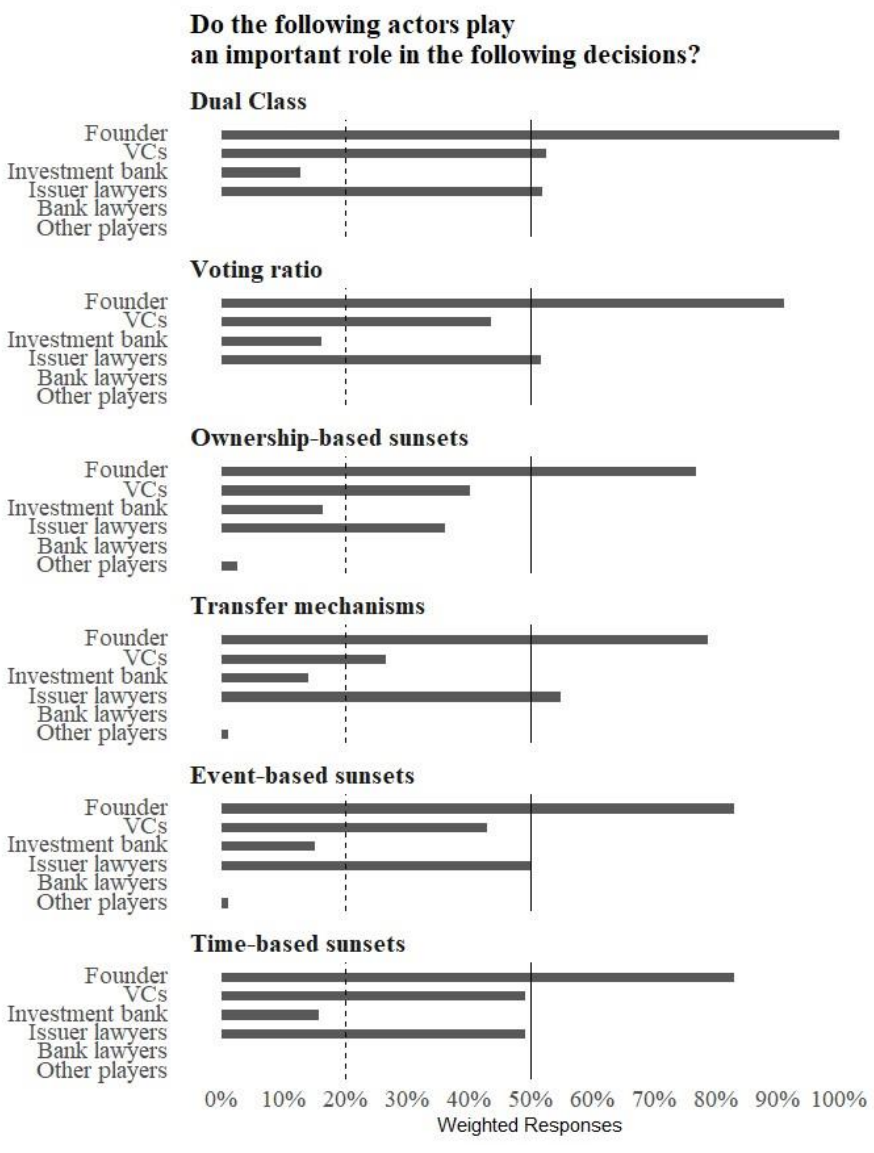
The next question is thus how these initial decisions get to be made and what role the various market players have in this process. Does the process resemble the standard, textbook story, in which the investment bank and the VCs negotiate with the founder to maximize firm value, whereas the founder seeks to balance firm value and private benefits, and the lawyers perform the technical task of explaining the legal implications of the various options and translating the final decisions into legal language?

To understand the process from an inside point of view, I asked the respondents to indicate the importance of the role played by founders, VCs, investment bankers, issuer lawyers, investment bank lawyers, public investors, and other players in some of the main decisions concerning the design of the dual-class structure: the categorical decision between single class and dual class, and the main dual-class features, such as voting ratio, ownership-based sunsets, transfer mechanisms, event-based sunsets, and time-based sunsets. Figure 12 reports the answers of the respondents, weighted according to their level of experience.

1. Founders

Unsurprisingly, there is universal agreement among respondents that the founder has an important role in shaping the features of the dual-class charter. Figure 12 reports the relevant responses. According to interview respondents, most founders start with very superficial notions on dual-class structures, and they are educated primarily by the lawyers. In some cases, however, founders have learned that other founders have successfully used certain features and want to emulate them.

Figure 12. Role of Market Players in Dual-Class Design



The Figure reports the percentage of respondents (weighted by overall experience with dual-class IPOs) who answered "An important role" to the question "Do the following parties and advisors play a role in determining the final shape of the following dual-class charter features?" The results are based on 37 responses.

This kind of emulation between founders happens not only with respect to dual-class IPOs, but with governance features in general. One experienced lawyer reported, for example, that after the unusually large compensation package that Tesla approved for Elon Musk, many founders inquired about the possibility of replicating similar packages for themselves. With respect to dual-class structures, founders often exchange information with other founders and start-up contacts in their social and professional circles and develop preferences or make final decisions based on this information. In an interesting episode reported by an interview respondent, a founder was initially inclined to accept the advice of the lawyers and to include a time-based sunset in the charter; then he asked a fellow founder, who led a dual-class company that had gone public with a time-based sunset, about the rationale for choosing the specific number of years for the company's sunset provisions. Since the fellow founder told him that the number of years "was completely random," with no economic rationale, the client of the respondent decided to exclude a time-based sunset from the charter. As another experienced lawyer put it, the founder community is "a village," meaning that it is a relatively close community in which information travels quickly and denizens of the community compare themselves and their experiences with one another.[74]

2. Investment Bankers

Contrary to the conventional narrative, respondents believe that the investment banker does not play an important role in the design of the dual-class structure. Only 13% of respondents believe that the investment banker has an "important role" in the categorical decision between dual-class and single-class structure. Similarly, few respondents believe that the investment banker has an important role in determining the voting ratio (16%), ownership-based sunsets (16%), transfer mechanisms (14%), event-based sunsets (15%), or time-based sunsets (16%).

According to some interview respondents, investment bankers do not have effective tools to push back against the founder's preferences. As one very experienced lawyer puts it, "the problem with bankers is that they can't really point to something investors don't like." Another very experienced lawyer said that "nobody can ever say whether a dual-class feature hurts [the price] or not. Bankers cannot really draw a line."

One respondent mentioned a case in which the company management asked the banker to "run the price" based on different assumptions, or to model a "dual class discount," but the banker could not. The respondent commented that bankers cannot model the price discount of dual-class as compared to single-class structures, let alone the effect of specific dual-class features. Another respondent reported that, in their experience, bankers believe that, as long as the dual-class structure is "normal," investors are indifferent

74. Benchmarking is a common practice in CEO compensation as well. *See* LUCIAN BEBCHUK & JESSE FRIED, PAY WITHOUT PERFORMANCE: THE UNFULFILLED PROMISE OF EXECUTIVE COMPENSATION 71–72 (2004) (discussing how "generous benchmarking" tends to "rachet" up CEO pay); John M. Bizjak, Michael L. Lemmon & Lalitha Naveen, *Does The Use of Peer Groups Contribute to Higher Pay and Less Efficient Compensation?*, 90 J. FIN. ECON. 152, 152 (2008) (finding that the "use of benchmarking is widespread and has a significant impact on CEO compensation"); Alex Edmans, Tom Gosling & Dirk Jenter, *CEO Compensation: Evidence from the Field*, 150 J. FIN. ECON. 103718 (2023) ("several studies have shown that CEO pay is correlated with peer pay").

between dual class and single class. In other words, conforming to what is standard is more important and useful than trying to estimate the value-maximizing customized features.

When it comes to dual-class contracting, the banker's role seems to be, just like the lawyers' role discussed below, to advise the company to "stick to what's standard." But since this "conformization" role has been previously and, according to the lawyers, more effectively performed by the issuer lawyers, the residual role of the banker is relatively modest.

To gather more information on the role of the investment banker, I asked the lawyers to indicate how often investment bankers worry about the negative price effect of certain high-inequality features: higher voting ratio than 10:1, transferability of super-voting power to family members after death, absence of ownership-based or time-based sunsets, and long time-based sunsets (15 years or longer). As Figure 13 shows, bankers seem to worry about a higher voting ratio than usual and, to a slightly lesser extent, unlimited-duration structures, but they worry much less about less salient features such as ownership-based sunsets, transfer mechanisms, or even longer-than-usual time-based sunsets.

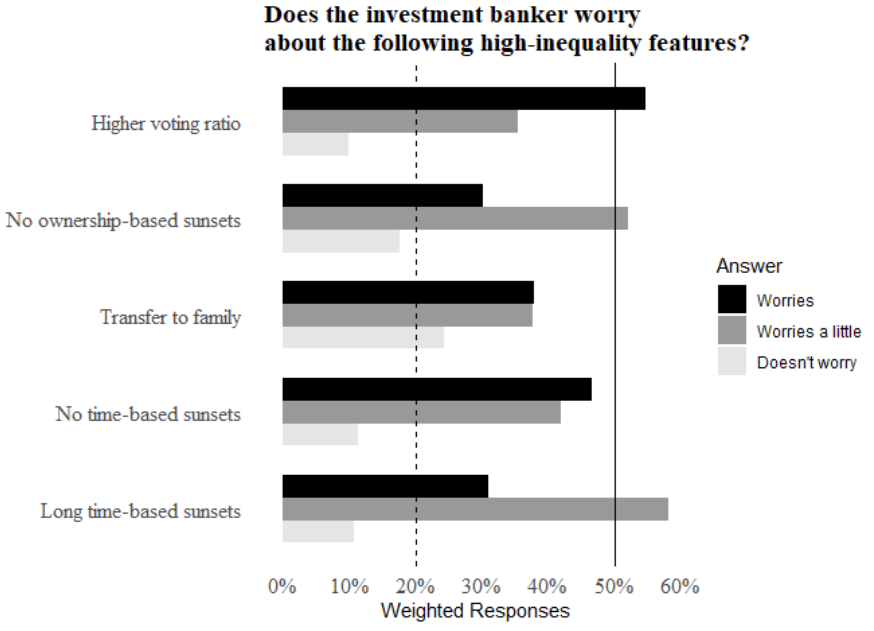
3. Venture Capitalists

Consistent with the conventional narrative, many respondents believe that VCs play an important role in dual-class contracting. This perception is stronger, however, for the categorical choice between dual-class and single-class structures than for the specific features of a dual-class structure. Indeed, as shown in Part II, there is no statistical association between VC backing and the size of the control lock, or even the decision to conform or deviate from the norm; there is however, starting from 2011, a statistical association between VC backing and the presence of a time-based sunset.

In the interviews, respondents added that usually VCs and founders do not have pre-existing agreements in place on whether the future IPO will be dual-class or single-class, let alone on the specific features of a dual-class IPO. One very experienced lawyer observed that the business model of VCs is very founder-friendly, and several interview respondents said that they have never experienced significant pushback from VCs on the dual-class structure designed by the company and its lawyers, unless it presented non-standard features.[75]

75. This picture of founder-friendly VCs is at odds with the traditional account of venture financing, according to which VCs actively monitor founders to reduce their extraction of private benefits. For a standard exposition of this account, see PAUL GOMPERS & JOSH LERNER, THE VENTURE CAPITAL CYCLE 157–271 (2d ed. 2006); Ronald J. Gilson, *Engineering a Venture Capital Market: Lessons from the American Experience*, 55 STAN. L. REV. 1067 (2003). For a recent study proposing an alternative account of venture financing, which persuasively explain why VCs have incentives to be more founder-friendly than the traditional account suggests, *see* Brian J. Broughman & Matthew T. Wansley, *Risk-Seeking Governance*, 76 VAND. L. REV. 1299 (2023).

Figure 13. Bankers' Reaction to High-Inequality Features



The Figure reports the percentage of responses (weighted by overall experience with dual-class IPOs) to the question "How often does the investment bank worry that the following charter features, which the client would like to include, may affect the IPO price?" The results are based on 29 responses.

4. Issuer Lawyers

According to the respondents, the most important actors in dual-class design after the founder are—surprisingly—the company lawyers. The perception of the importance of the issuer lawyers is stronger than that of VCs and much stronger than that of the investment bankers. Respondents working primarily as issuer counsel, and respondents working also as, or primarily as, underwriter counsel both share this view. Issuer lawyers are perceived as the first and most important filter that pushes against the founder's idiosyncratic preferences.

Such a widespread belief might seem puzzling, given that lawyers are commonly thought of as merely technical advisers: they are supposed to be agents of their clients, not autonomous players. However, this perception becomes sensible, and in fact quite obvious, when one considers the respondents' narrative, according to which, "market norms" play a significant role in the shaping of the dual-class contract. Lawyers are not only technical advisers, who explain the legal implications of rules and agreements, but also mentors and shepherds, who educate and guide founders and directors through the IPO process, its various stages, the written rules, and the unwritten norms.

Some respondents characterized standard dual-class structures using the same golf metaphor ("middle of the fairway") and explained their role as company lawyers as conveying to the company what is standard and what is not and trying to reshape the founder's

non-standard preferences into a standard-complying structure. As one very experienced lawyer put it: "If you can't point to a precedent, it's problematic."

The interaction of the lawyers with the founders is perceived by the same lawyers as the main driver of norm-conformity. As one respondent put it, "founders trust [lawyers] . . . [and] usually the conversation with the lawyers is decisive," for the shape of the dual-class structure. One experienced respondent observed that in many cases the lawyer has advised the founder since the company's formation and is one of the founder's most trusted advisors, who advises the founder also on estate planning matters and other personal issues (with the help of specialists). Another very experienced respondent observed that the responsibility of making the proposed structure consistent with standard practice is shared between issuer lawyers and bankers, "but it's more of a lawyer's job."

These findings are consistent with the sociological literature on law firm culture in Silicon Valley, particularly the work of Mark Suchman and Mia Cahill. In a 1996 article, Suchman & Cahill observed, based on semi-structured interviews with lawyers, venture capitalists, and entrepreneurs, that "Silicon Valley attorneys see themselves (and are seen by others) as key players in an informal apparatus of socialization, coordination, and normalization that serves to avert potential disputes between members of the local business community."[76] According to this study, lawyers "identify, create, transmit, and enforce the emerging norms of the community."[77]

More recently, Professor John Coyle and Joseph Green, based on interviews with attorneys working in New York and in the Research Triangle in North Carolina, painted a similar picture of startup lawyers outside of Silicon Valley.[78] Startup lawyers, Coyle and Green observe, serve as "transmitter of norms" and "actively work to instill these norms in their clients."[79] I will return to this point in Part IV.

A puzzling aspect of the respondents' narrative is that virtually all of them consider norms extremely important, but at the same time, most of them believe that the market is unable to price the terms of a dual-class charter and deviations from the norm are rarely met with hostility or actual price discount unless they are very salient and significant. This attitude raises the question of why market actors care about norms. If investors rarely push back and investment bankers are unable to model the price effect of dual-class features, what are advisers (and lawyers in particular) worried about?

Respondents do not have a clear answer. Two respondents, one of them very experienced, mentioned the publication of negative articles by the financial press. As one respondent put it, lawyers do not want to read "on the Wall Street Journal that [their client] is a control freak." Another respondent mentioned "downstream market reaction." Another very experienced respondent mentioned the risk of "get[ting] burned." Publicly salient episodes might rapidly evolve into a reputational disaster. As one respondent put it, "investors are like lemmings." Some respondents also believe that publicly salient episodes create and change market norms.

A plausible interpretation of these and other responses is that the risk lawyers (and bankers) are worried about is not sub-optimal pricing, but that the IPO becomes publicly

76. Mark C. Suchman & Mia L. Cahill, *The Hired Gun as Facilitator: Lawyers and the Suppression of Business Disputes in Silicon Valley*, 21 LAW & SOC. INQUIRY 679, 683 (1996).

77. *Id.*

78. John F. Coyle & Joseph M. Green, *Startup Lawyering 2.0*, 95 N.C. L. REV. 1403 (2017).

79. *Id.* at 1425.

perceived as a failure and the failure is associated, at least in part, with governance issues and to unusual dual-class features. In other words, the main preoccupation of lawyers and bankers is not strictly about value-maximization per se, but about a major visible failure. Publicly salient episodes are also, according to some respondents, the way these norms emerge and evolve. As mentioned above, one very experienced respondent believes (more or less accurately) that perpetual structures have become taboo after the spectacular failure of WeWork's IPO. Another experienced respondent conjectured that the use of conversion mechanisms in case of death of the founder might have been influenced by some salient fact, such as the death of a superstar founder like Steve Jobs.[80] Whether or not these beliefs accurately describe reality, it is an interesting fact that dual-class norms are considered very important but at the same time are believed to be driven by publicly salient episodes rather than by careful economic analysis.

5. Public Investors

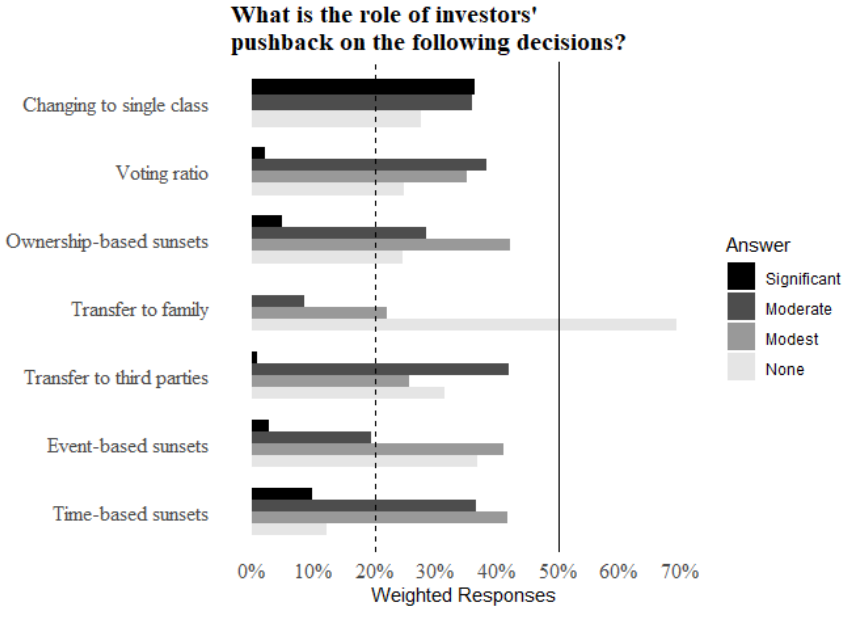
So far, we have been focusing on the market players directly involved in the initial decisions of going public with a dual-class structure and choosing specific dual-class features. Although interview respondents report that dual-class designs do not receive significant attention during the marketing phase, it is nonetheless possible that bankers and managers receive negative feedback and pushback from the investor community and therefore decide to revise some of these choices based on such feedback. This is after all consistent with the textbook story of the IPO process.

To shed light on this aspect, I asked lawyers to indicate what role, in their experience, investors' feedback plays in the decision to abandon a dual-class structure and instead adopt a single-class structure, and what role investors' feedback plays in the final design of specific dual-class features. Figure 14 reports the relevant responses.

Once again, the lawyers' narrative defies the textbook model. Public investors are believed to play a very modest role in the (infrequent) cases in which the company abandons its plans to go public with a dual-class structure and decides instead to adopt a single class structure. Furthermore, in the experience of most respondents, the pushback from public investors on dual-class features is only "a little" or "a moderate amount," and for about a third of respondents it is often nonexistent. Less than 13% of respondents report that investor pushback is "a lot."

80. Death conversion provisions did indeed become more and more frequent starting from 2011, the year Jobs died. Such an explanation, however, seems highly speculative.

Figure 14. Role of Public Investors' Feedback in Dual-Class Design



The Figure reports the percentage of responses (weighted by overall experience with dual-class IPOs) to the question "What factors drive the decision to abandon the plan to go public with a dual-class structure and instead choose a regular single-class structure?", for the factor "Specific pushback from the investor community," and to the question "How much do investors, directly or through the investment bank, push back on the following features of a dual-class IPO charter?" for each of the features reported on the vertical axis. The results are based on 37 responses to the first question and 29 responses to the second question.

Consistent with the hypothesis that some features (such as the voting ratio) are shaped by very strong norms, while other features (those pertaining to duration) are in flux or more vulnerable to individualized contracting, only 2% of respondents report significant investor pushback on the voting ratio, whereas 12% report significant investor pushback on time-based sunsets. In any case, however, investor feedback is not perceived to be a major driver of dual-class design.

The interviews confirm this picture. Respondents have never heard of large investors threatening to pass on an IPO (let alone actually passing on it) because of an aggressive structure. Several experienced lawyers said that they have never heard of dual-class features being changed because of investor pushback. One lawyer mentioned one case in which a company was "hammered" during the roadshow and decided to change from dual-class to single-class structure, but even categorical changes seem to be quite rare.

There is an exception, however. One very experienced lawyer reported that some large institutional investors have strong views on standard dual-class structures and may pass on one that does not conform to the standard. They reported, however, that all their IPOs have been "middle of the fairway," and that they have no experience with companies proposing

aggressive non-standard structures on the roadshow. Their experience of pushback from institutional investors is therefore second-hand. Another interview respondent distinguished crossover investors—who invest at the private company stage and have repeated interactions with the company during the IPO process—and pure public investors, who have very few opportunities to interact with the company. According to this interview respondent, crossover investors do play a somewhat significant role in the design of dual-class features, while regular investors do not.

Consistent with the data showing that perpetual structures have become rare, a respondent reported that "investors push back on transferability to family forever." According to another respondent, the failed IPO of WeWork attracted a lot of attention to perpetual structures and put a stigma on them, when CEO Adam Neumann said that he wanted his descendants to control the company 300 years after the IPO.[81] In reality, although in 2019 the press paid unusual attention to the issue of perpetual structures in connection with Neumann's speech, by that time perpetual structures had already declined significantly. In my sample, perpetual structures represent 69% of the IPOs between 1996 and 2010 and only 27% between 2011 and 2018 (before We's IPO failure). It is possible, however, that the WeWork case, as well as the public campaigns by investor groups and experts, have reinforced and supported this trend, thus contributing to the further decline of perpetual structures (which were only 16% of dual-class structures between 2020 and 2022). I will return to this point in Part IV.C.

Two very experienced lawyers specifically mentioned that whereas stewardship and governance teams of institutional investors have strong views on dual-class structures, portfolio managers do not seem to pay much attention to them. Portfolio managers are those participating in roadshows and interacting with the company and the investment bankers. Some dual-class features become problematic for portfolio managers only if they perceive that they are aggressively non-standard.

IV. WHAT THEORY OF DUAL-CLASS CONTRACTING?

The picture emerging from the data analyzed in Part II and from the experience of IPO lawyers discussed in Part III is a largely consistent story. Dual-class companies may potentially choose a variety of features leading to different levels of voting inequality, yet most of them consistently choose similar or identical degrees and durations of voting inequality. Most companies across the sample and the entire period chose a control lock in the very narrow range between 9% and 10%; before 2011, virtually all companies chose lifelong or perpetual duration; and, starting from 2011, time-limited structures have been on the rise. According to senior lawyers who work on dual-class IPOs, the process leading to these choices leaves little room for customization: issuer lawyers (and to some extent bankers) vigorously and effectively persuade companies to "stick to the norm" and investors do not push back against dual-class features, at least so far as they are "standard." From time

81. *See* Connie Loizos, *Adam Neumann Planned for His Children and Grandchildren to Control WeWork*, TECHCRUNCH (Oct. 18, 2019), https://techcrunch.com/2019/10/18/adam-neumann-planned-for-his-children-and-grandchildren-to-control-wework [https://perma.cc/AP89-C5JV] (quoting Neumann as saying "It's important that one day, maybe in 100 years, maybe in 300 years, a great-great-granddaughter of mine will walk into that room and say, 'Hey, you don't know me; I actually control the place. The way you're acting is not how we built it'").

to time, however, a handful of founders and other controllers refuse to conform and impose their idiosyncratic preferences.

But how should we reconcile this picture with the theory of the corporate contract? In this Part, I will try to situate my empirical findings within different strands of the literature on contractarianism. I will suggest that both the "classical contractarian theory" and the standard explanations of the "modern contractarian theories" are insufficient to explain some peculiarities of dual-class IPOs. I will then suggest an alternative conjecture, which I call the "market norms conjecture," which builds on theories of social norms, as studied by sociologists, economists, and legal scholars.

A. Classic Contractarian Theory

Contractarianism is the dominant theory of the corporation.[82] In this view, corporate charters are "contracts" between managers and investors.[83] In a competitive capital market, charter provisions are priced based on their effect on shareholder value.[84] Hence, insiders internalize this effect and will propose charter provisions that maximize value for all the parties involved (public investors and themselves).[85]

Voting inequality is one important dimension of IPO charters. Whatever the effect of voting inequality on shareholder value, positive or negative, it will be eventually reflected in the IPO price. This mechanism, contractarians argue, creates strong incentives for

82. *See, e.g.*, Robert Anderson, IV, *A Property Theory of Corporate Law*, 2020 COLUM. BUS. L. REV. 1, 1 ("The dominant view of the corporation in legal scholarship is contractarian, one that sees the corporation as a 'nexus of contracts' among the various suppliers of inputs to the business . . . .").

83. For classic defenses of the contractarian theory of the corporation, see generally William A. Klein, *The Modern Business Organization: Bargaining Under Constraints*, 91 YALE L.J. 1521 (1982); Henry N. Butler, *The Contractual Theory of the Corporation*, 11 GEO. MASON U. L. REV., Summer 1989, at 99; Easterbrook & Fischel, *supra* note 62; Jonathan R. Macey, *Corporate Law and Corporate Governance: A Contractual Perspective*, 18 J. CORP. L. 185 (1993); Stephen M. Bainbridge, *Community and Statism: A Conservative Contractarian Critique of Progressive Corporate Law Scholarship*, 82 CORNELL L. REV. 856 (1997) (book review).

For early critiques of the contractarian theory, see generally Victor Brudney, *Corporate Governance, Agency Costs, and the Rhetoric of Contract*, 85 COLUM. L. REV. 1403 (1985); John C. Coffee, Jr., *No Exit?: Opting Out, The Contractual Theory of the Corporation, and the Special Case of Remedies*, 53 BROOK. L. REV. 919, 921 (1988); Lucian Ayre Bebchuk, *Limiting Contractual Freedom in Corporate Law: The Desirable Constraints on Charter Amendments*, 102 HARV. L. REV. 1820 (1989); Robert C. Clark, *Contracts, Elites, and Traditions in the Making of Corporate Law*, 89 COLUM. L. REV. 1703 (1989; Jeffrey N. Gordon, *The Mandatory Structure of Corporate Law*, 89 COLUM. L. REV. 1549 (1989); David Millon, *Communitarianism in Corporate Law: Foundations and Law Reform Strategies*, *in* PROGRESSIVE CORPORATE LAW 1–33 (1st ed. 1995).

For more recent studies on contractarian theory, see generally Lucian Arye Bebchuk, *The Case for Increasing Shareholder Power*, 118 HARV. L. REV. 833 (2005); Klausner, *supra* note 15; Michael Klausner, *Fact and Fiction in Corporate Law and Governance*, 65 STAN. L. REV. 1325 (2013); Jill E. Fisch, *Governance by Contract: The Implications for Corporate Bylaws*, 106 CALIF. L. REV. 373 (2018); Anderson, IV, *supra* note 76; Grant M. Hayden & Matthew T. Bodie, *Codetermination in Theory and Practice*, 73 FLA. L. REV. 321 (2021); Holger Spamann, *Indirect Investor Protection: The Investment Ecosystem and Its Legal Underpinnings*, 14 J. LEGAL ANALYSIS 16 (2022).

84. *See* Klausner, *Fact and Fiction in Corporate Law and Governance*, *supra* note 833, at 1327.

85. *Id.* ("[M]arket forces would lead the parties to create governance arrangements . . . that would . . . thereby maximize firm value.").

insiders to choose value-maximizing charters.[86] A plausible corollary of this view is that what is value-maximizing depends on the specific characteristics of the individual company and its managers. Hence, each company will choose the features with the highest inherent value given the specific characteristics of the firm and the controller. As a favorite motto of contractarians' puts it, "one size does not fit all."[87]

This is a quite accurate summary of what I will call "classic contractarian theory." To illustrate how classic contrarianism would explain dual-class structures, consider the following example. Suppose that Alpha Inc. must decide whether to go public with a single-class structure or with a dual-class structure, and the specific circumstances are such that the dual-class structure has a net negative effect on the value of the firm. Suppose that Alpha stock is worth $100 million (or $100 per share) with a single-class structure and $90 million (or $90 per share) with a dual-class structure. If Alpha proposes a dual-class structure and the public investors can price its net negative effect, they will pay only $90 per share at the IPO. In this scenario, the pre-IPO shareholders (i.e., the insiders) bear the full cost of the dual-class structure in terms of stock value, and the public shareholders are not exploited or abused.

But why would Alpha's insiders choose a dual-class structure and bear the corresponding cost of $10 million? The most plausible reason is that the dual-class structure provides insiders with private benefits, which they valued at least $10 million. Perhaps insiders enjoy overseeing the firm they created; they value the social recognition that comes

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86. A concise and accurate description of the choice of charter provisions at the IPO, according to classic contrarianism, is the following:

> Pre-IPO managers and investors design the firm's governance structure. The market sets the price of the company's shares-a price that is expected to reflect the effectiveness of the firm's governance structure in reducing agency costs-and investors buy those shares in the market. The pre-IPO shareholders are expected to reap the benefit of a good governance structure and the cost of a bad one. They are therefore expected to design optimal governance mechanisms that suit each firm's circumstances and to provide for those mechanisms in the firm's charter-the "corporate contract."

Klausner, *Fact and Fiction in Corporate Law and Governance*, *supra* note 83, at 1327–28. This paradigm is the standard account in the contract law literature as well. *See, e.g.*, Julian Nyarko, *Stickiness and Incomplete Contracts*, 88 U. CHI. L. REV. 1, 7 (2021) ("much of modern legal and economic scholarship on contracts assumes that sophisticated parties routinely write optimal agreements"); Robert E. Scott, Stephen J. Choi & Mitu Gulati, *Revising Boilerplate: A Comparison of Private and Public Company Transactions*, 2020 WIS. L. REV. 629, 629 (2020) ("The textbook model of commercial contracts between sophisticated parties holds that terms are proposed, negotiated and ultimately priced by the parties. Parties reach agreement on contract provisions that best suit their transaction with the goal of maximizing the joint surplus from the contract.").

87. *See, e.g.*, John C. Coffee, Jr., *The Future of Disclosure: ESG, Common Ownership, and Systematic Risk*, 2021 COLUM. BUS. L. REV. 602, 615 (2021) ("It is traditional to begin any discussion that relies on 'law and economics' with the mandatory observation that 'one size does not fit all.'"); Lucian A. Bebchuk & Scott Hirst, *Private Ordering and the Proxy Access Debate*, 65 BUS. LAW. 329, 334 (2010) (reporting that opponents of a regulatory proposal on shareholder rights relied on the argument that "one size does not fit all"); Stephen M. Bainbridge, *The Creeping Federalization of Corporate Law*, 26 REGULATION 26, 29 (Spring 2003) (criticizing the director independence standard introduced by the NYSE and the Sarbanes-Oxley Act because, in corporate governance, "one size does not fit all"); Troy A. Paredes, Comm'r, SEC, Statement at Open Meeting to Propose Amendments Regarding Facilitating Shareholder Director Nominations (May 20, 2009), https://www.sec.gov/news/speech/2009/spch052009tap.htm [https://perma.cc/VWH6-ZMK7] (arguing that "one-size-fits-all mandates are inappropriate for many enterprises," and the appropriate approach is to allow "the internal affairs of each corporation to be tailored to its own attributes and qualities").

with being the head of a visible company; or they do not like the uncertainty associated with the risk of losing their job.[88] All these benefits associated with control are psychological, but control may also entail pecuniary private benefits. For example, the insiders could choose higher than optimal compensation; they can make the company buy services from another firm that they own at a higher than market price; and so forth.[89] The law addresses all these concerns and often deters the most egregious behaviors. Nonetheless, the law cannot realistically reduce these pecuniary benefits down to zero, and a rational self-interested controller would take them into account to some extent. In the above example, the dual-class structure decreases the value of the company by $10 million, the insiders obtain private benefits that they value at least $10 million, and the public investors get a "price discount" of $10 million. All involved parties are getting a fair deal and there is no need for regulatory interference.

As discussed in Part I, however, the allocation of voting rights between insiders and public investors is not a binary choice between single-class and dual-class structures. Voting inequality is a spectrum and different levels of voting inequality should be expected to produce different effects, whatever the effects on shareholder value and private benefits.[90] Thus, the contractarian choice of the optimal voting structure must include the choice of the optimal level of voting inequality.[91]

To examine how companies choose the optimal voting structure in the contractarian model, let us consider the following stylized scenario. An entrepreneur (Founder) owns 100% of the company she founded and now wants to take the company public to fund its further growth while keeping her job as CEO. After the IPO, the Founder will own 51% of the company, and public investors (Investors) will own the remaining 49%. In the following years, the Founder may or may not sell a substantial part of her stock, based on her needs for diversification and other personal considerations.

At the time of the IPO, the Founder must decide the voting structure for her company. She can choose a traditional, single-class structure with voting equality, or she can choose one of many potential levels of voting inequality under a dual-class structure. Each of these structures will have different effects on shareholder value and the Founder's private benefits. Since the Investors can price the positive or negative effects of voting inequality on shareholder value, the Founder will choose the level of voting inequality that maximizes the sum of shareholder value (V) and her private benefits (B).

To illustrate, suppose that the Founder is considering the dual-class structure S_i, in which she can keep a majority of votes with 20% of the shares for her entire life. If there

88. Voting inequality increases the cost of a takeover, as the outside buyer cannot obtain control without the assent of the incumbent controller. Although countervailing forces can exercise considerable pressure on founder-CEOs to step down, these forces are limited by control-enhancing mechanisms such as dual-class structures. *See generally* Yifat Aran & Elizabeth Pollman, *Ousted* (EUR. CORP. GOVERNANCE INST., LAW WORKING PAPER No. 740/2023, 2023).

89. For another example of non-pecuniary benefits, see Broughman & Fried, *supra* note 68, at 55 ("While control can always provide financial private benefits, non-pecuniary private benefits (for example, the satisfaction of bringing new products to market) are likely to be just as—or even more—valuable to the founders of a startup.").

90. For an illustration of this aspect, see Bebchuk & Kastiel, *supra* note 12, at 1466–68

91. *See* Winden, *supra* note 12, at 909 ("The optimal dual-class capital structure will be driven by the characteristics of a given situation and should be negotiated among the parties prior to an initial public offering . . . .").

is an alternative voting structure S_k that increases the aggregate value $(V + B)$ the Founder has an incentive to choose such an alternative structure S_k.

Indeed, if S_k increases shareholder value, the Founder will choose S_k because she will be able to sell shares at the IPO at a higher price and her stock will have a higher value too. If S_k increases her private benefits without harming shareholder value, she will choose S_k because she will be able to increase her own benefits without decreasing the price of the shares. Finally, if S_k decreases shareholder value but increases her private benefits, she will choose S_k if the increase in private benefits is larger than the decrease in shareholder value.

In short, the Founder will choose whichever combination of degree and duration of voting inequality maximizes the aggregate value $(V + B)$. Therefore, Founders with different preferences and companies with different characteristics will end up with different voting structures. This is, in more detailed and accurate terms, what the contractarian motto "one size does not fit all" means: that freedom of contract will lead to significant variation of voting structures across companies.

The evidence discussed in this Article raises some difficult questions for the classic contractarian model. If dual-class companies are supposed to choose value-maximizing levels of voting inequality based on their individual characteristics, why do most companies make similar choices? We do not know, of course, if the "standard" 9%–10% control lock happens to be value-maximizing for a majority of dual-class companies, or if lifelong or perpetual structures used to be value-maximizing for virtually all dual-class companies until 2011. It would be, however, a curious coincidence. Such a striking pattern of conformism is highly suspicious.

The previous literature has discussed at length why standardization and low variation in corporate charters are at odds with the classic contractarian model. As observed by Professor Klausner, low variation in corporate charters warrants "at least some rethinking of the contractarian theory."[92] Even Klausner, however, considered dual-class structures one of the very few instances of "deliberate contracting . . . in the drafting of corporate charters."[93] This Article has shown that this perception of tailor-made contracting in dual-class companies is vastly overstated. When it comes to dual-class contracting, one size seems to fit most.

B. Modern Contractarian Theories

Since the 1980s, when the classic contractarian theory was proposed by the first generation of law & economics scholars, corporate law scholars have directed their efforts to explaining the apparent anomalies of corporate contracting, including the high level of uniformity among corporate charters. Perhaps the most innovative and influential theory of standardization in corporate governance is the one proposed by Professors Michael Klausner and Marcel Kahan in a series of articles published in the 1990s.[94]

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92. Klausner, *supra* note 15, at 782.

93. *Id.* at 789–91. *See also* Fisch, *supra* note 16, at 930 (discussing how shareholders agreements can perform a similar function).

94. *See* Michael Klausner, *Corporations, Corporate Law, and Networks of Contracts*, 81 VA. L. REV. 757 (1995); Marcel Kahan & Michael Klausner, *Path Dependence in Corporate Contracting: Increasing Returns, Herd Behavior and Cognitive Biases*, 74 WASH. U. L.Q. 347, 349 (1996) [hereinafter Kahan & Klausner, *Path*

On this account, which broke from the classic contractarian orthodoxy dominant in those years, charter standardization is driven by learning and network externalities. The more companies adopt a charter provision, the more advantageous is for a new company to adopt it as well. Since the contractual term is familiar to both advisors and courts, the company adopting the standard term saves on advisory costs and reduces the uncertainty of legal interpretation. One possible explanation for the high level of uniformity in corporate charters is therefore that the learning and network benefits of choosing a "standard" structure outweigh the benefits of choosing an optimal but non-standard structure.

Are learning and network externalities a persuasive explanation for dual-class contracting? The dual-class version of this theory would argue that a dual-class company may find it rational to use a dual-class arrangement with lower inherent value than the optimal "tailor-made" arrangement if its adoption by many firms produces enough benefits in terms of drafting efficiency, legal certainty, familiarity to market actors, and network externalities.

In the case of dual-class structures, however, this theory seems much less compelling than in other cases. Dual-class companies can very easily alter the degree or duration of voting inequality with very little cost and virtually no risk of ambiguity or legal uncertainty, but in most cases, they choose not to do so. For example, ownership-based sunsets are well-known charter provisions, found in almost half of the companies in my sample. A threshold of 25% or 35% is not more expensive to write or to understand or interpret than a threshold of 10%, which most ownership-based sunsets adopt. Yet only three companies in my sample choose a 25% or 35% threshold. Similarly, almost all dual-class charters assign high-vote shareholders multiple voting rights per share. A voting power of five votes per share is not more expensive to write or to understand or to interpret than a voting power of ten votes per share. There is hardly any risk of misinterpretation: it is just a different number. Yet, 75% of dual-class companies choose ten votes per share, and only 4% choose five votes per share.[95]

To be sure, the most common features of dual-class structures are indeed more familiar to investors and advisers; therefore, modern contractarians could argue that these more familiar features are more easily priced than unfamiliar features, and that is why adopting them is beneficial. On a closer look, however, this hypothesis assumes that these features produce largely similar effects on different companies, whereas the key expectation of contractarianism, as we saw, is that "one size does not fit all," and therefore the optimal features for different companies should be different.[96]

Dependence] (explaining why there is a high level of uniformity in corporate charters is because learning and network benefits of choosing a "standard" structure outweigh the benefits of choosing an optimal but non-standard structure); Marcel Kahan & Michael Klausner, *Standardization and Innovation in Corporate Contracting (or "The Economics of Boilerplate")*, 83 VA. L. REV. 713 (1997) (finding standardization to be influenced by "learning and network externalities").

95. In fact, some standard provisions in dual-class charters create potential legal uncertainties but their level of standardization appears to be lower than the voting inequality provisions discussed in this Article. *See generally* Caley Petrucci, *Equal Treatment Agreements: Theory, Evidence & Policy*, 40 YALE J. REG. 620 (2023).

96. Other theories seeking to explain uniform corporate governance rely on cognitive biases, such as the "status quo bias," which would discourage market players from departing from standard terms, perceived as the status quo, or the "anchoring bias," which would give standard terms "an aura of stability and objectivity." *See, e.g.*, Kahan & Klausner, *Path Dependence*, *supra* note 94, at 359–62. These hypotheses—admittedly

An alternative explanation is that standardization is primarily driven by the lawyers and therefore charter uniformity is the product of a principal-agent problem. Here the seminal reference is once again the work by Professors Kahan and Klausner. They hypothesized that standardization in corporate contracting might also be driven by lawyers' "herd behavior."[97] This theory is based on two assumptions. The first is that lawyers' reputation is largely based on good or bad outcomes rather than on good or bad professional advice, because clients cannot judge the quality of technical legal advice. The second is that a bad outcome is worse for the lawyers' reputation when they choose innovative, non-standard terms than when they choose a standard term.[98]

In the case of dual-class structures, however, the "norm" concerns substantive features, such as the degree and duration of voting inequality, rather than legal terms. Agency theories of contractual standardization typically deal with technical provisions drafted by lawyers, which are not easily understood and assessed by the clients,[99] or with boilerplate Here, by contrast, founders, VCs, company directors, and institutional investors can easily observe the level of voting inequality chosen in the IPO charter and decide whether it accords with their preferences. Yet, as discussed in Part II, whereas there is significant variation in the way charters combine different legal terms (Part II.A), such variation mostly disappears when we consider the aggregate substantive effect of these provisions on the degree and duration of voting inequality (Parts II.B and II.C).

C. An Alternative Conjecture: Dual-Class Practice as Market Norms

Given the limits of classic and modern contractarian theories in explaining the real-world dynamics of dual-class contracting, we need a richer story. In the following pages, I will sketch a conjecture that draws from different literatures on social norms (by sociologists, economists, and legal scholars). Briefly stated, the conjecture is as follows. In dual-class contracting, "market norms" play an important role alongside individualized

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conjectural—would imply that dual-class norms depart from standard assumptions of economic rationality and do not properly belong to the set of "contractarian theories," classic or modern.

97. *Id.* at 355–58.

98. Agency problems and behavioral inertia have been proposed as plausible explanations of standardization and slow evolution also in the literature on commercial contracts and indentures. Stephen J. Choi & G. Mitu Gulati, *Innovation in Boilerplate Contracts: An Empirical Examination of Sovereign Bonds*, 53 EMORY L.J. 929 (2004); MITU GULATI & ROBERT E. SCOTT, THE THREE AND A HALF MINUTE TRANSACTION (2012); Barak Richman, *Contracts Meet Henry Ford*, 40 HOFSTRA L. REV. 77 (2011); Stephen J. Choi, Mitu Gulati & Eric A. Posner, *The Evolution of Contractual Terms in Sovereign Bonds*, 4 J. LEGAL ANALYSIS 131 (2012); Stephen J. Choi, Mitu Gulati & Robert E. Scott, *The Black Hole Problem in Commercial Boilerplate*, 67 DUKE L.J. 1 (2017); Robert Anderson & Jeffrey Manns, *The Inefficient Evolution of Merger Agreements*, 85 GEO. WASH. L. REV. 57, 57 (2017); Stephen J. Choi, Mitu Gulati & Robert E. Scott, *Variation in Boilerplate: Rational Design or Random Mutation?*, 20 AM. L. & ECON. REV. 1 (2018); Claire Hill, *Repetition, Ritual and Reputation: How do Market Participants Deal With (Some Kinds of) Incomplete Information*, 2020 WIS. L. REV. 151; Scott, Choi, & Gulati, *supra* note 86; Nyarko, *supra* note 86; Matthew Jennejohn, Julian Nyarko & Eric Talley, *Contractual Evolution*, 89 U. CHI. L. REV. 901 (2022).

99. A seminal study on how lawyers influence IPO charters is John C. Coates, IV, *Explaining Variation in Takeover Defenses: Blame the Lawyers*, 89 CALIF. L. REV. 1301 (2001), which Professor Coates found that law firms with transactional or litigation experience in mergers and acquisitions had a preference for takeover defenses, and IPO charters drafted by these law firms were more likely to include such defenses, even if they are considered value-decreasing. Coates argues that this agency problem between lawyers and issuers is possible because "[l]egal advice often… is a "credence good," for which quality may never fully known." *Id*. at 1309–11.

contracting. Indeed, the market practice in dual-class IPOs possesses certain essential characteristics of social norms: compression (i.e., low variation), stickiness (i.e., persistence over time), and the so-called punctuated equilibrium (i.e., long period of stasis followed by rapid change). Furthermore, the key insiders surveyed and interviewed for this Article seem to treat dual-class market practice as norms—standards that one ought to comply with even if their price-maximization rationale is unclear. Finally, the emergence of these norms resembles random mutation rather than rational design, with some important innovations appearing to have been spurred by the deliberate actions of individuals and organizations, akin to the role of "norm entrepreneurs" in changing social norms.

A theory of dual-class market practice as "market norms" accepts the possibility that dual-class structures may be bad for investors (contrary to the classic contractarian theory and the learning externalities theory) but does not blame the lawyers' self-interest (as in the agency theory) for this phenomenon. Instead, it places the focus on the thick interplay between economic optimization and relational norms within certain business and professional communities and the lawyers' traditional role as transmitters of norms within startup communities.[100] By viewing dual-class contracting through the lens of market norms, we can better understand how certain practices become entrenched, how they evolve, and why they may resist change despite apparent inefficiencies. In the following subparts, I will try to outline some essential elements of this hypothesis.

1. Market Norms in Dual-Class Contracting

The decision of most dual-class companies to follow some widespread, standard practices rather than choosing tailor-made structures resembles a well-known phenomenon in social theory: conformity to social norms. In the sense used here, social norms are standard or customary forms of behavior to which individuals in a given group conform.[101] Many social norms are backed by social sanctions, such as the norm concerning politeness with co-workers and neighbors.[102] Other norms are accompanied by internalized normative beliefs,[103] and therefore are often followed even when social sanctions are unlikely, such as

100. *See supra* notes 81–84 and accompanying text.

101. *See, e.g.*, Mary A. Burke & H. Peyton Young, *Social Norms*, *in* HANDBOOK OF SOCIAL ECONOMICS 313 (Benhabib, Bisin & Jackson eds., 2011) (defining social norm as "a standard, customary, or ideal form of behavior to which individuals in a social group try to conform"). There are many different definitions of social norms in the legal and economic literature. For a discussion of some of this definitional disagreement, *see* Richard H. McAdams, *The Origin, Development, and Regulation of Norms*, 96 MICH. L. REV. 338, 350–52 (1997) (focusing on norms as "informal, decentralized obligations"). Many authors distinguish between norms and mere conventions, with only the former being "obligations" (whether because of social sanctions or an internalized sense of duty). Here, I follow Burke & Young in using the term "social norm" in the broadest sense, including social and moral obligations as well as customs and conventions.

102. *See* Cristina Bicchieri, Ryan Muldoon & Alessandro Sontuoso, *Social Norms*, STAN. ENCYC. OF PHIL. ARCHIVE (Sept. 24, 2018), https://plato.stanford.edu/archives/win2018/entries/social-norms/ [https://perma.cc/9Z9F-ZFQ3] ("Group behavior (as opposed to individual behavior) is characterized by features such as a perceived similarity between group-members, cohesiveness, a tendency to cooperate to achieve common goals, shared attitudes or beliefs, and conformity to group norms.").

103. For a discussion of "internalization of norms through habituation," see Richard A. Posner, *Social Norms and the Law: An Economic Approach*, 87 AM. ECON. REV. 365, 366–67 (1997) (exploring the problems "norm internalizations" can create for freedom of choice).

the norm against littering in public spaces.[104] Some social norms are conventions that solve a coordination problem in some arbitrary but convenient way, such as extending the right hand when greeting someone.

Other social norms, however, are mere patterns of behavior that occur regularly and are therefore expected to occur again. Conformity to these norms is considered "normal" by members of a community, but deviation from the norm is not sanctioned, externally or internally. Cristina Bicchieri, a prominent scholar of the emergence and evolution of norms, calls this type of norms "descriptive norms."[105] She defines them as "a pattern of behavior such that individuals prefer to conform to it on condition that they believe that most people in their reference network conform to it."[106]

Dual-class norms could easily fit into this category. Conformity to these norms occurs regularly, although deviations are not infrequent. Conformity is considered normal, non-conformity raises questions and attracts attention. Companies feel some significant pressure to conform, although the reasons for doing so are not easily explained. The quantitative evidence on dual-class charters and the responses from senior lawyers discussed in Parts II and III are closely consistent with this picture. Indeed, dual-class norms seem to possess some of the essential characteristics commonly associated with social norms. Drawing from the work of H. Peyton Young on the evolution of social norms, I will focus on three typical characteristics: (1) compression, (2) stickiness, and (3) punctuated equilibrium.[107]

Compression

Most dual-class companies choose the same level of voting inequality, despite plausible variation in the underlying circumstances. Such a low level of variation is perhaps the most defining feature of social norms. In the presence of a norm, "individual choices tend to exhibit less variation than would otherwise be expected."[108] In other words, whereas each actor's cost-benefit analysis would suggest a broader variety of optimal individual choices, conformity to a norm compresses such variety into a much narrower range. To be sure, we do not know what the baseline level of variation is, and therefore we do not know whether variation of voting inequality is "less… than would otherwise be expected." It is possible, in theory, that the observed level of variation in dual-class contracting is not "compressed" at all. However, the fact that almost two-thirds of dual-class companies choose the same very narrow range of control lock out of a very wide range of possibilities is quite suspicious.

Adding weight to this hypothesis, the 10:1 voting ratio (which is the main determinant of the 9%–10% control lock) is probably the result of a historical accident. From 1926 to the 1980s, the New York Stock Exchange (NYSE) refused to list companies with

104. *See* Burke & Young, *supra* note 101, at 313 (explaining that the norm against littering is "held in place by an internalized sense of proper or moral conduct").

105. CRISTINA BICCHIERI, NORMS IN THE WILD 19 (2016).

106. *Id.*

107. *See generally* H. Peyton Young, *The Evolution of Social Norms*, 7 ANN. REV. ECON. 359 (2015) [hereinafter Young, *Evolution*] (describing the key features of norm dynamics as persistence, tipping, punctuated equilibrium, compression, and local conformity/global diversity); Burke & Young, *supra* note 101 (arguing that in the presence of norms individual behavior tends to be more uniform ("conformity warp"), there is "greater variability between groups than within groups (local conformity/global diversity)," and behavioral patterns have "long periods of inertia punctuated by occasional large changes (punctuated equilibrium)").

108. Young, *Evolution*, *supra* note 107, at 364.

nonvoting stock and accepted the listing of companies with low-vote shares only on a case-by-case basis.[109] The principle, as stated in the NYSE listed standards in 1983, was that under normal circumstances shareholders' voting power should be commensurate to their equity stake.[110] Consequently, dual-class listings on the NYSE were an exception. Starting in the late 1970s, however, other exchanges tried to attract dual-class listings. In 1976, the American Exchange (Amex) changed its listing standards to allow the listing of Wang Laboratories, Inc., which had been rejected by the NYSE precisely because of its unequal voting rights.[111] To accommodate the listing of Wang Laboratories, the new Amex policy allowed dual-class listings but imposed some restrictions on them, including the requirement that the voting ratio could not be greater than 10:1 (corresponding, in the absence of other relevant charter provisions, to a control lock of 9.09%).[112] Since then, the 10:1 voting ratio has become the standard in dual-class companies. Although today no exchange imposes any limits to the degree of voting inequality, most companies still converge on this focal point.

Stickiness

Social norms are sticky. They persist over time despite changes in circumstances.[113] This seems true for corporate voting inequality. As discussed in Part II, the market practice of choosing a 9%–10% control lock has been the prevailing one over the entire 27-year period examined, and we have evidence that it might have been the dominant degree of voting inequality for decades. Even for the duration of voting inequality, which has changed dramatically over time, we can easily identify a pre-2011 period, during which virtually all dual-class structures were lifelong or perpetual structures, and a 2011–22 period during which perpetual structures have progressively disappeared and time-based sunsets have become more and more common.

To be sure, these changes might be driven by specific characteristics of the companies, and to some extent, they probably are. However, the magnitude of both persistence and transformation is hard to explain exclusively by individualized contracting, and the widespread perception among experienced lawyers is that dual-class norms apply generally to all dual-class companies and do not require any tailoring.

Punctuated equilibrium and norm entrepreneurs

The literature on social norms has observed that when change happens, it typically does so with a rapid rather than an incremental transition. In his seminal work on focal points and convergent expectations, Thomas Schelling observed that players' expectations sometimes shift from one focal point to another, suddenly, because of an incident, of mutually perceived signals, or of "tipping"—that is, the crossing of some threshold that ignites "explosively convergent expectations."[114] When this happens, a long period of stasis is

109. *See* Seligman, *supra* note 22, at 689–90 (detailing the NYSE standards on voting rights).

110. *See id.* at 700 n.79 (quoting NYSE Listing Company Manual § 313.00) ("[T]he Exchange is of the view that any allocation of voting power under normal conditions to classes of stock other than common stock should be in reasonable relationship to the equity interests of such classes.").

111. *Id.* at 704.

112. *Id.* at 704 n.90.

113. *See* Young, *Evolution*, *supra* note 107, at 363 ("Norms tend to persist for long periods, and to respond very sluggishly to changes in external conditions that alter the benefits and costs of adhering to the norm.").

114. THOMAS C. SCHELLING, THE STRATEGY OF CONFLICT 90–91 (1960).

followed by a period of rapid change. Some authors, borrowing from evolutionary biology, call this phenomenon a "punctuated equilibrium."[115]

By contrast, there is no reason to expect a punctuated equilibrium in atomistic contracting. When parties make tailor-made contracts, they adapt the terms of the contract to their circumstances and preferences, not to some external focal point; consequently, the main driver of change is the set of specific characteristics of the deal and of the parties, not what other players are doing or expect others to do.

In dual-class contracting, we observe two phenomena that closely resemble punctuated equilibria. Figure 15 shows the explosion of dual-class IPOs in the tech sector, starting in the 2010s. From the late 1990s to the mid-2000s, dual-class IPOs were not very common in the tech sector; in fact, non-tech companies were more likely to choose a dual-class structure than tech companies. Dual-class structures were such an unusual choice for tech companies that when Google chose one in its 2004 IPO, its founders felt the need to explain to the market why they did so:

> While this structure is unusual for technology companies, similar structures are common in the media business and has had a profound importance there. The New York Times Company, the Washington Post Company and Dow Jones, the publisher of The Wall Street Journal, all have similar dual class ownership structures. . . . We understand some investors do not favor dual-class structures. . . . We have considered this point of view carefully, and we and the board have not made our decision lightly. We are convinced that everyone associated with Google—including new investors—will benefit from this structure.[116]

After Google's IPO and until 2010, the trend of tech dual-class IPOs continues to be flat: in this period, tech companies are roughly as likely as non-tech companies to choose a dual-class structure, but dual-class structures are still quite uncommon. Things changed abruptly in the 2010s. An increasing number of tech companies chose dual-class structures to go public, whereas non-tech companies tended to stick to the previous pattern. At the end of the sample period, one-third of tech IPOs are dual class.

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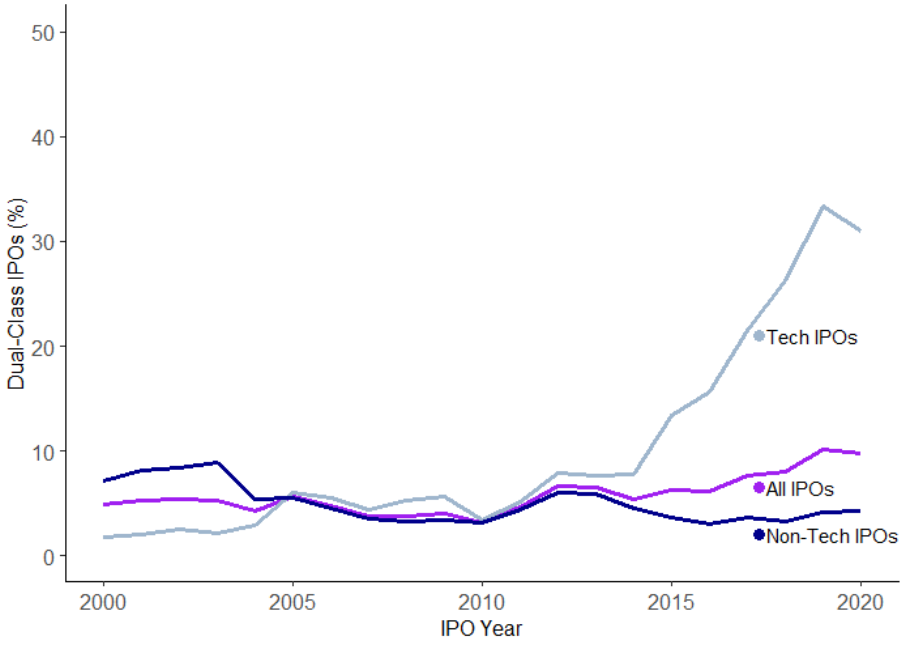
115. *See* Young, *Evolution*, *supra* note 107, at 363–64. For the original use in biology, see generally STEPHEN JAY GOULD, PUNCTUATED EQUILIBRIUM (2007). The concept has been widely used in social theory. *See* Kathleen Thelen, *Institutional Change in Advanced Political Economies*, 47 BRITISH J. INDUS. RELS. 471, 474 (2009) ("In the historical institutionalist literature, one sees this in the language of 'critical junctures' (or choice points) that occur in the past, and the historical trajectories that flow from the legacies they produce. Much of this work emphasizes long stretches of institutional stability, periodically interrupted by episodes of relatively rapid innovation.").

116. Google, IPO Prospectus, *supra* note 21, at 30.

Figure 15. Dual-Class IPOs in the Tech Sector and in Other Sectors



Percentage of IPOs that have a dual-class structure rather than a single-class structure (5-year moving period) for tech companies (gray line), non-tech companies (blue line), and all companies (purple line).

The other phenomenon resembling a punctuated equilibrium is the decline of perpetual structures after a long equilibrium in which perpetual structures were widespread. Figure 6 and the accompanying discussion in Part II.C.2 examine this phenomenon. Also in this case, we observe a long stasis and then a dramatic change, which is exactly what a punctuated equilibrium looks like.

2. Norm Innovators and Norm Transmitters

We can only speculate on what prompted the significant innovations observed in the previous Part. With respect to the rise of dual-class IPOs in the tech sector, Google and Facebook are plausible candidates as "norm innovators."[117] However, the possibility that in those years tech companies changed and this change caused them to choose dual-class structures more frequently cannot be ruled out.

With respect to the decline of perpetual structures, a plausible "norm innovation" story must include the role of Professors Lucian Bebchuk and Kobi Kastiel, who wrote an influential paper highlighting the perils of perpetual dual-class structures,[118] and the Council of Institutional Investors (CII), a prominent association of pension funds and other

117. *See, e.g.*, Fisch & Solomon, *supra* note 9, at 1067 ("Google opened the floodgates, and thereafter, dual-class stock has become a norm for technology companies.").

118. Bebchuk & Kastiel, *supra* note 11.

institutional investors, which conducted an advocacy campaign against lifelong and perpetual structures based on the work of Bebchuk & Kastiel and subsequent research by financial economists. The CII had consistently been opposed to the surge in dual-class IPOs.[119] Around 2017, however, the CII started a more focused campaign against lifelong and perpetual structures. In particular, it compiled a list of dual-class companies, noting those that adopted time-based sunsets, and it started writing letters to many companies preparing their dual-class IPO, criticizing the choice of dual-class structures, suggesting that the charter included at least a "time-based sunset that eliminates the super-voting shares within five years or less,"[120] and commending companies that had already included a time-based sunset in their proposed charter.[121] In 2019, the CII proposed an amendment to the Delaware General Corporation Law, which would provide that "no multi-class voting structure would be valid for more than seven years after an initial public offering (IPO), a shareholder adoption, or an extension approved by the vote of a majority of outstanding shares of each share class, voting separately, on a one-share, one-vote basis."[122] The timing of this campaign tracks quite closely the rise of time-limited structures. The Bebchuk &

119. Among other things, in 2012, the CII petitioned NYSE and NASDAQ for a rule prohibiting the listing of dual-class companies; in 2014, the CII supported several shareholder proposals in favor of voting equality, including proposals submitted to Cablevision Group, Donegal Group, Facebook, and other companies; and in 2017, it strongly opposed Snap's IPO, which adopted an extreme structure by issuing only nonvoting shares to public investors. Letter from Jeff Mahoney, Gen. Couns., Council of Inst. Invs., to Edward S. Knight, Exec. Vice President, NASDAQ OMX Grp. (Oct. 2, 2012), https://www.cii.org/files/issues_and_advocacy/correspondence/2012/10_02_12_cii_letter_to_nasdaq_dual_class_stock.pdf [https://perma.cc/X4ZY-L38E]; Letter from Jeff Mahoney, Gen. Couns., Council of Inst. Invs., to Claudia Crowley, CEO, NYSE Regul. (Oct. 2, 2012), https://www.pii.law.harvard.edu/materials/7a_Dual%20Class_CII-Letter-to-NYSE.pdf [https://perma.cc/JB9L-AJYU]; Letter from Ann Yerger, Exec. Dir., Council of Inst. Invs., to John R. Ryan, Chair, Audit Comm., Cablevision Sys. Corp. (Aug. 12, 2014), https://www.cii.org/files/issues_and_advocacy/correspondence/2014/08_20_14_Cablevision_Systems.pdf [https://perma.cc/EH9Y-6JGP]; Letter from Ann Yerger, Exec. Dir., Council of Inst. Invs., to Donald H. Nikolaus, Chairman & Chief Exec. Officer, Donegal Grp., Inc. (Aug. 12, 2014), https://www.cii.org/files/issues_and_advocacy/correspondence/2014/08_20_14_Donegal_Group.pdf [https://perma.cc/3XCJ-NM6Q]; Letter from Ann Yerger, Exec. Dir., Council of Inst. Invs., to Donald E. Graham, Lead Indep. Dir., Facebook, Inc. (Aug. 12, 2014), https://www.cii.org/files/issues_and_advocacy/correspondence/2014/08_20_14_Facebook.pdf [https://perma.cc/BZW3-PU5W]; Letter from Kenneth A. Bertsch, Exec. Dir., Council of Inst. Invs., to Evan Thomas Spiegel, CEO, Snap Inc., Robert Murphy, Chief Tech. Officer & Dir., Snap Inc., & Michael Lynton, Chairman-Designate, Snap, Inc. (Feb. 3, 2017), https://www.cii.org/files/issues_and_advocacy/correspondence/2017/02_03_17_SNAP_IPO.pdf [https://perma.cc/2YLV-G88N].

120. *See, e.g.*, Letter from Kenneth A. Bertsch, Exec. Dir., Council of Inst. Invs., to Ravi Ahuja, Chair, Nominating & Corp. Governance Comm., Roku, Inc., Ray Rothrock, Member, Nominating & Corp. Governance Comm., Roku, Inc., & Stephan Kay, Senior Vice President, Gen. Couns. & Sec'y, Roku, Inc. 2 (Sept. 12, 2017), https://www.cii.org/files/issues_and_advocacy/correspondence/2017/09_12_17_Letter%20to%20Roku.pdf [https://perma.cc/55AU-JT72] (suggesting this provision after reiterating that "going public with dual class shares in the first place is a poor idea").

121. *See, e.g.*, Letter from Kenneth A. Bertsch, Exec. Dir., Council of Inst. Invs., to Kevin Hartz, Exec. Chairman & Dir., Eventbrite, Inc., Roelof Botha, Lead Indep. Dir., Eventbrite, Inc., & Samantha Harnett, Senior VP & Gen. Couns., Eventbrite, Inc. (Aug. 24, 2018), https://cii.membershipsoftware.org/files/August%2024%20CII%20Letter%20to%20Eventbrite%20on%20Sunset.pdf [https://perma.cc/P99W-648C] ("We therefore applaud Eventbrite for including provisions in its IPO prospectus that provide for a time-based sunset to its dual-class unequal voting structure").

122. Letter from Kenneth A. Bertsch, Exec. Dir., Council of Inst. Invs., & Jeff Mahoney, Gen. Couns., Council of Inst. Invs., to Henry E. Gallagher, Jr, Council Chair, Corp. L. Sec. of the Del. State Bar Ass'n (Sept. 13, 2019), https://www.cii.org/files/issues_and_advocacy/correspondence/2019/September%2013%202019%20Final%20DGCL%20letter.pdf [https://perma.cc/C65B-VA8C].

Kastiel's study appeared in the spring of 2017; between the end of 2017 and 2018, the CII started its vigorous advocacy for time-based sunsets. At that time, time-based sunsets were not rare, but still a small minority. Between 2012 and 2016, time-based structures represented about 27.8% of dual-class IPOs. However, between 2017 and 2022, this percentage increased to 45.7%.[123]

The fact that norm innovation is sometimes spurred by the deliberate action of individual actors is a well-known phenomenon to scholars of social norms. In a 1996 article, Professor Cass Sunstein called these innovators "norm entrepreneurs" and defined them as individuals interested in changing existing norms, who sometimes succeed in creating "norm bandwagons" or "norm cascades"—the phenomenon in which "small shifts lead to large ones."[124] Sunstein referred to fundamental norms in social and political structures, but a similar phenomenon can occur in the much narrower field of corporate governance. The plausible norm cascades discussed here may well have been initiated or at least accelerated by market norm entrepreneurs, such as Google and Facebook (in the first case) and Bebchuk & Kastiel and the CII (in the second case). Other publicly salient episodes, such as the failure of The We Company's IPO in 2019 (its founder Neumann was caught on camera saying that his great-great-grandchildren would control the company)[125] might have contributed to discrediting perpetual structures even more.

Although the "norm innovation" story is suggestive (and, I believe, largely accurate), we cannot rule out the alternative hypothesis, according to which the dual-class companies of the post-2011 period were just different, and time-based sunsets were a better fit for them. Indeed, the unraveling of the "perpetuity" norm largely overlaps with the explosion of dual-class structures in the tech sector. Tech companies came to represent an increasingly larger percentage of dual-class companies. These are companies that, as just discussed, used to choose single-class structures; it is quite possible, therefore, that after Google and Facebook legitimized the use of dual-class structures in the tech sector, a larger number of founders who wanted a dual-class structure could obtain it more easily, but many of them had to settle for a time-limited one. Even in this alternative story, however, norms and norm innovation play a role alongside individualized contracting. Indeed, without norm innovation, dual-class companies would have gone public with a single-class

123. Groupon was the first IPO of the "new era," at the end of 2011. Groupon was the largest U.S. internet IPO since Google, and one of the most anticipated IPOs of 2011. Alistair Barr & Claire Baldwin, *Groupon's IPO Biggest by U.S. Web Company since Google*, REUTERS (Nov. 4, 2011), https://www.reuters.com/article/us-groupon/groupons-ipo-biggest-by-u-s-web-company-since-google-idUSTRE7A352020111104 [https://perma.cc/B6HQ-BNV4]; Shira Ovide, *Five Tech Deals We Want to See in 2011 (and One We Don't)*, WALL ST. J. (Jan. 4, 2011), https://www.wsj.com/articles/BL-DLB-30520 (on file with the *Journal of Corporation Law*). However, most of the subsequent largest IPOs until 2018, including Facebook (2012), Zoetis (2013), Coty (2013), First Data (2015), Altice (2017), and Switch (2017), still had a lifetime or perpetual duration. Aggarwal et al., *supra* note 12, at 125–26. In this period, time-based sunsets seem to be chosen mostly by smaller companies. *Id.* Over time, however, time-based sunsets were increasingly adopted by larger companies. *Id.* Another form of backlash against dual-class structures was the decision by certain index providers to exclude dual-class companies. For a discussion of how indices can affect dual-class governance, see generally Scott Hirst & Kobi Kastiel, *Corporate Governance by Index Exclusion*, 99 B.U. L. REV. 1229 (2019); Andrew Winden & Andrew Baker, *Dual-Class Index Exclusion*, 13 VA. L. & BUS. REV. 101 (2019); Byung Hyun Ahn, Jill E. Fisch, Panos N. Patatoukas & Steven Davidoff Solomon, *Synthetic Governance*, 2021 COLUM. BUS. L. REV. 476.

124. Cass R. Sunstein, *Social Norms and Social Roles*, 96 COLUM. L. REV. 903, 909 (1996).

125. Loizos, *supra* note 81 and accompanying text.

structure, and without the "compression" of dual-class norms and the deliberate action of norm entrepreneurs, time-limited structures would have been more heterogeneous.

During the long period of "equilibrium," however, norms get replicated and transmitted. As discussed in Part III.C.4, this role is primarily undertaken by the issuer lawyers, who play a sociologically crucial role in "identify[ing,], create[ing], transmit[ting], and enforce[ing] the emerging norms of the community."[126] Unlike in the agency cost hypothesis, however, lawyers are not primarily driven by self-interest, but rather by their role as "norm transmitters." These norms play an important function in the startup community (or, at least, the members of the community believe so) and the lawyers consider one of their key roles to educate their clients and to instill these norms in them.[127]

D. The Implications of the Market Norms Conjecture

1. Market Norms Conjecture vs Other Theories

A descriptive norm, in the sense discussed above, is simply the description of a behavioral regularity; therefore, one might conclude that the market norms conjecture is a mere relabeling of the phenomenon identified in Parts II and III, not an explanation of it. But even if our understanding of social norms is limited, some of their well-known patterns and characteristics can help us shed some light on dual-class contracting.

First, unlike the classic contractarian theory and the learning externalities theory, the market norms conjecture accepts the possibility that the prevailing dual-class norms are bad for investors. In the classic contractarian theory, the voting structure chosen by the company in a competitive market maximizes the joint surplus for investors and insiders, and any value-reducing effects of that structure are accurately incorporated into the IPO price. In the learning externalities theory, the voting structure chosen at the IPO may be suboptimal in terms of inherent value, but it is still the most efficient after accounting for cost savings and reduction of legal uncertainty. Therefore, on those two accounts, investors get a fair deal. By contrast, market norms do not necessarily emerge because they are efficient: if the stories proposed in the previous subpart are true, the most important dual-class norms emerged as random mutations, not by rational design, although continuing compliance suggests that these norms must serve the interests of some people, to some extent (plausibly, the founder's); and at least one of these norms was undone by the activism of norm entrepreneurs, not by atomistic contracting. More importantly, on this account dual-class norms do not persist because of significant advantages in terms of drafting or legal interpretation, but simply because they are a powerful and sticky focal point. If they are efficient, it is by sheer luck; under the market norms conjecture, our working hypothesis should be that they are not.

Second, unlike in the agency theory, in the market norms conjecture conformity to dual-class norms is not necessarily driven by self-interested advisors acting at the expense

126. Suchman & Cahill, *supra* note 76.

127. Another, more explicit way in which Silicon Valley lawyers have helped to identify and transmit the market norms of the startup community is through the creation of the National Venture Capital Association Model Legal Documents for venture financial transactions. *See generally* Robert P. Bartlett, *Standardization and Innovation in Venture Capital Contracting: Evidence from Startup Company Charters* (Stanford L. & Econ. Olin Working Paper No. 585, 2023), https://ssrn.com/abstract=4568695.

of their clients. In the agency theory, lawyers push for the standard structure because their reputational payoff is asymmetrical (they receive more blame if failure occurs with a non-standard structure), and they can get away with this because their clients are not able to assess whether the lawyers' advice is good or bad. In the market norms theory, by contrast, lawyers do not push for some technical legal term but for substantive features of dual-class structures: how large is the founder's super-voting power relative to public investors (control lock) and how long can such an unequal voting structure last (duration)? Founders and corporate managers understand these questions as well as (and better than) lawyers. If lawyers favor the standard structure due to asymmetrical reputational payoffs, it is not clear why founders sign off on this strategy.

Nevertheless, the market norms conjecture must not rely on the assumption that market players act irrationally, unlike the behavioral explanations embraced by some critics of contractarianism.[128] By this I mean that market players might very well choose, consciously and deliberately, to comply with the norm even if they process all the available information in an unbiased fashion. Indeed, in the literature on social norms, different hypotheses have been advanced to explain why people rationally decide to comply with norms.

An influential theory, for example, proposed by Professor Eric Posner, focuses on reputational signaling and can be roughly summarized as follows. People value reliable cooperation partners; conformity to norms is costly, whereas deviation is beneficial, at least in the short term; by conforming to social norms, people signal that they value the long-term benefits of cooperation more than the short-term costs of compliance, and therefore are reliable partners.[129]

By applying this framework to dual-class IPOs, we could suggest that founders decide to sacrifice firm value and private benefits in accepting the standard dual-class structure to signal to the other players in the start-up ecosystem (mainly, VCs, other founders, angel investors and other early-stage investors, incubators, accelerators, educational institutions, tech experts, and so forth) that they are reliable cooperation partners. In this case, conformity to norms is not only a rational decision but also a self-interested one. Many founders are serial entrepreneurs or otherwise benefit from long-term relationships with VCs and with other players in the start-up ecosystem.[130] Therefore, they care about their reputation within that community, just like lawyers and investment bankers do. It is possible that, whereas a start-up failure is generally perceived as an inevitable element of the start-up ecosystem, given that most start-ups do indeed fail,[131] a failed start-up IPO coupled with the founder's idiosyncratic nonconformism may harm the founder's reputation much more. This would explain why founders are willing to sacrifice IPO price and private benefits to cultivate good relationships for future entrepreneurial or investment projects. However,

128. For an overview of how cognitive biases may explain charter uniformity, see sources cited *supra* note 94.

129. *See generally* Eric A. Posner, *Symbols, Signals, and Social Norms in Politics and Law*, 27 J. LEG. STUD. 765 (1998); ERIC A. POSNER, LAW AND SOCIAL NORMS (2000).

130. *See generally* Ola Bengtsson, *Relational Venture Capital Financing of Serial Founders*, 22 J. FIN. INTERMEDIATION 308 (2013).

131. *See* Elizabeth Pollman, *Startup Failure*, 73 DUKE L.J. 327, 329–30 (2023) ("Approximately 75 percent of venture-backed startups fail—the number is difficult to measure, however, and by some estimates it is far greater").

even if we do not accept the signaling theory of social norms proposed by Posner and instead subscribe to more "sociological" accounts, conformity to norms may be and often is a deliberate and rational decision, not the result of a cognitive distortion.[132]

2. Market Norms Conjecture and the Policy Debate

To be sure, the market norms conjecture does not claim to be a complete explanation of dual-class contracting: it is very plausible, and I believe accurate, that some or all of the other forces that are central to the standard theories (contractual optimization, learning externalities, agency problems, and even cognitive biases) are at play in dual-class IPOs just like in many other business and social settings. However, if the market norms conjecture is an accurate explanation of an important portion of dual-class contracting, investors could be harmed due to the convergence of market players on some arbitrary focal point.

This recognition, if taken seriously, has potential implications for the policy debate on dual-class companies. In particular, the agenda for this debate, which has been traditionally centered on the *merits* of dual-class structures or specific features, should pay more attention to the *process* leading to the creation and persistence of dual-class norms: How do market players converge on these practices? Why do they follow them? What prompts them to revise them? What kind of revisions are successful and why? Which actors play what roles in the perpetuation of market norms and their evolution? Is there a role for the regulator to facilitate norm innovation and tailor-made customization, and which one? These questions, virtually ignored in the dual-class debate, are indeed of utmost importance if we accept that the market norms conjecture captures some important aspect of dual-class contracting.

Even a preliminary sketch of possible policy suggestions is beyond the scope of this Article. Two general observations, however, are useful. The first concerns the role of the regulator under the market norms conjecture. Although this view casts doubt on the contractarian motto that "one size does not fit all," it does so only in the narrow sense that actual market practice does not seem to live up to the motto, not in the broader sense that a standardized solution is optimal for most firms.

Some observers might be tempted to conclude that, since companies and investors do not seem to design dual-class structures in a customized way, but mechanically follow arbitrary market norms, the policymaker should step in and regulate corporate voting rights in a way that best protects investors and companies, for example by mandating a "one share, one vote" standard. However, there is no reason to believe that the policymaker is better positioned than market actors to design the optimal voting structure for public companies. Even if it were true that most dual-class companies choose sub-optimal voting structures, it does not follow that the policymaker would be able to choose optimal structures in their stead. In fact, the analysis presented here suggests that the traditional question in the policy debate on dual-class companies might be misleading. The key policy question should not be whether and how the policymaker should prohibit or regulate dual-class structures, but rather how the policymaker can facilitate tailor-made contracting and

132. For some perceptive critiques of the signaling theory of norms, see Dan M. Kahan, *Signaling or Reciprocating? A Response to Eric Posner's* Law and Social Norms, 36 U. RICH. L. REV. 367 (2002); Paul G. Mahoney, *Norms and Signals: Some Skeptical Observations*, 36 U. RICH. L. REV. 387 (2002); Lina Eriksson, *Social Norms as Signals*, 45 SOC. THEORY & PRACTICE 579 (2019).

innovation. The data suggest that there might be a deficit of customization in voting arrangements; therefore, one plausible policy goal should be to increase, not decrease the customization of voting arrangements.[133]

The second observation recommends some degree of strategic optimism. The data show that dual-class norms are sticky, but they may and do change, and norm innovation in dual-class structures has indeed proved quite successful. If dual-class conformity is bad for investors, there likely exist relatively low-cost ways to experiment with alternative focal points. In this strategy, the regulator could simply play the role of facilitator of these experiments. For example, it could require more information in IPO prospectuses (collecting and computing information on voting inequality are time-consuming activities); it could organize forums for investors, issuers, and advisors to discuss and revise market practice, including input from academics and policy researchers; it could disseminate information on market practice, including proceedings from these forums; and so forth. If these focal points are largely arbitrary, a more deliberate process can pick many low-hanging fruits.

CONCLUSION

This Article has presented quantitative and qualitative evidence regarding the variation of voting inequality in dual-class companies across nearly three decades. It has documented the persistence and evolution of recurring patterns in dual-class structures and has highlighted that, despite a broad spectrum of potential tailor-made options, most dual-class companies choose similar or identical levels of voting inequality and that innovation in market practice seems to occur by random mutation, rather than progressive optimization, as well because of the deliberate action of "norm entrepreneurs." This analysis challenges the view that dual-class charters are a textbook example of "deliberate contracting" and suggests a rethinking of the standard narrative. Additionally, this Article has highlighted the limits of learning externalities and agency problems in explaining certain peculiarities of dual-class contracting and has outlined an alternative conjecture with potential implications for policymaking and future research.

133. This is not to say, of course, that standardization is per se undesirable. In fact, as discussed in the previous Part, it is very likely that both contractarian optimization and learning externalities are partly the cause of dual-class standardization. To the extent that some degree of standardization is instead due to market norms, and these norms are arbitrary and bad for investors, customization is to be preferred to standardization.