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Superstar CEOs and Corporate Law

Assaf Hamdani & Kobi Kastiel

# From Powerful CEOs to Powerful Shareholders

In this Part, we begin by describing the transition from powerful CEOs to powerful shareholders. We, then, explain how even in era of powerful shareholders, corporate law is far from being dead. Some CEOs remain quite powerful either because investors believe they have star qualities and unique contribution to company value or because of the adoption of control enhancing mechanism, such as dual-class shares that enable them to maintain majority control over time. In both cases, shareholders are limited in their ability to monitor powerful CEOs.

## The Traditional View: Powerful Managers

Corporate law and scholarship distinguish between controlled and widely-held companies.[[1]](#footnote-2) In controlled companies, a single shareholder holds a majority of the voting rights, and therefore has the power to appoint board members.[[2]](#footnote-3) While controlling shareholders are generally insulated from the disciplinary force of the market for corporate control or from interventions by activist shareholders,[[3]](#footnote-4) their large equity stake provides them with powerful incentives to supervise management.[[4]](#footnote-5) Yet, the interests of controlling shareholders are not always aligned with those of other public investors, as controllers may exploit their dominant position and consume private benefits through related party transactions or other ways, at the expense of minority shareholders.[[5]](#footnote-6) Therefore, the principal concern in controlled companies has long been the protection of public investors from expropriation by controlling shareholders.

In widely-held companies, in contrast, share ownership is more dispersed, and no single shareholder can dictate vote outcomes or elect all members of the board. Thus, the CEOs of these companies had the *de facto* power to lead them (at least up until two decades ago), and the concern has been that they will use this power to promote their self-interest at the expense of other investors.[[6]](#footnote-7) Therefore, under the dominant view within corporate law scholarship, an important goal of corporate law in widely-held companies is to address the agency problem that arises from the misalignment of shareholders and management interests.[[7]](#footnote-8)

To be sure, shareholders of widely-held companies have always held the formal power to elect board members, who in turn have the power to appoint CEOs. In theory, therefore, CEOs of widely-held public companies could keep their position only as long as public investors were satisfied with their performance. Yet, these CEOs were considered to be quite powerful.[[8]](#footnote-9)

CEO power was the result of several reasons. *First*, while public shareholders had the formal power to nominate directors, they were quite passive and lacked sufficient incentives to become informed and nominate directors.[[9]](#footnote-10) Electoral challenges were rare, and shareholders often voted for the directors nominated by management.[[10]](#footnote-11) Shareholder passivity was reinforced by legal rules governing director elections. For example, under plurality voting, which used to be the prevailing method for director elections, directors who receive the most votes are elected.[[11]](#footnote-12) This means, in effect, that when the directors nominated by management are the only candidates for election - as is often the case - even directors who did not gain any shareholder support could be elected.[[12]](#footnote-13) Under this regime, being placed on the company’s slate was crucial, and virtually assured the election of the nominated directors.

*Second*, CEOs were often actively involved in board appointments, including those of independent directors. In many cases, CEOs chaired the board and played an important role in putting together the list of directors nominated by the company.[[13]](#footnote-14) Thus, it was quite difficult to get elected to the board if the CEO objected the nomination of a potential candidate.[[14]](#footnote-15)

*Third*, historically Delaware courts adopted a permissive approach to the use of structural defenses, such as poison pill, that insulated CEOs from the threat of hostile takeover attempts.[[15]](#footnote-16) Many public companies took advantage of such permissive approach by adopting antitakeover charter provisions as well as using a poison pill together with a staggered board—a combination that has proven to be a serious impediment to a hostile takeover.[[16]](#footnote-17)

Thus, the prevailing view among policymakers and academics (at least up until two decades ago) was that limiting CEO power is vital for constraining managerial agency costs. And the main prescription for addressing this problem was to make corporate boards more accountable to shareholders and less dependent on the CEO.[[17]](#footnote-18)

## The Rise of Powerful Shareholders

Today, a combination of governance, legal, and market changes have made shareholders significantly more powerful.[[18]](#footnote-19) Some of these changes are a direct result of federal intervention or changes to corporate law; others are the result of shareholder demands or market developments.[[19]](#footnote-20) But at the end of the day, the cumulative effect of these changes has been a persistent trend toward shareholder empowerment.[[20]](#footnote-21)

The *first* significant change is the push towards board independence. In the past three decades, market and legal changes resulted in an overwhelming decrease in insiders presence in the boardroom.[[21]](#footnote-22) Such movement, which was initially driven by market demand, has accelerated with the passage of mandatory legislation, such as the Sarbanes-Oxley Act (SOX),[[22]](#footnote-23) and with stock exchanges demanding to increase board independence.[[23]](#footnote-24) The main rationale for those reforms was that "non-insiders" are better suited to monitor managerial behavior and protect shareholders' interests.[[24]](#footnote-25) The result of these changes, as Jeff Gordon showed in a well-known article, was that the nominal independence of board members has increased dramatically in the last half century, from 20% in 1950 to around 80% in 2005, with the CEO often being the sole insider in the boardroom.[[25]](#footnote-26) And as recent research by one of us affirmed, this trend towards board independence continues.[[26]](#footnote-27)

The *second* significant change is the empowerment of shareholders to elect directors through de-classifying the boards of America's largest corporations and the constant move towards majority voting for director election. When a board is classified, each class of directors faces election every two or three years.[[27]](#footnote-28) This deters hostile takeovers because a potential acquirer cannot simply replace an entire board at once.[[28]](#footnote-29) When combined with a poison pill, this protection becomes extremely effective, forcing a potential acquirer to conduct a successful proxy contest at the company’s annual shareholder meeting for two consecutive years before it can take over the board and revoke the pill.[[29]](#footnote-30) In fact, there has never been a hostile acquisition of a firm with an effective staggered board where the firm kept its pill in place.[[30]](#footnote-31)

 While the academic debate on the merits of classified boards is still alive and kicking,[[31]](#footnote-32) shareholders have already made up their minds.[[32]](#footnote-33) As a result of their pressures,[[33]](#footnote-34) the effort for de-staggering corporate America has shown remarkable success, resulting in a decrease from 60% of S&P 500 firms with classified boards in 2000 to only 10% twenty years later.[[34]](#footnote-35) Moreover, while boards are free under Delaware law to adopt a poison pill, directors are hesitant to do so, fearing that proxy advisors will recommend, and institutional investors will vote, against their nomination to the board as a result of a unilateral adoption of a pill.[[35]](#footnote-36)

Another change towards increasing shareholder power is the rise of majority voting for director elections. As we noted earlier, under the traditional plurality voting standard, the elected directors do not have to earn the support of the majority of shareholders. In uncontested elections (which is the most frequent type of election), as long as there is a vacancy on the board, directors can be elected with minimal support (e.g., even a single vote).[[36]](#footnote-37) In contrast, under majority voting, a director is elected to the board only if she obtains a majority of votes.[[37]](#footnote-38) Shareholder campaigns on this subject had a tremendous impact, resulting today with the majority rule being the common voting standard in large companies.[[38]](#footnote-39)

With board de-classification and the shift towards majority voting rules, directors' elections are held more frequently, and directors' risk of losing their jobs becomes concrete (especially in large public companies).[[39]](#footnote-40) This, of course, profoundly influences directors' sense of accountability to shareholders.

Perhaps the most important change in this context is the growing power large institutional investors and the rise of activist hedge funds. Institutional investors today collectively own the majority of the shares of U.S. public companies.[[40]](#footnote-41) Moreover, these holdings are increasingly concentrated in a few large asset managers.[[41]](#footnote-42) As a result of their increased stake and ownership concentration, institutional investors have become powerful players with a dominant impact on vote outcomes of most public companies.[[42]](#footnote-43) In recent years, these investors have been willing to use their power to engage more often with portfolio companies; to monitor executive compensation more closely and vote against it when such compensation is excessive in their view; to support precatory shareholder proposals that empower shareholders; and to withhold vote against directors that systematically ignore shareholder demands or precatory proposals that receive large support.[[43]](#footnote-44) Recently, they also show increased interest in using their votes to advance social causes, such as climate change[[44]](#footnote-45) and board ethnic and gender diversity.[[45]](#footnote-46)

The rise in institutional holdings has also generated demand for voting advice by proxy advisors. As Kahan and Rock explain, proxy advisors function as "central coordinating and information agents." As such, "they help create a unified front of institutional investors, and thereby increase collective institutional shareholder influence."[[46]](#footnote-47) Proxy advisors can also facilitate activist campaigns or the adoption of governance practices that the majority of investors support by posing a credible threat of withholding campaigns against directors and boards that do not respond to shareholder-passed proposals.[[47]](#footnote-48) In this environment, one should not be surprised that corporate executives often ask to have direct meetings with proxy advisors to deliberate on management initiatives, as if they are shareholders themselves.[[48]](#footnote-49)

Perhaps most important, the rise in institutional investor ownership has facilitated the rise of activist hedge funds.[[49]](#footnote-50) These investors often take a significant equity position in target companies and use various tools, from direct communication with the management to proxy fights, to bring about change in the target companies’ business strategy or governance arrangements.[[50]](#footnote-51) Successful activist campaigns are often supported by institutional investors.[[51]](#footnote-52) The emergence of activist hedge funds, who “have shaken up boardrooms" and often force radical changes at many publicly-traded firms, is considered as a groundbreaking shift in the corporate governance of public firms.[[52]](#footnote-53) In many cases, these investors manage to appoint directors and lead to the departure of CEOs whose performance is deemed by the market as unsatisfactory.[[53]](#footnote-54)

The combined effect of the changes described above is a persistent trend of empowering shareholders and weakening CEOs' power over corporate strategy and governance.[[54]](#footnote-55) One of the primary outcomes of the shareholder empowerment trend is the shortening of CEOs' tenure. Steven Kaplan and Bernadette Minton provide evidence that CEOs' tenure in large U.S. companies between 1998-2005 was shorter than tenure length in the 1970s to the 1990s.[[55]](#footnote-56) Marcel Kahan and Ed Rock showed that in a significant portion of S&P 500 companies between 2000-2007, the tenure of outside directors precedes the CEO.[[56]](#footnote-57) This finding still holds today.[[57]](#footnote-58) Marcel Kahan and Ed Rock understand this finding as proof of outside directors acting independently and not being obligated to the current CEO. The decreasing commitment to the CEO is also translated to a greater willingness by board members to meet directly with shareholders. This willingness, in turn, helps institutional and activist investors achieve their goals more effectively.[[58]](#footnote-59)

To summarize, the persistent trend of shareholder empowerment and the rise of activist hedge funds mean that CEOs of widely held companies are much less powerful today than they used to be two decades ago. CEOs lost their formal influence over director nomination and contested elections are more prevalent. We do not argue that managerial agency costs have become extinct. It is fair to say, however, that underperforming CEOs face a realistic risk of removal by disgruntled investors.

## Powerful Shareholders: Is Corporate Law Dead?

The dramatic rise of shareholders power has triggered two types of responses. The first response argues that corporate law has lost its importance. The second response links the rise in shareholder power to the increasing use of dual-class shares that insulate company insiders from shareholder pressures.

As explained above, for many years, the dominant view within corporate law scholarship has been that corporate law’s principal objective for widely-held companies is containing the power of managers in order to protect public shareholders.[[59]](#footnote-60) However, in a market environment in which shareholders are sufficiently sophisticated, powerful and active, there is less need for legal intervention to protect their rights.

Edward Rock, for example, has claimed elsewhere that “since the early 1980s, the U.S. system has shifted from a manager-centric system to a shareholder-centric system.”[[60]](#footnote-61) More recently, Zohar Goshen and Sharon Hannes argued that the “transformation of American equity markets from retail to institutional ownership has relocated control over corporations from courts to markets and has led to the death of corporate law.”[[61]](#footnote-62) They use this theory to explain Delaware’s recent limits on judicial intervention. Under this view, with powerful shareholders, there is less need for judicial review of managerial conduct.

The second response to the rise in shareholder power claims that the balance has tilted too far in favor of powerful shareholders, who push corporate leaders to favor short-term gains over long-term value creation.[[62]](#footnote-63) Critics link the risk of shareholder power to an important, recent market development—the rise in dual-class initial public offerings (IPOs), which has shifted, once again, the balance of power towards founder-CEOs. Recent data shows that almost 30 percent of IPOs in 2017-2019 had dual-class structures.[[63]](#footnote-64) These structures are especially prevalent among high tech companies, with 43.2% of the tech IPOs in 2021 adopting them.[[64]](#footnote-65)

Dual-class structures enable company founders to have a lock on control (that is, the ownership of more than 50% of the voting power or a majority control of the board) with only a small (or even extremely small) fraction of the company’s equity capital.[[65]](#footnote-66) The desirability of dual-class structures has long been the subject of a heated debate, with some scholars and practitioners expressing concerns about the perils of entrenching company insiders for indefinite period of time.[[66]](#footnote-67) Others, however, emphasize that dual-class structures enable founders to execute their vision even when shareholders disagree with their strategy.[[67]](#footnote-68)

Interestingly, supporters of dual-class shares often hold the view that insulating managers from shareholder pressure is essential for allowing companies to develop long-term projects.[[68]](#footnote-69) They further argue that, in a market environment characterized by powerful shareholders who can unseat CEOs, founders increasingly insist on a dual-class structure to restore their power and implement their long-term strategy for the company.[[69]](#footnote-70)

Recent examples, however, question this view. Even in the era of active and strong shareholders, some CEOs remain quite powerful for long periods, even without dual-class shares. As the examples of Amazon, Netflix, J.P. Morgan, Tesla and other companies listed in *Table 1* demonstrate, CEOs can stay at the helm for long periods of time, although they hold a minority, and sometime even a tiny minority, fraction of the company’s equity interest and voting power. Moreover, some of these companies are newcomers that invested heavily in their long-term plans with the support of their shareholders without the protection of dual class shares. Therefore, even in the era of strong and activist shareholders, some CEOs may become quite powerful simply because they have—or investors believe they have—unique contribution to company value. We will elaborate on this point in the next Part.

Table 1. Prominent Examples of Former and Current Powerful CEOs[[70]](#footnote-71)

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| *Company* | *CEO* | *Founder* | *Chair-CEO* | *Ownership (%)*  | *Tenure* |
| Amazon | Jeffery Bezos | Yes | Yes | 15 | 27 |
| Apple | Steve Jobs | Yes | No | 0.6 | 14 |
| Fedex | Fred Smith | Yes | Yes | 7.5 | 50 |
| Hess | John Hess | Yes | Yes | 10.5 | 43 |
| Netflix | Reed Hastings | Yes | Yes | 1.2 | 24 |
| J.P. Morgan Chase | James Dimon | No | Yes | 0.3 | 17 |
| Microsoft | Bill Gates | Yes | Yes | 12.3 | 25 |
| Oracle | Larry Ellison | Yes | Yes | 25 | 37 |
| Saleforce.com | Marc Benioff | Yes | Yes | 3.4 | 22 |
| Tesla | Elon Musk | Yes | No | 18.3 | 17 |
|  |  |  |  |  |  |

Moreover, notwithstanding the rise of shareholder power, courts remain occupied with the challenge of protecting investors from powerful managers or controllers. In the case of Tesla, the Delaware court viewed Elon Musk, the visionary founder of the company who holds only 17% of the company's voting power as exercising effective control, although his holding is well below the 50% threshold necessary for having a lock on control.[[71]](#footnote-72) In fact, the top five investors of Tesla hold together the same percentage of shares.[[72]](#footnote-73)

Putting things together, even in era of powerful and activist shareholders, corporate law is far from being dead, as some CEOs remain quite powerful. Moreover, as we show in this Section, CEOs can be powerful even without the adoption of control enhancing mechanism, such as dual-class shares.

# Superstar CEOs

Our core claim is that some CEOs—we call them "Superstar CEOs"—remain powerful even when shareholders are powerful and boards are accountable to shareholders. The power of these CEOs stems not from their formal control over director elections, but from the *market belief* in their unique contribution to company value through their vision or their other exceptional abilities as CEOs. In this Part, we outline the features that make a CEO uniquely valuable and explore the implications of these features for corporate governance. We begin by focusing on the perception that the CEO is uniquely valuable (Section A). We, then, consider other features that often—but not always—bolster the power of superstar CEOs, and in particular founder status and a significant equity stake (Section B). Finally, we analyze the implications of superstar CEOs for corporate governance (Section C).

## Unique Contribution to Company Value

*1. Star Qualities*

It is worth noting at the outset that there is no precise definition of a "Superstar CEO." At some level, all CEOs are expected to be talented leaders with some positive effect on the value of their companies,[[73]](#footnote-74) and it could be difficult to draw a clear distinction between a CEO who simply does a good job, and a "superstar" or visionary CEO. Yet, within our framework, "Superstar CEOs" are CEOs who are perceived as *uniquely valuable* to the success of their companies. More important for our analysis, these are individuals that directors, investors and markets *perceive* them as a having a unique contribution to company value, so that replacing them would reduce the value of the company.

A Superstar CEO can be critical to the company’s success for various reasons. For example, CEOs may have the vision that allows them to set the company’s strategy in a way that would make it outperform its competitors. A CEO may possess exceptional skills to execute the company’s strategy. There is no one formula. And the precise reasons that make certain individuals uniquely valuable are not important for our analysis. For our purposes, what matters is that the market believes that the CEO is indeed a superstar, and that without the continuing leadership of this CEO, the value of the company is likely to decrease in a significant way.

The business and finance literature as well as the media have long identified the ‘star’ CEO phenomenon. The legal literature, in contrast, has largely overlooked the fact that some CEOs are perceived as essential for the company’s success.[[74]](#footnote-75) Before we discuss the finance literature, we would like to provide some illustrative recent examples.

*2. Examples*

The Superstar CEO phenomenon is not new. Yet, our era of fast technological changes and the rise of "winner takes it all market" provide many well-known examples of Superstar CEOs. Due to space limitation, we will focus on three highly influential CEOs -- Elon Musk of Tesla, Reed Hastings of Netflix and Jeff Bezos of Amazon. This discussion will demonstrate that the market belief that these individuals are uniquely valuable allows them to exercise significant influence over their companies with limited voting rights.

*Tesla*. Another prominent example is that of Teslaand its founder Elon Musk. Under his leadership, Tesla share price increased by 2,600% since its IPO, five years ago, making Tesla the world’s most valuable auto maker.[[75]](#footnote-76) The Forbes magazine recently elected Elon Musk as the most successful business mind of today (together with Jeff Bezos), indicating that he "works to revolutionize transportation both on Earth and in space."[[76]](#footnote-77) Musk is often viewed as the "face of Tesla."[[77]](#footnote-78) The CEO of Panasonic  recently suggested he is "a genius who defies common sense."[[78]](#footnote-79) And as another prominent expert in the auto industry defines it: “Elon is Tesla, Tesla is Elon.”[[79]](#footnote-80)

 Indeed, the notion that Musk has a unique contribution to Tesla was one of the reasons for the Delaware court decision that Musk was a controlling shareholder of Tesla in connection with the derivative lawsuit over the acquisition of SolarCity.[[80]](#footnote-81) In that case, the court found that when Musk insistently brought the proposed acquisition to the board for consideration, the board was "well aware of Musk's singularly important role in sustaining Tesla in hard times and providing the vision for the Company's success." His master plans, the court explained, "provide the architecture by which the Company has been and will be operated".[[81]](#footnote-82) And as the company itself acknowledged in its public filings, Tesla is "highly dependent" on the services of Elon Musk, and if it were to lose his services, it "could negatively impact the company business, prospects, as well as cause its stock price to decline.”[[82]](#footnote-83)

This dependence on Musk might be the reason why the board and investors did not oust Musk after he had smoke marijuana on a live web-show,[[83]](#footnote-84) and cost the company $20 million dollars in a fine imposed by the SEC for his use of Twitter. In August 2018, Musk posted a tweet saying that Tesla would be taken public with shares priced at $420 and that he had secured funding (though the funding had not been secured at the point). The SEC claimed that the tweet had no factual basis, but eventually Musk and Tesla settled with the SEC, agreeing to pay a fine of $20 million each.[[84]](#footnote-85) Musk’s unique contribution might also explain why the SEC did not suspend him for misleading investors. He was forced to step down as the company's chairman and to add additional independent directors to the board, but most importantly for our purpose, he remained the company CEO.[[85]](#footnote-86)

*Netflix*. In 1997, Reed Hastings co-founded Netflix, the first online DVD-rental store.[[86]](#footnote-87) In 1999, he took over the CEO position, demoting his co-founder and partner at the time, Marc Randolph.[[87]](#footnote-88) Hastings also served as Netflix's chairman of the board since its inception. Under his leadership, Netflix became the largest entertainment-media company by market capitalization, with over 195 million subscribers worldwide.[[88]](#footnote-89) Netflix success is not trivial. The company had to change its core business model over the years and adapt to its consumers desires (including the transition Netflix made in its core business from DVD rental to streaming service).[[89]](#footnote-90)

Netflix success is attributed to its unique culture, which encourages competitiveness, critical thinking, invention and transparency.[[90]](#footnote-91) Reed Hastings is the public face of this culture, which he named "No Rules Rules".[[91]](#footnote-92) A PowerPoint presentation outlining Hastings' radical management philosophy has been viewed over 20 million times since he posted it online. Sheryl Sandberg, the chief operating officer of Facebook, described it as "the most important document ever to emerge from Silicon Valley".[[92]](#footnote-93) Hastings' book about is management philosophy is a best seller in the Unites States and abroad, and he is considered to be a great storyteller, presenting even his worst mistakes as breakthrough moments.[[93]](#footnote-94)

Interestingly, Hastings holds only an extremely tiny fraction of Netflix's voting rights, which amount to 1.2%. Without an effective lock on control, Hastings could be subject to shareholder pressures and even be ousted at any given minute. In the past decade, shareholders expressed significant concerns about Netflix corporate governance structure, and a majority of them even supported at some point a precatory proposal to split the CEO and Chairman roles.[[94]](#footnote-95) Yet, the dependence on Hastings and his ability to turn Netflix into a huge success story explains why the vast majority of the company shareholders kept voting in favor of his election to the board on three different occasions in the past three years.[[95]](#footnote-96) It also explains why shareholders did not try to vote him out of office despite the fact that Netflix has systematically ignored shareholder demands and proposals that receive large support.[[96]](#footnote-97)

*Amazon*. Jeff Bezos, who founded Amazon in his garage in Seattle in 1994 served as the company CEO for 27 years.[[97]](#footnote-98) He is credited with having the strategic vision that led the company to its phenomenal success, transitioning it from a modest online bookseller into one of the world's most powerful corporations.[[98]](#footnote-99) Under his leadership, Amazon share price increased by 198,989%(!) since its IPO in 1997, making Amazon the fifth largest company by market cap as of the end of 2021.[[99]](#footnote-100) The media viewed Bezos as unique leader: he was described as having a “magic touch,” or as a “once in a generation type CEO".[[100]](#footnote-101)

Not surprisingly, investors also believed that Bezos was essential for the company’s meteoric growth,[[101]](#footnote-102) and he was praised for his ability to make big and important decisions without offering his shareholders any financial or strategic rational.[[102]](#footnote-103) Jeff Bezos holds 15% of the company voting power,[[103]](#footnote-104) but as one commentator noted, "his influence would be the same if he had 51 percent shares outstanding or 1 percent."[[104]](#footnote-105) And while recently Bezos handed over the CEO role to Andy Jassy, he still retains a key role, as Executive Chair of the company, and will remain engaged in important Amazon initiatives and focus his attention on new products.[[105]](#footnote-106)

*3. Empirical Evidence*

The business and financial literature has developed a rich body of research that examines the contribution of individual business leaders to the company value. Due to the inevitable difficulty of defining Superstar CEOs, this literature has relied on external, measurable proxies to identify CEOs that are uniquely valuable to their companies. One prominent proxy, through which the CEO is often elevated to superstar status, is the receipt of business awards from a prestigious national magazine or newspaper.[[106]](#footnote-107) Earlier studies also looked at other factors that could make a CEO more powerful or dominant, such as being the company founder, the size of the CEO equity ownership, the number of titles the CEO receives (such as serving as chairman of the board and the president), and whether the CEO is the only insider on the board.[[107]](#footnote-108) These factors do not, by themselves, define star qualities, but they can be highly correlated with it.

The startup literature highlights the importance of the quality of entrepreneurs as a major factor that ultimately determines the investment decisions of venture capital firms ("VC firms") in startups.[[108]](#footnote-109) These findings are particularly applicable to experienced entrepreneurs, who often receive higher valuations because of reduced risk of operating failure from the point of view of the VC.[[109]](#footnote-110)

Other studies focus on larger, public companies. These studies empirically document the impact of individual CEO on firm value and try to identify the characteristics of individual CEOs that make them uniquely valuable to their companies.[[110]](#footnote-111) A long line of research, for example, shows that CEOs who founded the company tend to increase firm value or its operating performance, and their firms enjoy higher valuation when compared to professional CEO firms.[[111]](#footnote-112) Additional studies showed that family ownership increases firm value only if founders serve as CEOs or as the chair,[[112]](#footnote-113) and that founder premium is prevalent in the early stage of the company life cycle, and then disappears as the firm grows up and develops.[[113]](#footnote-114)

Another line of studies establish the link between individual CEOs and firm value by showing how the sudden departure of certain CEOs or founders is painful to their organization.[[114]](#footnote-115) In particular, these studies document significant decrease in firm value when CEOs suddenly die or experience other unexpected event (such as hospitalization). This effect is especially large for powerful or young CEOs, in growing and family-controlled firms, or in human-capital-intensive industries.[[115]](#footnote-116) In contrast, sudden deaths of older, long-tenured and entrenched CEOs are, on average, associated with large value gains to shareholders.[[116]](#footnote-117)

Other studies try to identify the channels through which individual CEOs may affect firm value, by focusing on the link between certain CEO characteristics or managerial ‘style’ and firm performance.[[117]](#footnote-118) Studies also suggest how founders can have a significant effect on their firms, through their *distinctive* human capital.[[118]](#footnote-119) Therefore, they emphasize the importance of retaining founder-CEOs,[[119]](#footnote-120) especially for technology-driven acquisitions of young firms.[[120]](#footnote-121) Interestingly, some economists have argued that CEOs might strategically act to make themselves indispensable, by making the firm invest in assets whose value is higher under them than under the best alternative manager.[[121]](#footnote-122)

There is also a line of literature that examine the overall effects (both positive and negative) of superstar CEOs on their firms decision making.[[122]](#footnote-123) In particular, empirical evidence shows that dominant CEOs are prone to take bigger risks and thus could lead the company to either "big wins or big losses";[[123]](#footnote-124) that founder CEOs are more overconfident than professional CEOs and thus they invest more in innovation;[[124]](#footnote-125) and they also tend to pursue market expansion more aggressively than professional CEOs, but they lack the administrative infrastructure that is essential for a growing firm.[[125]](#footnote-126)

On the negative side, empirical evidence shows that the presence of a founding CEO increases the probability of restating earnings and accounting manipulation,[[126]](#footnote-127) as well as the chances of backdating the executive stock options (especially in the high-tech industry).[[127]](#footnote-128) The business press also discusses the problems that arise when companies are too dependent on their charismatic leaders.[[128]](#footnote-129) And management experts discuss the difficulty of filling the position of visionary CEOs.[[129]](#footnote-130)

Taken together, the sources above suggest that certain individuals can make a difference for firm performance and company value. Or at least they demonstrate that markets believe that some CEOs have unique contribution to company value. Striving to better understand this phenomenon and its financial implications, management scholars and financial economists have long studied the emergence of these powerful CEOs and their overall impact on firm value and its decision making.

The legal literature, in contrast, has largely overlooked the phenomenon of superstar CEOs and its governance implications.[[130]](#footnote-131) Yet, the notion that certain corporate leaders might have a unique contribution occasionally plays a role in court decisions.[[131]](#footnote-132) Part of the reason that legal scholars ignore the phenomenon of "Superstar CEOs" stems, in our view, from the fact that this category is quite an elusive one. As we shall see, the difficulty of identifying Superstar CEOs matters for the legal implications that follow in the next Part. Yet, the fact that this category of CEOs is an elusive should not prevent us from examining its legal implications (similarly to what financial economists have long done).

## Founder Status, Equity Stake and Structural Power

In this Section we discuss several additional factors that bolster the power of CEOs, and therefore of Superstar CEOs. These include founder status, large equity stake and additional structural factors, such as long tenure and combined CEO-chair role.

*1. Founder Status and Significant Equity Stake*

Superstar CEOs are often, but not always, founders with a significant equity stake. For example, Elon Musk, the legendary founder of Tesla holds 18% of the company shares;[[132]](#footnote-133) Jeff Bezos the founder of Amazon, holds 11.2% of the company shares;[[133]](#footnote-134) and Larry Ellison the co-founder of Oracle held about 25% of Oracle's shares when he was the CEO of the company.[[134]](#footnote-135)

This is not a coincidence. As reflected from *Table 1*, it is typically the case that Superstar CEOs are founders. Since founders are the ones who have the vision to invent new products and markets or disrupt existing ones, they often become instrumental to their companies.[[135]](#footnote-136) More broadly, data we collected from the GMI dataset shows that in 2018 about 11% of the U.S. public companies without a controlling shareholder have founder or family ownership. While this group of CEOs may, on average, outperform non-founder CEOs,[[136]](#footnote-137) it is unlikely that all of them have superstar qualities. Thus, a founder status is not a prefect approximation for Superstar CEOs.

A significant equity stake is often the outcome of the CEO being the company founder.[[137]](#footnote-138) While founders can get diluted as the company raises more capital, some of them are still able to retain a significant fraction of the company shares after the IPO. And as we further explain in the next Section, a significant minority ownership stake provides Superstar CEOs with additional form of power.

It is important to note that our framework excludes founder-CEOs who retain a majority control after the IPO, usually through the use of dual-class share structure. Mark Zuckerberg, for example, holds about 60% of Facebook’s voting rights, which would clearly make him a controlling shareholder.[[138]](#footnote-139) In the case of founder-controllers it is impossible to disentangle the sources of their power and determine whether they stem from their control over the company voting rights or from their unique contribution to the firm value. Therefore, our analysis focuses on companies where public investors could, at least in theory, outvote the CEO.[[139]](#footnote-140) Indeed, even Larry Ellison, with his significant 25% equity stake, could not exercise a full control over Oracle vote, and in 2015 a majority of the company shareholders voted against the approval of his executive compensation.[[140]](#footnote-141)

It is also important to note that founder status and significant equity stake are not necessary conditions for becoming Superstar CEOs. First, even extremely talented founders can get massively diluted over time. Examples of founders without a significant equity stake include Reed Hasting of Netflix, who holds only 1.2% of the company stake, or Apple under Steve Jobs who held less than 1% of the firm equity capital.[[141]](#footnote-142) Second, markets may lose their faith in founders. Consider Apple’s decision to fire Steve Jobs in the 1980s.[[142]](#footnote-143)

Moreover, not all superstar CEOs are the company founders. There are also talented professional CEOs, who become instrumental to the success of their companies along the years. Jamie Dimon is a prominent example of a non-founder CEO who is perceived as essential for the company’s success. Dimon, the mythological CEO of J.P. Morgan, was featured four times on Time magazine’s list of the world’s 100 most influential people, and he was elected several times as the most admired CEO among peers or the top CEO of the year.[[143]](#footnote-144)

Another example is that of Renault-Nissan alliance under Carlos Ghosn, the Brazilian-born executive, who led the companies for two decades and according to experts, "saved Nissan."[[144]](#footnote-145) Fortune identified him as one of the 10 most powerful people in business outside the U.S,[[145]](#footnote-146) and surveys jointly published by the Financial Times and PricewaterhouseCoopers named him for several consecutive years as one of the most respected business leaders.[[146]](#footnote-147) After that, he quickly achieved celebrity status in Japan and in the business world.[[147]](#footnote-148) Eventually Ghosn was arrested for corruption allegations at the end of 2018. Market reaction in the period that followed this event shows his immense impact, as shares in both Nissan and Renault have sunk by one-third.[[148]](#footnote-149)

A third prominent example of a professional Superstar CEO that is not a company founder, is that of Leslie Moonves who served as the CEO of CBS Corporation for about two decades, until his resignation in September 2018.[[149]](#footnote-150) Under his direction, CBS became a ratings powerhouse, and the network was ranked first in total viewers for 10 consecutive years.[[150]](#footnote-151) Along the way, he became "one of the most powerful men in television,"[[151]](#footnote-152) and has often been one of America highest-paid CEOs.[[152]](#footnote-153)

*2.* *Structural Power*

The financial literature often uses additional factors such as long CEO tenure (relative to the industry average) and concentration of titles, such as combined chair-CEO, as an indication of structural power.[[153]](#footnote-154) According to this view, when the CEO holds additional titles such as the chairman of the board or the president of the company, that CEO has more influence.[[154]](#footnote-155) Indeed, Table 1 reinforces this view, showing that all the Superstar CEOs in our top-10 sample has a median tenure of 25 years, that is significantly longer than the median tenure of all CEOs in the S&P 500, which is about 5 years.[[155]](#footnote-156) Moreover, eight out of our the top-10 Superstar CEOs hold the dual CEO-chair title, and another one (Musk), used to hold it prior to the settlement he reached with the SEC.[[156]](#footnote-157)

We note, however, that according to the traditional view, these structural factors are the source of CEO power. For example, when leadership roles are combined together, they arguably confer much greater power on the CEO.[[157]](#footnote-158) Similarly, CEOs with tenure that is longer than the industry median, should be more powerful vis-à-vis the board, and is more likely to be involved in the nomination of the directors.[[158]](#footnote-159)

In our framework, the causation goes in the opposite direction: the CEO power stems mostly from being instrumental to the success of firm value, and it is the market belief in the star quality of the CEO that enables her to retain the CEO position for a long period of time or to hold a dual role. The case of Satya Nadella, the existing CEO of Microsoft is a clear example of that dynamic. After leading Microsoft successfully in the past seven years, making it more prominent in technology and business altogether, and having its stock risen more than 600%, the company board has decided, unanimously, to make him also the chair of the board, replacing an independent director.[[159]](#footnote-160)

## Superstar CEOs and Corporate Governance

Our analysis sheds new light on the relationship between Superstar CEOs, boards, and shareholders. We explore these implications below. First, we discuss the ways in which the star qualities of some CEOs provide them with power vis-à-vis boards and shareholders, even in our era of powerful shareholders and independent boards. We also consider the implication of having superstar CEOs with a significant equity stake. We, then, discuss the limits of CEO power, which critically depends on investors’ belief that the CEO is vital for the company’s success. Finally, we elaborate our analysis by considering the case of powerful CEOs in private companies, and the increasing use of dual-class shares by powerful CEOs. We conclude by summarizing the governance implications of our analysis.

### CEO Power: Boards

Boards of directors do not run companies. Rather, they appoint CEOs and monitor their performance.[[160]](#footnote-161) As we explained above, during the 2000s and 2010s, governance reforms were based on the premise that, to ensure the effective performance of their monitoring function, boards should become sufficiently independent from management and accountable to shareholders.[[161]](#footnote-162)

But what happens if directors who are fully accountable to shareholders and genuinely committed to the company’s success believe that the CEO is crucial for the company success? In this case, directors might be limited in their ability to effectively monitor the CEO.[[162]](#footnote-163) Moreover, directors might doubt their own judgment and their ability to question the decisions of superstar CEOs. After all, investors (who elect the board members) believe that it is the CEO’s vision and insights that allow the company to become successful. And it is exactly this perception commonly shared by boards, investors and the market that the CEO is crucial for company value that makes the CEO quite powerful vis a vis the board of directors.

Consider, for example, members of the board nominating committee who are required to nominate new members to the board. They consider a candidate who seems very promising. Yet, the CEO strongly disapproves the candidate. Directors might defer to the CEO and not nominate the candidate because they believe that the costs of a confrontation with the CEO—or even the potential for disharmonious working relationship between the CEO and the would-be director--will outweigh the benefits of having the candidate join the board. They could also believe that the CEO knows better what candidates would be best positioned to work with her and improve corporate performance.

The same logic applies to other board decisions: approving a strategic transaction that the CEO proposes; deciding on CEO pay package; or, based on the *Tesla* case,[[163]](#footnote-164) disciplining the CEO for misusing their Tweeter account.

As we further stress below, this CEO power stems not from directors’ agency costs (such them being slack, too beholden to the CEO, or lacking the qualifications to monitor the CEO). Rather, it is directors’ belief that alienating the CEO or questioning his judgment would reduce company value.

### CEO Power: Shareholders

A similar logic applies to shareholders. One of the mechanisms for ensuring that board decisions are beneficial for the company is subjecting them to a vote by shareholders.[[164]](#footnote-165) When a company is led by a Superstar CEO, however, providing shareholders with additional say on corporate affairs might not significantly enhance their ability to discipline the CEO. If shareholders believe that the CEO is crucial to the company's success, then they might defer to her judgment on corporate affairs. Moreover, their threat of removing the CEO lacks bite. From shareholders' perspective, there is no point to throw the baby out with bathwater. The examples of Tesla, Netflix and Oracle nicely illustrate this point.

As we explained in Section **[XX]**, Elon Musk, the leader of Tesla, was involved in a series of scandals in recent years, such as smoking marijuana on a live web-show, or posting a tweet that could be considered a violation of securities law. Moreover, as we explain in the next Part, there are at least two derivative lawsuits pending against Musk, with one of them accusing him of abusing his power to make Tesla acquire SolarCity. But judging by their ballots, Tesla investors seem to be very content with Musk. Indeed, data we collected from the Voting Analytics database shows that Musk was up for election twice since Tesla went public in 2014 (in 2017 and 2020), and in each of these cases his appointment to the board was approved by extremely high margins. Over 97% of the votes cast at these board elections supported his re-election to the board.[[165]](#footnote-166)

Moreover, between 2014 and 2019 Tesla received 12 shareholder proposals that eventually were submitted to a shareholder vote at the company annual meetings. Some of these proposals were on topics that generally receive large shareholder support, such as declassifying boards, the adoption of majority voting and proxy access rights.[[166]](#footnote-167) Yet, none of these proposals received majority support, despite the fact that 8 out of these 12 proposals were also supported by ISS, the largest and most influential proxy advisory firm.[[167]](#footnote-168)

Elon Musk also received the largest stock option package ever granted by a public company. It was valued at $2.6 billion at the date of the award, and the ultimate sum that Musk could realize, was estimated at $55 billion, entitling him the option to acquire 12% of the then outstanding shares of the company.[[168]](#footnote-169) Interestingly, such massive and unprecedented compensation package was approved by 73% of shareholders of Tesla, who are unaffiliated with the company management.[[169]](#footnote-170) Another interesting feature of the plan is that it ensured that Musk would be paid if—and only if—he succeeded in driving very substantial increases in stockholder value. If Tesla’s results fell short of the required milestones—even by a penny—the options contingent on those milestones would not vest, and Musk would be paid nothing. Indeed, only five years after approving the plan, Musk had achieved all but two of the twenty milestones, with Tesla’s market capitalization having grown more than ten times, rivaling that of General Motors.[[170]](#footnote-171)

As the Tesla case clearly illustrates, when a CEO performs extraordinarily well and delivers tens of billions of dollars in actual returns, shareholders are willing to "bite the bullet", open the wallet, and forgive any otherwise unacceptable behavior on his end.

Other high-profile examples show that even when shareholders are dissatisfied with the company’s governance, they do not take measures that they would otherwise take to discipline the board or a powerful CEO. Consider the case of Netflix. In 2013, Netflix shareholders who were dissatisfied with the company's lack of accountability mechanism, submitted a proposal to split the CEO and Chairman roles. New York City Comptroller Scott Stringer, who was one of the proposal’s biggest advocates told the New York Times that “a board that ignores its shareholders is a house of cards.”[[171]](#footnote-172) At the company annual meeting, 73% of the shareholders of Netflix voted in favor of this non-binding proposal, but the board of directors did not take any action, arguing that their current model has been highly effective. The following year, a similar proposal received only 47% of the vote.[[172]](#footnote-173) As one commentator explained, "given that Netflix shares soared nearly 300 percent in 2013… investors weren’t inclined to penalize Hastings after such an accomplishment."[[173]](#footnote-174)

More broadly, data we collected from the ISS database shows that 26 governance-related proposals that were submitted to Netflix between 2013 and 2020 received *majority* support.[[174]](#footnote-175) This seems like a huge win for shareholders. But Netflix, as the data further show, routinely disregards these results. Usually, when companies systematically ignore shareholder concerns, their directors are likely to be subject to withhold campaigns that are embarrassing or that can result in their defeat or resignation.[[175]](#footnote-176) Still, at least in the case of Hasting, he kept receiving in three separate elections that were held in 2014, 2017 and 2020 significantly more support vote than negative votes (and despite the fact that the ISS recommended shareholder to withhold their support from his nomination).[[176]](#footnote-177)

As the head of ESG of a large institutional investor pointed out, the fact that Netflix shareholders remain mostly powerless, is “even more egregious” considering that the company does not have a dual-class stock structure that provides the company founder with a majority control.[[177]](#footnote-178) Under our analysis, however, this outcome is not surprising at all. As long as the market believes in the star qualities of the company’s CEO, shareholders are unlikely to discipline its CEO. The question how long the company and the board may have this freedom to ignore shareholder concerns depend on how well the company does. As another governance expert explained: "shareholders are more likely to overlook bad ESG or corporate governance standards when a company’s stock is outperforming."[[178]](#footnote-179) And Netflix’s stock performance has been way ahead of the Nasdaq for the most recent five-year time period.[[179]](#footnote-180)

Interestingly, while a majority of Netflix shareholders were unwilling to unseat Hastings, they did escalate their action against other outside directors of Netflix. Six of them received less than a majority support in at least one corporate election (mostly in 2019),[[180]](#footnote-181) but since the company has a plurality voting system, they continued to serve on the board and were not forced to resign.

Another interesting example is that of Larry Ellison, the powerful founder of Oracle, who was one of the highest compensated executives in corporate America. In 2012, the company shareholders started to express concerns with regard to his lucrative pay packages. For two years in a row (2012 and 2013), they voted against Ellison's pay package in non-binding say-on-pay votes.[[181]](#footnote-182) Since Ellison held 24-25% of the company's outstanding shares, this means that the overwhelming majority of public investors opposed his compensation package. More interestingly, however, at the *same* annual meetings, the very same shareholders voted in favor of his re-election to the board by wide margin (97% and 95%, respectively).

How can one explain this split in voting patterns? Note that, as the outcome of the votes on pay demonstrate, Ellison *cannot* dictate vote outcome, although he holds a significant fraction of votes. Why do shareholders disapprove Ellison's executive pay package while at the very same time overwhelmingly support his re-election to the board? The most plausible explanation is that shareholders, while perhaps dissatisfied with size of Ellison's generous pay package, prefer not to use their power to ‘rock the boat’, and oust Ellison from the company given the belief in his contribution to the company.[[182]](#footnote-183) Indeed, in the seven following years (2014-2020), Ellison was re-elected to the board by a very large margin in all but one of these cases.[[183]](#footnote-184)

Oracle shareholders, however, did express their disapproval of several independent directors who served on the company compensation committee during the relevant period. For example, in 2013 and 2016 a majority of non-Ellison votes withheld support for these directors due to their failure to address stockholder concerns about executive compensation,[[184]](#footnote-185) and these independent directors were able to continue serving on Oracle board only due to Ellison support.[[185]](#footnote-186) Eventually, Oracle made some changes to its executive long-term equity grants to address some shareholder concerns,[[186]](#footnote-187) but it took the company six proxy seasons to do so, and it was well after Ellison handed over the CEO role. Most interestingly, while public investors escalated their fight against independent directors who served on the compensation committees or on the special committee that approved a high profile related-party transaction with Ellison, they avoid taking similar steps against Ellison.

A recent empirical study provides systemic evidence, that go beyond these three illustrative examples, to support the theory we present in this Article. The study finds that shareholders in aggregate, and mutual funds in particular, are more likely to vote with management (i.e., against shareholder proposals) when the CEO is a superstar (as measured by wining prestigious business awards).[[187]](#footnote-188) In particular, the authors show that shareholder proposals, especially contested ones and those that are supported by ISS, are significantly more likely to fail when the CEO is a superstar. The authors of the study, therefore, conclude that CEOs who benefit from superstar status become more immune to changes in governance policies promoted by shareholders.[[188]](#footnote-189)

Taken together, the illustrative examples and empirical evidence presented in this Section show that when CEOs are perceived as delivering high return to shareholders, the latter tend to tolerate what they would otherwise consider as unacceptable practices. To be clear, this evidence does not suggest that shareholders shall not be eligible to have any "say" on the firm's corporate governance or on executive compensation; rather it shows the limits of solutions that are solely based on shareholder votes in the presence of powerful CEOs.

### Equity Ownership

As we explained in Section [XX], some Superstar CEOs are founders with a significant equity stake. A large equity stake has two major effects on the relationship between superstar CEOs, boards, and shareholders.

*First*, CEOs are more powerful when they have a significant equity stake, and hence considerable influence through their voting. A significant blockholder is more influential in director elections, and in many cases, she can be the pivotal shareholder who determine vote outcomes, so that directors depend on her for reelection.[[189]](#footnote-190) Directors would not want to be in a position where a large shareholder objects to their appointment, even if there is a theoretical possibility that they would be elected against this objection. It is also more difficult to oust a CEO with a significant equity stake. Yet, it is not impossible (as in our framework the control is contestable).[[190]](#footnote-191)

*Second*, a significant equity stake provides CEOs with incentives to enhance firm value. Similarly to the case of a majority controller (although to a lesser extent), a shareholder with a significant equity stakes bears a significant fraction of the costs of her actions and captures a significant fraction of the benefits.[[191]](#footnote-192) This analysis is supported by a significant body of empirical work, which consistently document the positive effect of the rise in insider's ownership rights on the company valuation.[[192]](#footnote-193)

### The Limits of CEO Superstar Power

So far we have shown that even in era of powerful shareholders and independent boards, some CEOs could be quite powerful due to their vison and star qualities, and that such power his further enhanced when a CEO holds a significant equity stake. CEO power, however, is not without limits.

In the past, CEO power was the outcome of their formal influence over board nomination and shareholder passivity. In the present era of active and powerful shareholders, however, CEO power crucially depends on the widespread *perception* that the CEO is *vital* for the company’s success. Therefore, such power is limited both in terms of duration and scope. If the company is under-performing, investors might lose faith in the CEO’s vision or star qualities. This, in turn, might trigger institutional investors’ pressure or make the company a target of an activist attack.

Moreover, the insulation of powerful CEOs from any disciplinary actions by the company board and shareholders is limited to the extent of the CEO’s unique contribution to the company value. Assume, for example, that the CEO is believed to be responsible for generating 5% of the company value. Such powerful CEO will be immune from market pressures as long as her problematic, value-decreasing actions are not expected to cause any harm exceeding 5% of the company value. Once a CEO causes the company damages that exceed 5% of its value, powerful shareholders are more likely to oust her.

This can also take place when the powerful CEO becomes a liability (rather than asset) for other reasons—such as misconduct that significantly undermines the company’s reputation. The case of Papa John's demonstrates this point. John Schnatter started selling pizzas in 1984 in the back of his father’s Indiana Tavern. In 1985, he founded Papa John's, and under his leadership, the company grew into one of the top-selling pizza delivery companies in the United states, with 5,000 stores and $1.7 billion in revenue.[[193]](#footnote-194) In addition to being the CEO and the owner of almost 30% of the company stocks, Schnatter also held an outsized role being the face of the company. He often starred in the company’s commercials and delivered its signature line - “Better ingredients, better pizza.”[[194]](#footnote-195)

But then, in November 2017, he criticized the NFL’s handling of national anthem protests, calling the whole affair a “debacle.” Papa John’s shares crashed by 11% in hours and kept falling, Schnatter lost his CEO title and estimated franchise sales dropped by more than 5%.[[195]](#footnote-196) Still, according to Forbes investigation, little changed in the company day-to-day management, and if anything, Schnatter actually became “more involved than ever” in an attempt to manage the crisis.[[196]](#footnote-197) Then, in July 2018, Forbes learned that Schnatter had used the N-word and made other controversial remarks on a conference call.[[197]](#footnote-198) After the report of the second incident, company shares fell nearly 5%, bringing the stock’s decline to about 30% during a nine-month period.[[198]](#footnote-199) On the day that news broke, Schnatter resigned as chairman,[[199]](#footnote-200) and company share price rebounded, closing 11% higher.[[200]](#footnote-201) Following this event, an independent committee of Papa John's board adopted a poison pill that effectively prevented Schnatter (and his family members or friends) from raising their combined stake to 31%. The pill was aimed to protect the company against a hostile takeover attempt by Schnatter.[[201]](#footnote-202)

Furthermore, as a comprehensive Forbes report shows, Schnatter alleged behavior included not only inappropriate statements, but also other problematic conducts ranging from spying on his workers to sexually inappropriate conduct, which has resulted in at least two confidential settlements.[[202]](#footnote-203) The toxic culture he created turned into a PR and financial disaster for the company: the National Football League terminated its sponsorship deal with the company, the Major League Baseball suspended a joint promotion arrangement, and The New York Yankees cut ties with it.[[203]](#footnote-204) To recover, Papa John's did everything to distance itself from Schnatter. The company removed his image from marketing materials, booted him from subleased office space at the corporate headquarters and asked him not to speak to the media.[[204]](#footnote-205) Schnatter’s example shows that even a powerful founder with a significant equity stake is not immune from being ousted (unlike founder of a company with a dual-class shares). But it happens only in extreme circumstances.

It may also take shareholders some time to react, as in the case of Dov Charney, the powerful founder of American Apparel, who also lost his jobs over sexual harassment and the creation of toxic working environment. Charney, who founded the successful clothing company in 1989, managed to hold onto his CEO title notwithstanding a well-publicized record of sexual harassment allegations (including allegedly masturbating in front of a reporter in 2004 and facing lawsuits for sexual harassment by eight former female employees in 2005 and 2011).[[205]](#footnote-206) It was, however, only in June 2014, that the board ousted him as CEO after an internal investigation revealed that he had allowed an employee to post naked photos on the Internet of a former American Apparel employee who had sued Charney for sexual harassment.[[206]](#footnote-207)

Another prominent examples are those of Carlos Ghosn and Leslie Moonves. Ghosn, the powerful CEO of Nissan and Renault, was ousted from the company after being accused and arrested for corruption allegations at the end of 2018.[[207]](#footnote-208) Moonves, the superstar CEO of CBS Corporation, resigned in September 2018, a few weeks after the New Yorker magazine revealed that six women had accused him of sexual harassment and intimidation, and the company itself faced a lawsuit in federal court in New York for securities fraud.[[208]](#footnote-209)

Taken together, these examples show that there are limits to the power of Superstar CEOs. In particular, when these CEOs are involved in sexual harassment or illegal activities that significantly undermines the company’s reputation. However, as the data we present in Section [XX] shows, when it comes to less egregious actions, such as being inattentive to shareholder governance demands, extracting lucrative executive pay or smoking marijuana on a live web-show, shareholders may show more patient as long as the CEO have exceptional performance.

### Powerful CEOs in Private Companies

Cases of powerful CEOs are not limited to public firms. They can also arise in private companies with powerful and sophisticated investors. In theory, private firms are less likely to suffer agency costs. There is less separation of ownership and control and more stringent oversight of board and management behavior by the firm's shareholders.[[209]](#footnote-210) Moreover, VC investors serve on boards and have a reputation for monitoring founders.[[210]](#footnote-211) However, a close look at two recent case studies reveals that shareholders are not rushing to exercise their power over the superstar CEOs even in private companies with low agency costs.

Our first case study concerns Uber's CEO and co-founder, Travis Kalanick. Under Kalanick's leadership, Uber caught headlines, not necessarily in the way its investors would wish to happen. Uber and its CEO were constantly accused of inappropriate sexual behavior. In 2014, Kalanick made several sexist remarks in an interview[[211]](#footnote-212) and was caught visiting an escort with a group of senior employees in Seoul.[[212]](#footnote-213) In another incident, during a promotion in France, the company collaborated with a French app that sends users photos of women. Due to negative media coverage in the U.S., Uber abandoned the collaboration but did not apologize.[[213]](#footnote-214)

However, Uber's reputation regarding sexual misconduct does not sum up to the incidents above. In 2017, a former Uber engineer exposed that the company systematically failed to address reports on sexual harassment and described a toxic working environment for female employees.[[214]](#footnote-215) Kalanick denied any former knowledge of the allegations.[[215]](#footnote-216) In response, the company hired Eric Holder, former U.S. attorney general, to investigate the claims.[[216]](#footnote-217) The investigation eventually included 215 employee complaints. Four months later, Uber fired more than 20 employees as part of its internal investigation concerning the culture of sexism.[[217]](#footnote-218)

Uber also had its name linked with privacy controversies. The company collected data on users' geolocation and credit card information[[218]](#footnote-219) and used technologies to track down drivers that simultaneously worked for Lyft, its main competitor.[[219]](#footnote-220) Other scandals include a lawsuit by Waymo, Alphabet's self-driving car company, accusing Uber of technology theft,[[220]](#footnote-221) and a 20$ million settlement reached in 2017 after the company admitted it misled drivers as to their expected earnings.[[221]](#footnote-222)

One may rightfully wonder: Where were Uber's major investors? How did they react to the company's ongoing involvement in the mentioned scandals? In 2014, Billy Gurley of Benchmark emphasized his confidence in Kalanick's skills.[[222]](#footnote-223) Another prominent investor, Peter Theil, noted at the same time that Uber was the "most ethically challenged company in Silicon Valley". He thought Uber was on the edge of "going too far".[[223]](#footnote-224)

However, Thiel's concerns did not seem to change Uber's investors' treatment of Kalanick. Only three years later, Uber's investors started questioning Kalanick's abilities to lead the company more seriously. After the sexual harassment scandal exploded in June 2017, Gurley began thinking that the corporate's management needed change. During board meetings, David Bonderman of TPG Capital started having many arguments with Kalanick.[[224]](#footnote-225) Other investors reached Kalanick in an open letter and expressed their disappointment of his failure to change the firm's "toxic atmosphere".[[225]](#footnote-226) Nevertheless, some of Uber's investors still showed faith in Kalanick and thought he should stay in the company, even if he will not remain its CEO. [[226]](#footnote-227) Only in June 2017, long after VC investors became aware of Kalamick in appropriate behavior, he resigned from his role as Uber's CEO.[[227]](#footnote-228)

Another story of a powerful CEO in a private company concerns Adam Neumann of WeWork. Neumann made WeWork notoriously known for its unusual working atmosphere, with summer camps planned by the company, including heavy drinking and the use of marijuana. Neumann himself used to walk around the office in bare feet and installed a pool and a sauna in his office in Manhattan.[[228]](#footnote-229) However, it was not only Neumann's "unique" working routine that made WeWork catch the eyes of the press. Between 2016-2018, former WeWork employees exposed the company's poor treatment of sexual harassment accusations and the toxic environment against women.[[229]](#footnote-230)

Under Neumann's leadership, WeWork was also criticized for its poor corporate governance and financial misbehavior. Neumann used to do business with the company regularly: he owned stakes in buildings leased to the company and repeatedly borrowed money from it. Neumann also had his relatives and friends employed by WeWork and made his wife a key person in the corporation.[[230]](#footnote-231)

Nevertheless, WeWork's board and investors did not seem to hurry and discipline their CEO and demand change. Bruce Dunlevie from Benchmark warned the board that Neumann holds excessive power and control over the company. However, this did not dissuade the board from approving Neumann to recapitalize the company's voting structure in his favor.[[231]](#footnote-232) In particular, JP Morgan and Goldman Sachs seemed to forfeit their monitoring abilities, present Neumann to unrealistic valuations, and did not oppose Neumann taking loans from the company.[[232]](#footnote-233)

The cases of Uber and WeWork provide evidence that the phenomenon of powerful CEOs is not limited to public corporations only. The VCs invested in those companies were familiar with the CEOs' problematic behavior. Still, they abstained from taking actions and did not initiate steps to their dismissal for a significant amount of time. It is an additional evidence of the strength of the phenomenon of powerful CEOs. Even though previous literature identified investors' monitoring abilities in private firms as more efficient and less costly, the cases of Uber and WeWork show that investors will not rush to discipline problematic behavior by CEOs with star qualities. They consider the powerful CEOs' stardom and vision an asset and are reluctant to exercise their power and oversight more closely on CEO conduct.

### Powerful CEOs and Dual Class Shares

Our analysis also has implications for the debate about dual class companies. A prominent justification for the use of dual class structure is that founders need uncontestable control to implement their long-term strategy for the company.[[233]](#footnote-234) Our analysis, however, questions this view. At least some visionary founders can lead companies for the long term without dual-class shares and with contestable control. As long as these founders significantly outperform and the market has faith in the founder star quality, shareholders are unlikely to oust them. In fact, as our examples of Netflix and others demonstrate, shareholders may even allow such founders to maintain pay arrangements and other governance practices that they generally disfavor.

Our analysis offers a more nuanced understanding of the dynamic underlying the dual class structure. To begin, this structure is not essential for allowing founders to focus on the long term. Rather, this structure is needed by founders for times when the market—rightly or wrongly—no longer perceives the founders to be essential for the company success. Indeed, as one of us has explained, dual class structure allows founders to pursue their vision even against investors’ objections.[[234]](#footnote-235) That is, precisely when CEOs lose their star aura, and investors might want to replace the company’s leadership.

But why would investors agree to such a regime at the outset? Why would dual-class IPOs are recently on the rise,[[235]](#footnote-236) despite empirical evidence and analysis (including by one of us) showing that the costs of these structures tend to increase over time? And why would a large fraction of dual-class firms still go public without time-based sunset provisions, which limit their duration, despite the increasing opposition of proxy advisors and large institutional investors to the use of perpetual dual-class shares?[[236]](#footnote-237)

Our analysis shed light on this puzzle by explaining how powerful founders may be able to bargain for more control rights with VCs or public investors.[[237]](#footnote-238) If founders are perceived as crucial for the success of the business at its early stages, then they are likely to use their considerable bargaining power to insist on adopting dual-class shares at the IPO stage. In other words, founders insist on the dual class structure precisely for the period when it is most likely to be less desirable by investors or the market.[[238]](#footnote-239)

The increased bargaining power of talented founders is further enhanced by changes in product markets: technological changes and the rise of "winner takes it all market" increase demand for CEOs that can move fast and disrupt incumbent players in the market or even entire industries.[[239]](#footnote-240) These CEOs, in turn, require more control rights at the IPO stage. Investors give them these control rights not because they believe that founders will always know better than markets how to lead the company, rather it is because these founders are perceived as indispensable at the IPO stage.

### Governance Implications

Our analysis suggests that superstar CEOs can be quite powerful. Yet, the source of this power is not the misalignment of interests between directors and shareholders or shareholder general passivity; nor the formal power that the CEO has in director elections. Rather, the source of CEO power is the market belief that the CEO has the vision or leadership skills that make the company’s success depend on the CEO continued leadership. Our analysis has several implications.

*First*, it shows that the failure of corporate boards to monitor CEOs may not always be the result of agency costs. Thus, it could explain why cases of powerful CEOs arise also in private companies, such as Uber or WeWork, with powerful and sophisticated investors.[[240]](#footnote-241) Elizabeth Polman has offered an explanation to this puzzle that relies on the complex capital structure of late-stage startup and the conflict of interests of VC directors who would like to maintain their reputation as founder-friendly.[[241]](#footnote-242) Our analysis provides an alternative explanation as to why this phenomenon takes place in private companies: VCs who believe in the founder’s unique ability to produce superior returns are in a structural disadvantage. As long as the CEO is perceived as a star and the company depends on her vision and leadership, they are less likely to challenge the CEO.

*Second*, our analysis suggests that making the directors more independent or accountable to shareholders will not address the problem of unaccountable Superstar CEOs. In fact, CEOs are powerful precisely because boards believe they produce value for shareholders.

*Third*, and similarly to the previous point, our analysis highlights the limits of shareholder voting rights in the presence of a powerful CEO. Even if shareholders are dissatisfied with certain behavior of a Superstar CEO, they are unlikely to replace her, although they have the formal power to do so. This is because a change in the company leadership may have adverse financial effect on them. They have no reason to throw the baby out with the bathwater. Therefore, at the most, they will use their voting power to send a *non-binding* signal of dissatisfaction to the powerful CEO without translating it into concrete actions, or to withhold vote against other independent directors.[[242]](#footnote-243)

*Finally*, CEO power is also contingent upon the perception of star qualities. Once this fades away, a CEO who misbehaves can, and often will, be replaced.[[243]](#footnote-244) The need for legal intervention, thus, becomes weaker as control is more contestable, and in the presence of activist hedge funds or powerful institutional investors that could terminate misbehaving CEOs who lost their "golden touch."

# Corporate Law Implications

Superstar CEOs raise two normative questions for corporate law. In this part, we uncover these questions and use them to shed a new light on several fundamental doctrines that have long occupied courts and corporate law scholars.

*First*, what should be the role of corporate law in policing superstar CEOs? On the one hand, these CEOs are powerful, , and they might use their power to the detriment of investors (and other stakeholders). On the other hand, their power arises from the market’s appreciation of their unique contribution to company value. Thus, the conventional remedy of empowering shareholders is less likely to be effective in constraining superstar CEOs. Moreover, the ability of these CEOs to act opportunistically is limited by the magnitude of their unique contribution. And once their star quality fades away and, they are likely to face a real risk of removal.

*Second*, assuming that the CEO has some degree of unique contribution to the company value, should corporate law allocate the extra value created by the CEO to shareholders or to the CEO?

In this Part, we show how these two questions inform three recent developments—the expansion of the definition of controlling shareholders; courts’ treatment of management buyouts and other corporate control transactions; and the role of corporate law in protecting constituencies other than shareholders. The analysis we provide in this Part is a first important steps towards addressing complex issues that these three recent developments raise.

## Definition of Control

### Tesla: New Definition of “Control”

Under Delaware law, the legal treatment of related-party transactions critically depends on the company’s ownership structure and whether or not it has a controlling shareholder.[[244]](#footnote-245) Consider, for example, a company that acquires a business owned by the public company’s CEO. If a majority of the public company directors are disinterested and independent and the company has no controlling shareholder, courts will generally defer to the board’s decision to approve the transaction by applying the *business judgment rule*.[[245]](#footnote-246) However, if the CEO is the company’s controlling shareholder, courts will generally scrutinize the transaction under the more demanding *entire fairness* standard.[[246]](#footnote-247) In order to avoid a fairness review, the transaction has to be approved by a special committee of independent directors and a majority of disinterested shareholder.[[247]](#footnote-248)

Shareholders who hold 50% or more of voting rights or who have the ability to nominate 50% of the board are clearly controlling shareholders.[[248]](#footnote-249) However, plaintiffs wishing to challenge related-party transactions and have these transactions being subject to entire fairness standard (or to MFW conditions) often try to argue that courts should treat minority blockholders—those with less than 50% of the votes—as controlling shareholders.[[249]](#footnote-250)

The distinction between controlling and other significant shareholders has traditionally focused on shareholders’ voting power (or contractual rights to appoint directors). To be sure, in some borderline cases courts relied on shareholders’ influence as managers to classify them as controllers.[[250]](#footnote-251) Yet, shareholders with significantly less than 50% of the votes were not treated as controllers.[[251]](#footnote-252)

The *Tesla* decision marked a substantial departure from prior case law.[[252]](#footnote-253) Plaintiffs challenged Tesla's acquisition of SolarCity, another company founded by Musk.[[253]](#footnote-254) Although Elon Musk held only 20% of Tesla's voting rights, the Delaware court found him to be Tesla’s controlling shareholder with respect to the acquisition.[[254]](#footnote-255) Accordingly, the court subjected the transaction to the entire fairness standard.[[255]](#footnote-256) Notably, one of the reasons that led the court to conclude that Musk controlled Tesla was his unique contribution at the company’s visionary. As the court explained, “the Board was well aware of Musk's singularly important role in sustaining Tesla in hard times and providing the vision for the Company's success.”[[256]](#footnote-257)

The departure from prior case law triggered criticism. In a recent article, for example, two former Justices from Delaware’s Supreme Court and a leading expert on Delaware corporate law argue “that Musk was so talented and visionary that the company could not succeed without him – does not rationally imply that someone is a controlling stockholder.”[[257]](#footnote-258) Yet, Delaware courts seem to continue and take this fact (as well as some other factors) into account in deciding whether blockholders should be treated as controlling shareholders.[[258]](#footnote-259) And recent academic research has also expressed support of this view.[[259]](#footnote-260)

Our framework explains this development in Delaware law. Superstar CEOs share some features with controlling shareholders. Yet, treating these CEOs as controlling shareholders overlooks the real question underlying related-party transactions involving these CEOs.

The main justification for subjecting transactions with controlling shareholders to judicial review is the power that controlling shareholders have over directors.[[260]](#footnote-261) Disinterested and independent directors presumably have both the power and the motivation to prevent value-reducing transactions with CEOs. Especially in the present era of powerful shareholders,[[261]](#footnote-262) directors who approved a related-party transaction that harmed the company might not get re-elected.[[262]](#footnote-263) However, when controlling shareholders have the power to elect directors to the board, even truly independent directors might fail to prevent opportunistic self-dealing by these shareholders.[[263]](#footnote-264)

The previous Part has identified two distinct sources of CEO power: superstar status and equity ownership. Let us start with superstar qualities. At first sight, our analysis supports the *Tesla* treatment of superstar CEOs as controlling shareholders. As the previous Part explained, regardless of voting power, the mere perception that superstar CEOs are uniquely valuable to the company provides them with power over directors. These directors might therefore become less reliable as a mechanism for preventing opportunistic self-dealing.[[264]](#footnote-265)

This power is bolstered when the powerful CEOs own a significant equity stake that provides them with considerable voting power. Regardless of their status as CEOs or founders, blockholders who do not have a lock on control still have the power to influence—albeit not dictate—the outcome of shareholder votes. A shareholder with say 20% of the votes (similarly to Musk) could be pivotal in contested director elections even without a lock on control.[[265]](#footnote-266) This power, in turn, incentivizes directors to cater to the interests of this shareholder.

It is, therefore, tempting to treat superstar CEOs as controlling shareholders. After all, if directors are too weak, why not use judicial review to protect public investors from opportunistic related-party transactions? Our analysis, however, also points to the distinction between the case of majority shareholders and that of superstar CEOs.

Under the long-standing Delaware approach, courts did not equate *influence* with *control*. Courts did not treat blockholders as controlling shareholders if public investors had a realistic opportunity to win votes against the objection of these blockholders.[[266]](#footnote-267) In other words, controller status focused on the question whether control is *contestable.[[267]](#footnote-268)* That is, whether public investors have the collective power to outvote the blockholder.

Should this outcome change when the blockholder happens to be a superstar CEO? Visionary CEOs are powerful only to the extent that investors believe in their ability to produce above-market returns. The power of superstar CEOs is therefore limited along too important dimensions: *First*, boards are more likely to stand up to these CEOs if the expected harm from self-dealing exceeds the value of the CEO’s unique contribution to company value. *Second*, superstar CEOs lose their power once markets no longer believe in their ability to produce superior returns. These constrains also apply to CEOs who hold a significant fraction of the company shares. As we show in the previous Part, powerful CEOs with significant holdings (like Papa John's CEO) do get fired when the perception about their contribution to company value changes.[[268]](#footnote-269)

These constraints, however, do not apply to majority controlling shareholders and do not prevent them from expropriating minority shareholders. Controlling shareholders power is not based on their contribution to company value, but on their control over director appointments. Regardless of the views of other shareholders, they can appoint whomever they want to the board.[[269]](#footnote-270) Both majority shareholders and superstar CEOs can use related-party transactions to divert value from the company. Only superstar CEOs, however, face the constraint that they cannot extract more than the expected value of their unique contribution to company value.

This points to the difficult normative question underlying the *Tesla* approach. In this type of cases, investors are sufficiently powerful to defend against a CEO that reduces company value—whether by mismanagement or self-dealing. Investors can get this "downside protection" by exercising their voting power as a disciplining mechanism. Rather, the real question at stake concerns the distribution of the "upside" generated by the visionary CEO between her the public investors (an "upside protection"). Should corporate law allow Superstar CEOs to capture a fraction of their unique contribution to company value through related-party transactions? Treating superstar CEOs as controlling shareholders can be justified under the view that courts should prevent independent directors from awarding these CEOs part of their unique contribution to company value.

Up until the *Tesla* case, Delaware courts generally avoided treating powerful CEOs as controlling shareholders. There are several institutional dimensions that in our view explains courts' reluctance to elaborate the definition of controlling shareholders.

*First*, as we have just shown, in the case of powerful CEOs and related-party transactions, the potential "harm" to public investors from a more relaxed judicial review is capped by two safety valves that public investors have: they can remove the CEO if she loses her magic touch or outvote other independent directors and thereby signal their dissatisfaction with certain actions of the powerful CEO. Such safety valves may reduce courts willingness to intervene.

*Second*, a test that is based on "*contestability*", which limits to some extent the scope of the already broad and open-ended definition of "control" that Delaware courts use, increases certainty. And while there can be some disagreements as to the exact percentage in which control becomes contestable, such test provides a relatively clear metric to market players and enable them to anticipate in advance the level of judicial review to which the related-party transaction will be subject.

In contrast, a test that is based on broad notions such as "power" and "influence" constitutes a vague standard that can create ambiguity and uncertainty. As we have shown, some powerful CEOs can hold as little as 2% of the votes and still have significant influence on the firm decision making. Shall their related-party transactions be also subject to entire fairness review? If any powerful CEO could potentially exercise significant influence on the firm decision making, even with a tiny equity stake, where shall courts draw the line? Will they be able to distinguish between superstar CEOs and ‘regular’ ones? And shall courts also treat other influential blockholders, such as activist hedge funds, as effective controllers? As one can see, once the court elaborate the definition of "control" to also include powerful CEOs (or other minority holders) it introduces a whole host of complicated questions.

*Third*, subjecting transactions with Superstar CEOs to a substantive fairness analysis could also pose significant institutional challenges because often it requires an assessment by courts of the contribution of the powerful CEO to the firm. Consider, for example, the lawsuit against Elon Musk compensation,[[270]](#footnote-271) what would one consider in that case as "unfair" pay package that requires court intervention? Do courts have the ability to estimate the value of Musk's vision and unique skills to the company shareholders, and what metrics shall they use to do so?[[271]](#footnote-272) If shareholders themselves are willing to pay Musk and unprecedent amount once he meets certain super ambitious thresholds, which would make Tesla the largest automaker in the U.S. and deliver them imaginary returns, shall courts intervene in such contractual agreement?

As we can see, if one assume that the CEO’s unique contribution should be assessed together with the terms of the specific transactions, there is a hard question as to whether courts should be tasked with determining the value of superstar CEOs. This might require courts to assess the value of their unique vision.[[272]](#footnote-273) Thus, from institutional perspective, treating superstar CEOs as controlling shareholders makes sense only under the view that, courts could and should, perform this task.

In the case of majority controlling shareholders, courts rarely engage in substantive fairness analysis due to the adoption of the *MFW* standard, which encourages controllers to submit the transaction to a majority-of-minority vote in order to enjoy the deferential treatment of the business judgement rule.[[273]](#footnote-274) But such dual approval has its own costs. And while this process may be inevitable in order to protect public shareholders from unilateral expropriation by a majority controller, in the case of powerful CEOs, where shareholders still have the ability to replace the them if something goes wrong, such enhanced protection plays a more limited role.

 *Finally*, the rationale underlying the *MFW* approach is that shareholders are better positioned than courts to determine if a proposed conflicted transaction is desirable. In the previous Part, however, we explained that superstar CEOs’ power over boards stems from the market’s belief in their unique contribution to company value, not from directors’ lack of accountability to investors. Like boards of directors, shareholders might support a suboptimal related party transaction if they believe that its harm does not exceed the expected value of the CEO’s unique contribution. In Tesla, for example, both the SolarCity transaction and Musk's executive compensation scheme were approved by the overwhelming majority of disinterested shareholders.[[274]](#footnote-275) Tesla shareholders also gave their blessing to the appointment of Musk's brother as a company director, although appointment of relatives to the board are rare in a public company without a controller.

Despite the limited effectiveness of having a specific shareholder vote on a related-party transaction, it is not meaningless. For example, Superstar CEOs might be less confident in their ability to win such a vote if the related related-party is questionable or might fear the reputational cost of publicly losing such a vote. Moreover, in the absence of a separate vote on a specific related-party transaction, as long as a powerful CEO continues to outperform, shareholders are likely to extend her tenure and bear the "price" of a suboptimal related-party transaction with her. At the most, they would be able to express their frustration by voting against other directors who approved the opportunistic transaction by the CEO. Thus, as a matter of institutional design, two separate votes (one on director election and one a related-party transaction) enable shareholders to enjoy a larger share of the upside generated by a powerful CEO, compared to a situation where shareholders are able to express their view on a related-party transaction only indirectly in the annual election of directors.

Delaware law, however, does not include a mandatory requirement to subject a related-party transaction with a CEO (powerful or not) to a mandatory vote. Under the current regime, courts can either decide that the powerful CEO is not a controller, and then the transaction can be cleansed just by an approval of independent directors, or determine that the CEO is a controller and then the transaction it will be subject entire fairness or to MFW terms. There is no intermediate solution of just having a separate shareholder approval to transactions by powerful CEOs. And between these two options, courts have tended to prefer the first one. The analysis we set forth in this Section sheds light on the institutional reasons behind such choice as well as its distributive implications.

## Control Transactions

Our analysis also sheds a new light on one of the most litigated areas of corporate law, mergers and acquisitions. The law governing corporate acquisitions aims at ensuring that managers’ potential conflicts do not undermine investors’ right to receive the fair value of their shares. This desirable goal, however, becomes more challenging when management is uniquely valuable, that is, when the value of the company depends on the identity of its CEO. We first consider MBOs. We then consider other sales.

### 1. MBOs

In a management buyout transaction (MBO), the CEO—normally in cooperation with a private equity fund or another financial sponsor—takes a public company private by acquiring it from its public investors. In 2013, for example, Michael Dell, who owned approximately 16% of Dell, Inc. and served as its CEO and Chairman, together with Silver Lake Partners, acquired Dell from its public investors and took the company private.[[275]](#footnote-276)

MBO transactions create inevitable conflicts of interest between shareholders and management, whose interest is to buy the company from its shareholders at the lowest price possible. The conventional view identifies two main concerns associated with these conflicts. First, CEOs know the company better than shareholders and independent directors.[[276]](#footnote-277) They can use their informational advantage to buy the company at an unfair price. Second, CEOs might use their power to influence the company’s sale process in their favor and undermine potential bidders’ ability to make competing bids.[[277]](#footnote-278)

These concerns have led commentators to call for more extensive judicial review of MBO transactions.[[278]](#footnote-279) More recently, the question of the desirable legal treatment of MBOs has focused on the appraisal remedy, which allows dissenting shareholders in mergers to ask the court to determine the fair value of their shares.[[279]](#footnote-280) In appraisal cases, courts rely on valuation by experts, normally using the discounted cash flow method, to determine the fair value of the company.[[280]](#footnote-281) The question that has occupied courts and scholars is whether an adequate sale process is sufficient to ensure that shareholders receive the fair value of their shares. Under one approach, if the merger terms are the outcome of an auction or another competitive process, courts can rely on the merger price and forego the complicated task of determining the fair value of company.[[281]](#footnote-282) Under another approach, courts should independently value the company regardless of the process leading to the merger.[[282]](#footnote-283)

The Dell case is notable for bringing together the superstar CEO phenomenon and the appraisal debate. Following the Dell MBO, shareholders filed an appraisal action, and the defendants argued that, since the sale process provided other buyers with a meaningful opportunity to submit competing bids, the merger price was the best evidence of the company’s fair value.[[283]](#footnote-284) The Court of Chancery, however, found several imperfections in the sale process that prevented the court from relying on it to determine the company’s fair value. Thus, the court used the DCF method to value the company.[[284]](#footnote-285) The Supreme Court rejected the Court of Chancery’s reasons for disregarding the deal price,[[285]](#footnote-286) and significantly relied on the fact that other bidders could have submitted higher proposals to acquire the company.[[286]](#footnote-287)

Interestingly, the Delaware Chancery Court in the Dell case has expressly addressed, for the first time, the issue of “valuable CEOs," indicating that: "[a] competing bidder that did not have Mr. Dell as part of its buyout group would be bidding for a company without that asset and would end up with a less valuable" and that "Mr. Dell's unique value and his affiliation with the Buyout Group were negative factors that inhibited the effectiveness of the go-shop process".[[287]](#footnote-288) Later on, the Delaware Supreme Court undermined the factual basis of this thesis, stating the Court of Chancery "did not identify any possible bidders that were actually deterred because of Mr. Dell's status."[[288]](#footnote-289)

In an insightful Article, Guhan Subramanian shed additional light on the factors that undermines the effectiveness of a market check prior to an MBO. In particular, he explains that a market canvass process is no longer a useful mechanism for price discovery when management is valuable and chooses not to work with third-party bidders.[[289]](#footnote-290) Therefore, he has put forward a set of proposals that boards and their advisors shall follow to level the playing field and improve the role of auctions in price discovery.[[290]](#footnote-291)

 Our analysis offers a new explanation for the tension underlying MBOs, at least for companies with superstar CEOs. The law of corporate acquisitions ultimately seeks to ensure that the target’s shareholders get the fair value of their shares, that is, their pro rata share of the value of the company as a going concern, without the gains that the acquisition will produce (synergies).[[291]](#footnote-292) This objective, in turn, relies on the premise that the value of the company does not depend on the identity of its CEO. This premise, however, does not hold when the CEO is uniquely valuable. Thus, we argue, underlying the choice between appraisal and deal price as a measure of firm value is a normative question: who is entitled to value created by the CEO’s unique contribution to company value?

Assume that a CEO acquires the company from its public investors. Assume further that the value of the company under the leadership of the current CEO exceeds that of its value under any other CEO. What is the ‘fair value’ of the company under these assumptions? In other words, from a normative standpoint, what value should public investors be entitled to? The (lower) value of the company without the CEO or the (higher) value with the CEO?

This is not an easy question to answer. On the one hand, until the CEO decided that she wanted to take the company private, there was no doubt that the extra value that she produced belonged to shareholders. The CEO is entitled to a compensation package (that may include company shares or other forms of equity-based compensation), and shareholders are entitled to all the company’s residual cash flows. On the other hand, shareholders depend on the CEO for the company to produce this extra value. Investors cannot force a CEO to continue and provide their services to the company.[[292]](#footnote-293)

We do not intend to take a stand. Rather, we make two points. First, the difficulty with regulating MBOs exists not only because of asymmetric information or the threat of opportunistic behavior by CEOs. It can exist even when boards are powerful, independent and genuinely accountable to public investors. This explains why the rise of shareholder power does not necessarily imply ‘the death of corporate law’ for judicial review of M&A transactions. The rise of shareholder power somewhat mitigates the concerns about opportunistic MBOs. Directors who are more accountable to shareholders and less dependent on CEOs can be expected to control the sale process, by forming a special committee, for example.[[293]](#footnote-294) But this cannot solve the problem of value diversion to a powerful CEO through M&A transactions.

Second, we argue that one’s view about the normative question leads to a different legal treatment of MBOs. Relying on deal price as a measure of fair value is supported by the view that public investors are entitled to the value of the company without the CEO. The appraisal remedy, in contrast, is consistent with the other approach. To see why, consider the prevalent method for valuing companies, the discounted cash flow method (DCF). This method is notorious for its reliance on hired-gun experts that produce divergent valuations. Our analysis, in contrast, identifies a feature that would exist even if expert opinions were not biased. The DCF method relies on future cash flows. This measure takes into account both past cash flows and management projections. Thus, this method of valuation captures the unique value produced by the superstar CEO (unless she postponed implementing plans).

Now consider an auction led by the board. The CEO announces that she will join only one of the bidders. Even with a ‘clean’ process and full information, if the CEO is uniquely valuable, then other bidders would offer a lower price for the company than that offered by the CEO simply because the company is worth less without its CEO. In contrast, if the CEO is not uniquely valuable, a robust market check could produce superior bids.[[294]](#footnote-295)

Note that in our superstar CEO example, the more valuable the CEO, the ‘fair value’ of the company shares will likely be higher with appraisal. The appraisal remedy will take into account the past contribution of the CEO to firm value. It does not formally incorporate the CEO identity into the model. Other bidders, in contrast, will try to assess the expected value of the company without its superstar CEO.

Thus, to the extent that public investors are not entitled to the extra value that the CEO produces, then relying on the deal price is preferable to judicial valuation.[[295]](#footnote-296) On the other hand, the appraisal remedy will tend to provide public investors with a share of the extra value attributable to the CEO leadership.

Moreover, unlike the case of self-dealing, this regime does not require courts to determine whether the CEO is indeed uniquely valuable. If he is not valuable, other bidders will offer better value, and there will be little difference between the value under appraisal and the deal price method.

Our analysis does not mean that there are no other concerns with MBOs. Asymmetric information is a problem and management may take steps to deter other bidders.[[296]](#footnote-297) These concerns, however, should be incorporate into the deal process inquiry.

Note that our analysis differs from that that Guhan Subramanian offers. Indeed, he also recognizes the problem of “valuable CEOs” (to the best of our knowledge he was the first and only one to do so). His analysis, however, focuses on the obstacle that superstar CEOs might create for bidders – they cannot free ride the bid of the insiders because it may reflect the value with the CEO.[[297]](#footnote-298) In his view, this means that auctions are less likely to work.[[298]](#footnote-299) This analysis leads him to make several proposals to improve the deal process, and especially make sure that ‘valuable’ management works with other bidders, etc.[[299]](#footnote-300) But the ability of valuable CEO to offer a higher price is not necessarily a negative outcome. Rather, it reflects a normative question as to whether superstar CEOs—and not shareholders—are entitled to the extra value that they produce.

###  Acquisitions by Third Parties

Our analysis thus far has focused on the measure of fair value in MBO transactions. Yet, the superstar CEO phenomenon can shed light on other aspects of M&A litigation.

M&A deals are an important source for litigation. Until *Corwin*, they were subject to enhanced scrutiny under *Revlon* case*.* The concern justifying enhanced scrutiny was CEO conflicts, normally in the form of preferential treatment to bidders who are more favorable to the CEO, for example, by offering future employment or bonuses. Indeed, Guhan Subramanian argues that the distinction between an MBO and a freeze transaction by a controller is not so clear in private equity deals.

In our framework, we distinguish between two types of payments. One type of payment is for departing CEOs, through non-compete arrangements or closing bonuses.[[300]](#footnote-301) This payment is typically intended to induce the CEO to agree to a sale of the company.[[301]](#footnote-302) Other types of benefits concern retention agreements or other arrangements under which the buyer will employ the existing management.

We focus on the latter type. If the CEO is valuable, then buyers would like to retain them. On the one hand, this should make the target more attractive, and thus increases the likelihood of an acquisition transaction that also benefit shareholders of the target as well. On the other hand, this could simply be a way to divert value from shareholders to the CEO. Assume that the company is sold to a third party. The buyer believes that the CEO is valuable and would like to retain her or pay her consulting fees. The concerns here are like in the previous case. On the one hand, this payment may reflect her unique contribution to value. On the other hand, this may be a form of ‘bribery’ to induce the CEO to favor one bidder over another.

Forming a special committee to run the process can ensure that CEO conflicts do not affect the process, and most importantly, provides a meaningful opportunity to make a competing bid.[[302]](#footnote-303) But, even a perfect process cannot deal with the issue of valuable CEOs.

Under *Corwin*, a shareholder vote that is informed and not coerced will entitle the transaction to a business judgment review. The major criticism here is that bundling the decisions into a single vote cannot ensure that public shareholders gets their fair share. Separating the votes, and having one on the transaction and another on the side payment to the CEO, would not help if the acquirer conditions the transaction on retaining the powerful CEO and paying her a side benefit. Moreover, why would shareholders agree to such payment that reduce their share of the pie? So, as in the previous Section, the real issue at stake is who should be entitled to the extra value generated by the powerful CEO. Our framework shows that the *Corwin* doctrine lets powerful CEOs capture a larger share, and that even competing bids cannot take this away.

## ESG and Oversight

In recent years, there has been a growing interest in the role of corporate law and governance in protecting the interests of stakeholders, other than shareholders.[[303]](#footnote-304) Our framework sheds new light on the extent to which companies can pursue stakeholder interests under existing governance arrangements and on board failure to prevent managerial misconduct.

*1. Superstar CEOs and Stakeholder Protection*

We begin with the implications of our analysis for the wide questions of ESG and the protection of stakeholders. There seems to be a growing optimism that increasingly powerful shareholders can play an important role in pushing companies to incorporate ESG considerations into their policies.[[304]](#footnote-305) In recent years, shareholders bring more and more ESG-related proposals[[305]](#footnote-306) and prominent scholars argue that shareholders shall have a greater say on these topics.[[306]](#footnote-307) Institutional investors engage in high-profile initiatives aimed at protecting stakeholder interests, and even activist hedge funds started to bring ESG interests on their agenda.[[307]](#footnote-308)

However, our analysis shows that there are limits to the reliance on shareholders to cause firms to take stakeholder interests into consideration. The presence of a Superstar CEO in the boardroom may change the whole dynamic between shareholders and management. The hope that shareholders will drive corporations to change implicitly relies on the substantial increase in shareholder power. But even powerful shareholders may simply be too deferential to iconic CEOs. In those situations, the question whether the company will also protect stakeholder interests depends on the good will of the Superstar CEO, and she may, or may not, support a stakeholderist approach.[[308]](#footnote-309) Either way, shareholders will have a limited say on these matters due to their lack of incentives to replace a successful CEO or acting against her will.[[309]](#footnote-310)

Our analysis is also supported by recent empirical evidence showing that targets that outperform or that have superstar CEOs are less likely to be subject to ESG activism. For example, a recent study finds that shareholder proposals are significantly more likely to fail when the CEO is a superstar.[[310]](#footnote-311) Amazon, for instance, has faced mounting scrutiny over labor and workplace safety issues. We found that between 2015 and 2020, the company was subject to 26 shareholder proposals on environmental and social issues, including those related to human rights and labor issues, but none of them passed (or even received more than 35% support).[[311]](#footnote-312)

Another study that analyzes a proprietary dataset of a large international, socially responsible activist fund shows that targets of ESG activism have lower potential growth opportunities and have a high entrenchment score.[[312]](#footnote-313) A third study that examines a large dataset of firm-level ESG news and their reaction on stock prices find that "investors differentiate in their reactions based on whether the news is likely to affect a company’s fundamentals, and therefore their reactions are motivated by a financial rather than a nonpecuniary motive."[[313]](#footnote-314) Commenters also note that even the poster child of climate activism, the campaign launched by Engine No. 1 against Exxon Mobil, was mostly motivated by severe underperformance of Exxon.[[314]](#footnote-315)

One could argue, however, that shareholders in the above-mentioned examples may be reluctant to advance stakeholder interests not because they are too deferential to a Superstar CEO, but rather because their preferences are perfectly aligned with those of the CEO and they both prefer maximizing the company profits at the expense of advancing stakeholder interests. To disentangle between these two alternative explanations, we turn now to the example of managerial misconduct. In certain types of managerial misconducts, it is clear the managerial behavior will not maximize shareholder value, and therefore shareholders have no interest to support it.

*2. Superstar CEOs and Managerial Misconduct*

One of the timely questions in corporate governance is the role of directors in exercising their oversight duty to prevent managerial misconduct. It worth emphasizing at the outset that our discussion of misconduct does not include cases when the board knowingly decided to violate the law.[[315]](#footnote-316) Rather, we focus on so-called oversight failure cases.

The first type of corporate misconduct is directly related to the company’s business, and might even increase profits if undetected. However, such misconduct could also result in corporate liability and penalties if corporate incompliance with government regulations is detected. When corporate misconduct leads to penalties, plaintiffs often file *Caremark-*type derivative lawsuits alleging that the boards failed to monitor.[[316]](#footnote-317) Delaware courts seem to be more receptive to these lawsuits in recent years.[[317]](#footnote-318)

The second type of managerial misconduct and wrongdoingis *not* directly related to the company business, and thus might be costly for the company and shareholders. For example, consider allegations against the founder of WeWork use of drugs in the workplace and self-dealing; sexual harassment claims against corporate executives;[[318]](#footnote-319) or even Musk’s use of Twitter.

Both types of cases raise the following question: why do boards fail to prevent CEOs from engaging in misconduct? The existing view focuses on CEO power or board agency costs. For example, it has been argued that board members are rewarded with equity-based compensation that leads them to prefer short-term profits over long-term performance.[[319]](#footnote-320) Under this view, making boards more independent would make them better suited to prevent CEO misconduct.

But this view fails to explain the second type of managerial misconduct (the one that is not directly related to the company business). Why would directors turn a blind eye towards unlawful behavior by the CEO, such as discriminatory practices, that is not likely to benefit the corporation?

Agency cost theories also cannot explain both types of misconduct at start-up companies, such as Uber and WeWork, with powerful and sophisticated investors that can closely monitor management.[[320]](#footnote-321) Governance scholars have offered an explanation to this puzzle that relies on the complex capital structure of late-stage startup and the conflict of interests of VC directors. For example, Elizabeth Polman argues that directors appointed by VC funds lack incentives to uncover problems given the need to bring in new investors.[[321]](#footnote-322) Donald Langevoort and Hilary Sale argue that public markets and their governance structure are better at monitoring CEOs.[[322]](#footnote-323)

We offer another explanation: directors face difficulty in monitoring Superstar CEOs, as they are afraid from the consequences to the company of losing a Superstar CEO (including by uncovering information about CEO misconduct). Consider, for example, a CEO that is believed to be critical for the company’s success. At the same time, the CEO engages in unlawful conduct that might be harmful to the company, such using Twitter irresponsibly, using drugs, or even engaging in sexual misconduct.[[323]](#footnote-324) In those cases, the board may be reluctant to dismiss the Superstar CEOs or, more realistically, might find it optimal to remain ignorant of their misconduct. Moreover, boards with Superstar CEOs are likely to be deferential to them when it comes to business strategy, including the way to manage business risks. This tendency might extend to legal risks and compliance strategy.[[324]](#footnote-325)

This leads to two implications. *First*, making directors more independent or more accountable to shareholders will not improve their performance in exercising oversight over powerful CEOs to prevent misconduct. In other words, there is need for some legal intervention to prevent these third-party externalities.

*Second*, it informs the under theorized *Caremark* doctrine. Why is there a need for a special doctrine to require boards to monitor compliance? Our analysis shows that boards might prefer ignorance not because they are afraid of personal liability (which is rare anyway).[[325]](#footnote-326) Rather, because there is a need for some form of external intervention to make directors focus on compliance, either because they prefer not to know facts that would force them to confront Superstar CEOs or because they are too deferential to those powerful CEOs.

Our analysis, thus, provide additional support to the view that *Caremark* doctrine is not really about protecting shareholder interests, but rather about advancing the interests of stakeholders. In particular, we show that shareholders may benefit from the continued leadership of a powerful CEO and are likely to tolerate this misbehavior, despite its externalities on third parties and as long as it does not harm the company value significantly.[[326]](#footnote-327)

1. See, e.g., Lucian A. Bebchuk & Assaf Hamdani, *The Elusive Quest for Global Governance Standards*, 157 U. Pa. L. Rev. 1263 (2009); Ronald J. Gilson, Controlling Shareholders and Corporate Governance: Complicating the Comparative Taxonomy, 119 Harv. L. Rev. 1641 (2006). [↑](#footnote-ref-2)
2. *See, e.g.,* Lucian A. Bebchuk & Assaf Hamdani, *Independent Directors and Controlling Shareholders*, 165 U. Pa. L. Rev. 1271, 1273 (2017) (hereinafter: Bebchuk & Hamdani, *Independent Directors*). [↑](#footnote-ref-3)
3. See, e.g., *Kobi Kastiel, Against All Odds: Hedge Fund Activism in Controlled Companies*, 2016 Colum. Bus. L. Rev. 60, 126 (2016). [↑](#footnote-ref-4)
4. *See, e.g.,* Lucian A. Bebchuk & Kobi Kastiel, *The Perils of Small-Minority Controllers*, 107 Geo. L.J. 1453, 1459 (2019); Zohar Goshen & Assaf Hamdani, *Corporate control, dual class, and the limits of judicial review*, 120 Columbia Law Review 941, 963-64 (2020). [↑](#footnote-ref-5)
5. See, e.g., Simeon Djankov et al., *The Law and Economics of Self-Dealing,* 88 J. Fin. Econ. 430 (2008). For a review of The analysis of the relative efficiency of rules regulating self-dealing was developed several years earlier. For a review of this prevailing view and related studies, see Zohar Goshen & Assaf Hamdani, *Corporate Control and Idiosyncratic Vision*, 125 Yale L.J. 560, 571-73 (2016). [↑](#footnote-ref-6)
6. See, e.g., Lucian A. Bebchuk & Assaf Hamdani, *The Elusive Quest for Global Governance Standards*, 157 U. Pa. L. Rev. 1263 (2009). [↑](#footnote-ref-7)
7. *See, e.g.,* ADOLF A. BERLE, JR. & GARDINER C. MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY 139–40 (1932) (observing that managers “while in office, have almost complete discretion in management”); Michael C. Jensen & William H. Meckling, Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure, 3 J. FIN. ECON. 305, 308, 315 (1976) (noting that “there is good reason to believe that the agent will not always act in the best interests of the principal”); Roberta Romano, Metapolitics and Corporate Law Reform, 36 Stan. L. Rev. 923, 923 (1984) (“[A]fter half a century, discussion of the corporate form still invariably begins with Berle and Means’ location of the separation of ownership and control as the master problem for research.”). [↑](#footnote-ref-8)
8. *See, e.g.,* Lucian Bebchuk & Jesse Fried, Pay without Performance: The Unfulfilled Promise of Executive Compensation 23-33; Marcel Kahan & Edward Rock, *Embattled CEOs*, 88 TEX. L. REV. 987, 1038 (2010); Jay Lorsch & Elizabeth Maciver, *Pawns or Potentates: The Reality of America's Corporate Boards* (Harvard Business School Press, Cambridge, MA) 20-23 (1989). [↑](#footnote-ref-9)
9. *See, e.g.,* Bernard S. Black, *Shareholder Passivity Reexamined*, 89 Mich. L. Rev. 520, 584-91 (1990) (discussing rational apathy, and shareholder’s lack of incentives to become informed). See also Bayless Manning, *The Shareholder’s Appraisal Remedy: An Essay for Frank Coker*, 72 YALE L. J. 223, 261 (1962) (“It is commonplace to observe that the modern shareholder . . . does not think of himself or act like an ‘owner.’ He hires his capital out to the [corporate] managers and they run it for him; how they do it is their business, not his, and he always votes ‘yes’ on the proxy.”). [↑](#footnote-ref-10)
10. *See, e.g.,* Lucian A. Bebchuk, *The Myth of the Shareholder Franchise*, 93 Va L. Rev. 675, 680 (2007) (providing empirical evidence on the small number of electoral challenges). *See also* Kobi Kastiel & Yaron Nili, *Competing for Votes* 10 Harvard Business Law Review 287, 290 (2020) (explaining how in the past, shareholder voting was largely inconsequential, and shareholders often sided with management). [↑](#footnote-ref-11)
11. Claudia H. Allen, Neal, Gerber & Eisenberg, LLP, *Study of Majority Voting in Director Elections*, at ii (2007), http://www.ngelaw.com/files/upload/majoritystudy111207.pdf ("Until recently, virtually all directors of U.S. public companies were elected under a "plurality' vote standard."); Kahan & Rock, *supra* note 8, at 1010 ("[o]f S&P 100 companies, only ten deviated from plurality voting in 2003"). [↑](#footnote-ref-12)
12. See Allen, *id.*, at ii ("A nominee in an election to be decided by a plurality could theoretically be elected with as little as one vote, thereby ensuring that, in an uncontested election, nominees slated by a board will be elected and that board seats will not be left vacant."). [↑](#footnote-ref-13)
13. *See*, e.g., Anil Shivdasani & David Yermack *CEO involvement in the selection of new board members: An empirical analysis,* 54 J. Fin. 54 1829, 1830 (1999) (CEO is involved in nominating directors when the company has no nominating committee and the CEO serves on the board or when the CEO is a member of the nominating committee); Lucian Bebchuk & Jesse Fried, Pay without Performance: The Unfulfilled Promise of Executive Compensation 23-33 (2004). [↑](#footnote-ref-14)
14. *See* Jay Lorsch & Jack Young, *Pawns or Potentates: The Reality of America's Corporate Boards*, 4 The Executive 85, 85-86 (1990) (“in spite of the existence of nominating committees in most boards, the chairman/CEO still is a major influence on the selection of directors. It is no exaggeration to say that many directors are beholden to the CEO for their position, when they are in fact supposed to be monitoring the CEO's performance/position.”) [↑](#footnote-ref-15)
15. *See, e.g.,* Moran v. Household Int’l, Inc., 500 A.2d 1346, 1357 (Del. 1985) (applying the business judgment rule to the board’s adoption of a poison pill because it was adopted “in the good faith belief that it was necessary to protect” the corporation); Air Prods. & Chems., Inc. v. Airgas, Inc., 16 A.3d 48, 57 (Del. Ch. 2011) (approving the board’s continued use of a poison pill even when combined with a staggered board—a board in which only a third of its members are up for reelection every year). [↑](#footnote-ref-16)
16. Lucian Arye Bebchuk, John C. Coates, & Guhan Subramanian, *The Powerful Antitakeover Force of Staggered Boards: Theory, Evidence, and Policy*, 54 Stan. L. Rev. 887, 910, 913 (2002) (explaining that there has never been a hostile acquisition of a firm with an effective staggered board where the firm kept its pill in place); [↑](#footnote-ref-17)
17. Bebchuk & Hamdani, *supra* note 1, at 1276-80 (discussing the need to make directors more accountable to shareholders); Jeffrey N. Gordon, *The Rise of Independent Directors in the United States, 1950-2005: Of Shareholder Value and Stock Market Prices*, 59 Stan. L. Rev. 1465, 1468 (2007) (estimating that the percentage of independent directors has increased from around 20% in 1950 to around 80% in 2005). [↑](#footnote-ref-18)
18. Edward B. Rock, *Adapting to the New Shareholder-Centric Reality,* 161 University of Pennsylvania Law Review 1907, 1922 (2013) ("the old story of dispersed ownership, passive shareholders, and directors under the thumb of an imperial CEO is no longer accurate"). [↑](#footnote-ref-19)
19. S*ee, e.g.*, Dorothy S. Lund & Elizabeth Pollman, *The Corporate Governance Machine*, 121 Colum. L. Rev. (forthcoming 2021) (manuscript at 4-10) https://ssrn.com/abstract=3775846. [↑](#footnote-ref-20)
20. *Id.* [↑](#footnote-ref-21)
21. Jeffrey N. Gordon, *The Rise of Independent Directors in the United States, 1950-2005: Of Shareholder Value and Stock Market Prices*, 59 Stan. L. Rev. 1465, 1473 n. 9 (2007). [↑](#footnote-ref-22)
22. Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745. [↑](#footnote-ref-23)
23. N.Y. Stock Exch., N.Y.S.E. Listed Company Manual §§ 303A.01, .04, .05, .06 (2021) https://nyse.wolterskluwer.cloud/listed-company-manual/document?treeNodeId=csh-da-filter!WKUS-TAL-DOCS-PHC-%7B0588BF4A-D3B5-4B91-94EA-BE9F17057DF0%7D--WKUS\_TAL\_5667%23teid-69 [https://perma.cc/F4QK-2SW3]; Nasdaq, Nasdaq Stock Market LLC Rules § 5605(b)(1), (c)(2), (d)(2), (e) (2021) https://listingcenter.nasdaq.com/rulebook/nasdaq/rules/Nasdaq%205600%20Series. [↑](#footnote-ref-24)
24. Kobi Kastiel & Yaron Nili, *"Captured Boards": The Rise of "Super Directors" and the Case for a Board Suite*, 19 Wis. L. Rev. 25-26 (2017). [↑](#footnote-ref-25)
25. Jeffrey N. Gordon, *The Rise of Independent Directors in the United States, 1950-2005: Of Shareholder Value and Stock Market Prices*, 59 Stan. L. Rev. 1465, 1473 n. 9 (2007). [↑](#footnote-ref-26)
26. Kobi Kastiel & Yaron Nili, *The Corporate Governance Gap*, 131 Yale L.J. (forthcoming, 2022) (manuscript pp. 39-40), https://papers.ssrn.com/sol3/papers.cfm?abstract\_id=3824857 (hereinafter: Kastiel & Nili, *The Corporate Governance Gap*). [↑](#footnote-ref-27)
27. Lucian Arye Bebchuk, John C. Coates IV & Guhan Subramanian, *The Powerful Antitakeover Force of Staggered Boards: Theory, Evidence, and Policy*, 54 Stan. L. Rev. 887, 894 (2002). [↑](#footnote-ref-28)
28. *Id*. [↑](#footnote-ref-29)
29. *Id*. at 912-13.Cite Airgas Delaware case XX (allowing the board to keep the poison pill even after the bidder won one round of director elections). [↑](#footnote-ref-30)
30. *Id.* at 914. [↑](#footnote-ref-31)
31. For a review of the empirical evidence showing that annual elections annually make directors more accountable to shareholders, see Lucian Bebchuk, Scott Hirst, & June Rhee, *Towards the Declassification of S&P 500 Boards*, Harv. Bus. L. Rev. 157, 165 (2013). For the opposite view, *see* K.J. Martijn Cremers, Lubomir P. Litov & Simone M. Sepe, *Staggered Boards and Long-Term Firm Value, Revisited*, 126 J. Fin. Econ. 422, 422-23 (2017) (finding a positive association between staggered boards and long-term firm value). *See also,* Yakov Amihud, Markus Schmid, and Steven Davidoff Solomon, *Settling the Staggered Board Debate*, 166 U. PA. L, Rev. 1475 (2018). [↑](#footnote-ref-32)
32. Marcel Kahan & Edward Rock, *Embattled CEOs*, 88 Tex. L. Rev. 987, 1008 (2010) (hereinafter: Kahan & Rock, *Embattled CEOs*). [↑](#footnote-ref-33)
33. A notable example in that regard is the Shareholder Rights Project at Harvard Law School, which assisted institutional investors in using shareholder proposals to precipitate the declassification of previously staggered boards at roughly 100 S&P 500 and Fortune 500 companies. *See* Lucian Bebchuk, Scott Hirst, & June Rhee, *Towards the Declassification of S&P 500 Boards*, Harv. Bus. L. Rev. 157 (2013). [↑](#footnote-ref-34)
34. Kastiel & Nili, *The Corporate Governance Gap*, *supra* note 26, at pp. 33-34. [↑](#footnote-ref-35)
35. Zohar Goshen & Sharon Hannes, *The Death of Corporate Law*, 94 New York University Law Review, 263, 279-280 (2019); Institutional S’holder Servs., United States Proxy Voting Guidelines: Benchmark Policy Recommendations 13 (Nov. 21, 2016). [↑](#footnote-ref-36)
36. Stephen J. Choi, Jill E. Fisch, Marcel Kahan & Edward B. Rock, *Does Majority Voting Improve Board Accountability?*, 83 U. Chi. L. Rev. 1119 (2016). [↑](#footnote-ref-37)
37. *Id.* [↑](#footnote-ref-38)
38. *Id*. *See, also* David Webber, The Rise Of The Working-Class Shareholder: Labor’s Last Best Weapon 75 (2018) (discussing how the United Brotherhood of Carpenters Fund utilized shareholder proposals to successfully influence many target companies to adopt majority voting in shareholder elections); Kastiel & Nili, *The Corporate Governance Gap*, *supra* note 26, at 43-44 (showing that 88% of companies that make up the S&P 500 required a majority vote for board elections in 2020, and above 60% and 55% of the S&P 400 and S&P 600, respectively, require majority voting. [↑](#footnote-ref-39)
39. Kahan & Rock, *Embattled CEOs*, *supra* note 32, at 1042. [↑](#footnote-ref-40)
40. *See, e.g.,* Edward B. Rock, *Institutional Investors in Corporate Governance*, in The Oxford Handbook of Corporate Law and Governance 363, 365 (Jeffrey N. Gordon & Wolf-Georg Ringe eds., 2018); Assaf Hamdani & Sharon Hannes, *The Future of Shareholder Activism*, 99 B.U. L. Rev. 971, 973 (2019). [↑](#footnote-ref-41)
41. *See, e.g.,* Lucian A. Bebchuk & Scott Hirst, The Specter of the Giant Three, 99 B.U. L. Rev. 721, 725-26 (2019); John C. Coates, The Future of Corporate Governance Part I: The Problem of Twelve (Harvard Pub. Law Working Paper No. 19-07 2018), <https://corpgov.law.harvard.edu/wp-content/uploads/2019/11/John-Coates.pdf>. [↑](#footnote-ref-42)
42. Bebchuk & Hirst, *id.*, at 732-40 (documenting that the “Big Three” collectively vote about 25% of the shares in all S&P 500 companies and that stock held by index funds has risen dramatically over the past two decades and can be expected to continue growing). [↑](#footnote-ref-43)
43. Kobi Kastiel & Yaron Nili, *Competing for Votes*, 10 Harv. Bus. L. Rev. 287 312-314, 319-312 (2020) (providing evidence that "investors do not always stick in the pocket of management" in connection with votes on proxy fights, shareholder proposals, say-on-pay votes and uncontested director elections); Ryan Bubb & Emiliano Catan, *The Party Structure of Mutual Funds* (Feb. 14, 2018) (analyzing voting by mutual funds by breaking it down into three major groups: the managerial, shareholder intervention, and shareholder veto; the characterization of which depends on whether they vote with or against management).  [↑](#footnote-ref-44)
44. Lund & Pollman, *The Corporate Governance Machine*, *supra* note 19, at p. 3. [↑](#footnote-ref-45)
45. *See, e.g.,* BlackRock, Our 2021 Stewardship Expectations: Global Principles and Market-Level Voting Guidelines (2021), https://www.blackrock.com/corporate/literature/publication/our-2021-stewardship-expectations.pdf. [↑](#footnote-ref-46)
46. Kahan & Rock, *Embattled CEOs*, *Supra* note 32, at p. 1007. [↑](#footnote-ref-47)
47. Kastiel & Nili, *The Corporate Governance Gap*, *supra* note 26, at pp. 9-10. [↑](#footnote-ref-48)
48. Leo E. Strine, Jr., *The Delaware Way: How We Do Corporate Law and Some of the New Challenges We (and Europe) Face*, 30 Del. J. Corp. L. 673, 688(2005) ["[P]owerful CEOs come on bended knee to Rockville, Maryland, where ISS resides, to persuade the managers of ISS of the merits of their views about issues like proposed mergers, executive compensation, and poison pills. They do so because the CEOs recognize that some institutional investors will simply follow ISS’s advice…"]. [↑](#footnote-ref-49)
49. Ronald J. Gilson & Jeffrey N. Gordon, *The Agency Costs of Agency Capitalism: Activist Investors and the Revaluation of Governance Rights*, 113 Colum. L. Rev. 863, 874-75 (2013) [↑](#footnote-ref-50)
50. Alon Brav, Wei Jiang, Frank Partnoy & Randall Thomas, *Hedge Fund Activism, Corporate Governance, and Firm Performance*, 63 J. Fin. 1729, 1734-36 (2008) (describing the main characteristics of hedge funds); Lucian A. Bebchuk, Alon Brav, Wei Jiang & Thomas Keusch, *Dancing with Activists*, 137 J. Fin. Econ. 1 (2020) (providing a comprehensive analysis of the drivers, nature, and consequences of activists’ engagements and settlements with companies). [↑](#footnote-ref-51)
51. [↑](#footnote-ref-52)
52. *See,* Frank Partnoy & Randall Thomas, *Gap Filling, Hedge Funds, and Financial Innovation*, *in* New Financial Instruments and Institutions: Opportunities and Policy Challenges 101, 101 (Yasuyuki Fuchita & Robert E. Litan eds., 2007) (observing that activist hedge funds “have shaken up boardrooms and forced radical changes at many publicly-traded firms”). See also Jonathan Macey, for instance, claimed that hedge funds and private equity firms “are the newest big thing in corporate governance” and that they “actually deliver on their promise to provide more disciplined monitoring of management.” Jonathan R. Macey, Corporate Governance: Promises Kept, Promises Broken 241, 272 (2008). Marcel Kahan and Ed Rock expressed hope that activist hedge funds “may act ‘like real owners’ and provide a check on management discretion.” Kahan & Rock, *supra* note \_, at 1047. [↑](#footnote-ref-53)
53. Marcel Kahan & Edward B. Rock, *Hedge Funds in Corporate Governance and Corporate Control*, 155 U. Pa. L. Rev. 1021, 1029-32, 1061-62 (2007); Dancing with activists, supra note [\_], at \_\_. [↑](#footnote-ref-54)
54. Goshen & Square; Lund & Pollman; Kahan & Rock; Kastiel & Nili, *The Corporate Governance Gap*, *supra* note 26, at p. 10. [↑](#footnote-ref-55)
55. Steven N. Kaplan & Bernadette A. Minton, How Has CEO Turnover Changed? 1, 1-4 (Nat'l Bureau of Econ. Res. working paper no. 12465, Aug. 2006), https://www.nber.org/system/files/working\_papers/w12465/w12465.pdf. [↑](#footnote-ref-56)
56. Kahan & Rock, *Embattled CEOs*, *Supra* note 32, at p. 1032. [↑](#footnote-ref-57)
57. Kastiel & Nili, *The Corporate Governance Gap*, *supra* note 26, at pp. [XX]. [↑](#footnote-ref-58)
58. Kahan & Rock, *Embattled CEOs*, *Supra* note 32, at pp. 1030-32, 1042. [↑](#footnote-ref-59)
59. Cross reference. [↑](#footnote-ref-60)
60. *See* Edward Rock, *Adapting to the New Shareholder-Centric Reality*, 1910. [↑](#footnote-ref-61)
61. Zohar Goshen & Sharon Hannes, *The Death of Corporate Law*, 94 New York University Law Review, 263, 265 (2019). [↑](#footnote-ref-62)
62. *See, e.g.,* Roe & Shapira*, The Power of the Narrative in Corporate Lawmaking*, HBLR 3 (2020) (describing the view that “executives, confronted with a demanding stock market of traders and activists, focus too much on boosting the immediate quarterly financial statements, rather than on the business’s long-term health.") [↑](#footnote-ref-63)
63. Dhruv Aggarwal, Ofer Eldar, Yael V. Hochberg & Lubomir P. Litov, *The Rise of Dual-Class Stock IPOs*, 2-8 (2021), https://papers.ssrn.com/sol3/papers.cfm?abstract\_id=3690670. [↑](#footnote-ref-64)
64. Jay R. Ritter, *Initial Public Offerings: Updated Statistics***,** Warrington College of Business, 68 **(**Oct. 1, 2021) <https://site.warrington.ufl.edu/ritter/files/IPO-Statistics.pdf>. [↑](#footnote-ref-65)
65. *See, e.g.,* Lucian A. Bebchuk & Kobi Kastiel, *The Perils of Small-Minority Controllers*, 107 Geo. L.J. 1453 (2019). [↑](#footnote-ref-66)
66. Lucian A. Bebchuk & Kobi Kastiel, *The Untenable Case for Perpetual Dual-Class Stock*, 103 Va. L. Rev. 585 (2017); Robert J. Jackson Jr., Comm’r, U.S. Sec. & Exch. Comm’n, 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; Petition from Council of Institutional Inv’rs to Elizabeth King, Chief Regulatory Officer, Intercontinental Exch. Inc. (Oct. 24, 2018), https://www.cii.org/files/issues\_and\_advocacy/correspondence/2018/20181024%20NYSE%20Petition%20on%20Multiclass%20Sunsets%20FINAL.pdf. [↑](#footnote-ref-67)
67. See, e.g., Zohar Goshen & Assaf Hamdani, Corporate Control and Idiosyncratic Vision, 125 Yale L.J. 560, 567 (2016). [↑](#footnote-ref-68)
68. For early work raising the claim that dual-class stock facilitates long-term planning, see George W. Dent, Jr., Dual Class Capitalization: A Reply to Professor Seligman, 54 Geo. Wash. L. Rev. 725, 748 (1986), and Daniel R. Fischel, Organized Exchanges and the Regulation of Dual Class Common Stock, 54 U. Chi. L. Rev. 119, 137–38 (1987). *See also* Steven Davidoff Solomon, *Shareholders Vote with Their Dollars to Have Less of a Say*, N.Y. Times: DealBook (Nov. 4, 2015), http://www.nytimes.com/2015/11/05/business/ dealbook/shareholders-vote-with-their-dollars-to-have-less-of-a-say.html (“Many defend dual-class stock because it may insulate a company from pressure to take short-term actions at the behest of shareholders.”). [↑](#footnote-ref-69)
69. Vijay Govindarajan , Shivaram Rajgopal , Anup Srivastava and Luminita Enache, *Should Dual-Class Shares Be Banned?*, HBR (Dec. 3, 2018) ( “A dual-class structure, offering immunity against proxy contests initiated by short-term investors, could be optimal if it enables founder-managers to ignore pressures from the capital markets and avoid myopic actions such as cutting research and development and delaying corporate restructuring.”). *See also* Bernard S. Sharfman, *The Undesirability of Mandatory Time-Based Sunsets in Dual Class Share Structures: A Reply to Bebchuk and Kastiel*, 93 S. Cal. L. Rev. Postscript 1 (2019); David J. Berger, *Dual-Class Stock and Private Ordering: A System That Works*, Harv. L. Sch. F. on Corp. Governance & Fin. Reg. (May 24, 2017), <https://corpgov.law.harvard.edu/2017/05-24/dual-class-stock-and-private-ordering-a-system-that-works/>. [↑](#footnote-ref-70)
70. <https://ceoworld.biz/2021/10/12/best-ceos-2021/>; https://www.businessinsider.com/best-ceos-past-30-years-2011-7#some-men-are-born-great-some-achieve-greatness-22 [↑](#footnote-ref-71)
71. [add cross reference to Part III] [↑](#footnote-ref-72)
72. <https://money.cnn.com/quote/shareholders/shareholders.html?symb=TSLA&subView=institutional>; [↑](#footnote-ref-73)
73. Cite sources that explain rising CEO pay by the competition for talents. [↑](#footnote-ref-74)
74. One exception is the discussion by Guhan Subramanian [↑](#footnote-ref-75)
75. Tesla, Inc. (TSLA), yahoo! finance, https://finance.yahoo.com/quote/TSLA/ [https://perma.cc/9YAH-JA83] (last accessed December 9, 2021). [↑](#footnote-ref-76)
76. https://www.forbes.com/lists/innovative-leaders/#3610349f26aa [↑](#footnote-ref-77)
77. *In re* Tesla Motors, Inc., 2020 Del. Ch. LEXIS 51, 2020 WL 553902 (Del. Ch. Feb. 4, 2020). [↑](#footnote-ref-78)
78. See Panasonic CEO Says Tesla's Elon Musk a "Genius' who Can Be "Overly Optimistic', Reuters (last updated July 7, 2020, 12:00 PM), https://www.reuters.com/article/us-panasonic-tesla-idUSKBN2482BF [https://perma.cc/Y5XT-A82T]. [↑](#footnote-ref-79)
79. <https://www.mccarter.com/insights/teslas-stock-option-grant-to-elon-musk-part-2-new-york-law-journal/> (quoting Ed Kim, vice president of industry analysis at AutoPacific, and noting that "Mr. Musk is a visionary leader of Tesla and Tesla very much depends on his outstanding talents in the design, production and marketing of Tesla vehicles"). [↑](#footnote-ref-80)
80. *In re* Tesla Motors, Inc., 2020 Del. Ch. LEXIS 51, 2020 WL 553902 (Del. Ch. Feb. 4, 2020). [↑](#footnote-ref-81)
81. *Id.* [↑](#footnote-ref-82)
82. *Id.* [↑](#footnote-ref-83)
83. https://www.theguardian.com/technology/2018/sep/07/tesla-chief-elon-musk-smokes-marijuana-on-live-web-show [↑](#footnote-ref-84)
84. <https://www.cnbc.com/2018/10/29/teslas-elon-musk-says-his-tweet-that-led-to-a-20-million-fine-was-worth-it.html>; http://fortune.com/2018/10/01/tesla-shares-soar-musk-sec-settlement/. [↑](#footnote-ref-85)
85. *Id.* [↑](#footnote-ref-86)
86. Nicole Sperling, [*Long Before ‘Netflix and Chill', He Was the Netflix C.E.O*](https://www.dropbox.com/home/Superstar%20CEOs?preview=Sperling%2C+Nicole%2C+Long+Before+%E2%80%98Netflix+and+Chill%2C%E2%80%99+He+Was+the+Netflix+C.E.O.%2C+New+York+Times+(Online).pdf)*.* **New York Times**. 15.09.2019. [↑](#footnote-ref-87)
87. *Id.* [↑](#footnote-ref-88)
88. [Number of Netflix paid subscribers worldwide from 3rd quarter 2011 to 3rd quarter 2020](https://www.statista.com/statistics/250934/quarterly-number-of-netflix-streaming-subscribers-worldwide/), **Statista**. 16.11.2020. [↑](#footnote-ref-89)
89. Initially Netflix tried to divide the subscription into DVDs and streaming, which caused the subscription price to increase. This decision, led by Hastings himself, caused 800,000 subscribers to leave in just few months. Hastings had to pull back his idea and apologies to Netflix's costumers. *See* [Rani Molla and Peter Kafka, *How one of Netflix’s biggest mistakes helped build its culture,*](https://www.dropbox.com/home/Superstar%20CEOs?preview=Rani+Molla+and+Peter+Kafka%2C+How+one+of+Netflix%E2%80%99s+biggest+mistakes+helped+build+its+culture%2C+Vox.pdf)**Vox.** 23.06.2020. [↑](#footnote-ref-90)
90. For example, Hastings treats his employees as members of a pro sports team, which means they should expect to be replaced by better performers for their spot if Netflix can find them ([*Netflix Shows How to Build a Winning Culture*](https://www.dropbox.com/home/Superstar%20CEOs?preview=Netflix+Shows+How+to+Build+a+Winning+Culture%2C+The+Spectator.pdf)*.* **The Spectator.** 19.09.2020); When an employee is fired, the reasons for his dismissal are emailed to the whole staff (Todd Spangler, [*Reed Hastings on New Book, Netflix’s Future and One of His Toughest "Keeper Tests",*](https://www.dropbox.com/home/Superstar%20CEOs?preview=Todd+Spangler%2C+Reed+Hastings+-++Netflix+Future%2C+Hardest+Keeper+Test%2C+Lessons+From+Book%2C+Variety.pdf)**Variety.** 07.09.2020); Any employee can access confidential information, and executives seal multimillion-dollar deals without the approval of top brass ([*The Hastings doctrine: Can Reed Hastings preserve Netflix’s culture of innovation as it grows?*](https://www.dropbox.com/home/Superstar%20CEOs?preview=The+Hastings+doctrine+-+Can+Reed+Hastings+preserve+Netflix%E2%80%99s+culture+of+innovation+as+it+grows%2C+The+Economist.pdf) **The Economist.** 12.09.2020); and High-achieving employees are rewarded with the highest salaries in the business (Brandon Katz, [*Netflix CEO Reed Hastings Explains Why His Company Pays So Well*](https://www.dropbox.com/home/Superstar%20CEOs?preview=Katz+Brandon%2C+Netflix+CEO+Reed+Hastings+Explains+Why+His+Company+Pays+So+Well%2C+The+New+York+Observer.pdf)*,* **The New York Observer.** 21.09.2020). [↑](#footnote-ref-91)
91. Nicole Sperling, [*Long Before ‘Netflix and Chill', He Was the Netflix C.E.O*](https://www.dropbox.com/home/Superstar%20CEOs?preview=Sperling%2C+Nicole%2C+Long+Before+%E2%80%98Netflix+and+Chill%2C%E2%80%99+He+Was+the+Netflix+C.E.O.%2C+New+York+Times+(Online).pdf)*.* **New York Times**. 15.09.2019. [↑](#footnote-ref-92)
92. [*The Hastings doctrine: Can Reed Hastings preserve Netflix’s culture of innovation as it grows?*](https://www.dropbox.com/home/Superstar%20CEOs?preview=The+Hastings+doctrine+-+Can+Reed+Hastings+preserve+Netflix%E2%80%99s+culture+of+innovation+as+it+grows%2C+The+Economist.pdf) **The Economist.** 12.09.2020. [↑](#footnote-ref-93)
93. *See* Nicole Sperling, [*Long Before ‘Netflix and Chill', He Was the Netflix C.E.O*](https://www.dropbox.com/home/Superstar%20CEOs?preview=Sperling%2C+Nicole%2C+Long+Before+%E2%80%98Netflix+and+Chill%2C%E2%80%99+He+Was+the+Netflix+C.E.O.%2C+New+York+Times+(Online).pdf)*.* **New York Times**. 15.09.2019; [Rani Molla and Peter Kafka, *How one of Netflix’s biggest mistakes helped build its culture,*](https://www.dropbox.com/home/Superstar%20CEOs?preview=Rani+Molla+and+Peter+Kafka%2C+How+one+of+Netflix%E2%80%99s+biggest+mistakes+helped+build+its+culture%2C+Vox.pdf)**Vox.** 23.06.2020. [↑](#footnote-ref-94)
94. [Add a cross reference to below] [↑](#footnote-ref-95)
95. *Id.* [↑](#footnote-ref-96)
96. *Cf* the sources in supra note 43.  [↑](#footnote-ref-97)
97. https://www.usatoday.com/story/tech/2021/07/05/amazon-ceo-jeff-bezos-leaving-andy-jassy/7847643002/ [↑](#footnote-ref-98)
98. Jeffrey Dastin, Arjun Panchadar, *Jeff Bezos keeps Amazon voting power in divorce settlement,* REUTERS (April 4, 2019, 8:31 PM)<https://www.reuters.com/article/us-people-bezos/jeff-bezos-keeps-amazon-voting-power-in-divorce-settlement-idUSKCN1RG2CI>; https://www.ndtv.com/world-news/jeff-bezos-leaves-enduring-legacy-as-he-steps-away-as-amazon-ceo-2478759 [↑](#footnote-ref-99)
99. Amazon.com, Inc. (AMZN), https://finance.yahoo.com/quote/AMZN/ (last accessed December 9, 2021). *See also* https://companiesmarketcap.com/. [↑](#footnote-ref-100)
100. Brian Sozzi, *Why Amazon CEO Jeff Bezos' departure would be bad news for investors*, YAHOO (May 30, 2019) <https://finance.yahoo.com/news/why-amazon-ceo-jeff-bezos-departure-would-be-bad-news-for-investors-181555666.html> [↑](#footnote-ref-101)
101. *Id* [↑](#footnote-ref-102)
102. James Mackintosh*, Where Bezos Leads, Amazon Shareholders Blindly Follow,* WALL ST. J. (June 22, 2017 8:16 pm) <https://www.wsj.com/articles/where-bezos-leads-amazon-shareholders-blindly-follow-1498147966> (discussing Bezos' ability to launch the big takeover of Whole Foods without offering any strategic or financial rationale. [↑](#footnote-ref-103)
103. See Table 1. [↑](#footnote-ref-104)
104. *Id.* [↑](#footnote-ref-105)
105. https://www.ndtv.com/world-news/jeff-bezos-leaves-enduring-legacy-as-he-steps-away-as-amazon-ceo-2478759 [↑](#footnote-ref-106)
106. *See*, Ulrike Malmendier & Geoffrey Tate, *Superstar CEOs*, 124 Q.J. Econ. 1593 (2009); Manuel Ammann, Philipp Horsch & David Oesch, *Competing with Superstars* 62 Management Science, 2842 (2016); Thomas David, Alberta Di Giuli & Arthur Petit-Romec, *CEO Reputation and Corporate Voting* (working paper, 2020). [↑](#footnote-ref-107)
107. *See*, e.g., Finkelstein, S., *Power in top management teams: dimensions, measurement, and validation*, Academy of Management Journal, 35, 505, 509-512 (1992); Adams, Renée B., Heitor Almeida, and Daniel Ferreira, *Powerful CEOs and Their Impact on Corporate Performance*, 18.4 The Review of Financial Studies 1403, 1404-1409 (2005). [↑](#footnote-ref-108)
108. *See, e.g.,* Ian C. Macmillan, Robin Siegel & P.N. Subba Narasimha, *Criteria Used by Venture Capitalists to Evaluate New Venture Proposals*, 1 J. Bus. Ventur. 119 (1985) (Using a questionnaire to determine the most important criteria that a sample of one hundred VCs use to decide on funding new ventures, and finding that the quality of the entrepreneur ultimately determines the funding decision); Francesco Ferrati & Moreno Muffatto, *Reviewing equity investors’ funding criteria: a comprehensive classification and research agenda*, 23 Venture Cap. 157 (2021) (conducting a literature review of the studies that assess criteria used by equity investors in their funding decision-making process, and finding that in many studies (25) the key element in the valuation concerns is the characteristics of the entrepreneurial team). [↑](#footnote-ref-109)
109. *See, e.g.,* David H. Hsu, *Experienced entrepreneurial founders, organizational capital, and venture capital funding*, 36 Rsch. Pol'y 722 (2007) (using a dataset of 149 early-stage start-ups, and finding that prior founding experience (especially financially successful experience) increases the likelihood of VC funding); Tarek Miloud, Arild Aspelund & Mathieu Cabrol, *Startup valuation by venture capitalists: an empirical study*, 14 Venture Cap. 151 (2012). [↑](#footnote-ref-110)
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113. See, e.g., Bradley E. Hendricks & Travis Howell, *The Founder Premium Revisited* (working paper, 2021). For a theoretical analysis of the negative impact of the time dimension of the costs of dual-class shares, *see* Lucian A. Bebchuk & Kobi Kastiel, *The Untenable Case for Perpetual Dual-Class Stock*, 103 Va. L. Rev. 585 (2017). For subsequent empirical studies on the topic, which tested and confirmed this economic prediction see Bebchuk & Kastiel, *The Perils of Small-Minority Controllers*, *supra* note 4, at 1458. [↑](#footnote-ref-114)
114. Haveman, H. A., & Khaire, M. V, *Survival beyond succession? The contingent impact of founder succession on organizational failure,*19 Journal of Business Venturing 437 (2004). [↑](#footnote-ref-115)
115. See, e.g., Morten Bennedsen, Francisco Pérez‐González, and Daniel Wolfenzon, *Do CEOs Matter? Evidence from Hospitalization Events* J. Fin. (forthcoming 2020); Dirk Jenter, Egor Matveyev, & Lukas Roth, *Good and bad CEOs* (working paper, 2019). *See also* Combs, J.G., Ketchen, D.J., Jr, Perryman, A.A. and Donahue, M.S. (2007), *The Moderating Effect of CEO Power on the Board Composition–Firm Performance Relationship Journal of Management Studies*, 44: 1299-1323 (finding that shareholders mourned the deaths of high-power CEOs whose boards were outside director dominated). [↑](#footnote-ref-116)
116. *See* Jenter et al., *id.*; John R. Graham et al., *CEO-Board Dynamics* 1, 35 (working paper, 2019). [↑](#footnote-ref-117)
117. Marianne Bertrand & Antoinette Schoar, *Managing with Style: The Effect of Managers on Firm Policies*, 118 Q. J. Econ. 1169 (2003) (finding evidence consistent with managerial ‘style’ affecting corporate policies and performance); Kenny Phua, Tham T. Mandy, Chishen Wei, *Are overconfident CEOs better leaders? Evidence from stakeholder commitments*, 127 J. of Fin. Econ. 519 (2018). [↑](#footnote-ref-118)
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119. *Id.* [↑](#footnote-ref-120)
120. Keivan Aghasia, Massimo G. Colombob & Cristina Rossi-Lamastra, *Post-Acquisition Retention of Target Founder-CEOs: Looking Beneath the Surfac*, 57 Journal of Management Studies 2101(2021) (also showing that "when the target firms are mature… the fact that the target CEO is one of the firm’s founders does not influence post- acquisition retention"). [↑](#footnote-ref-121)
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122. *See* Rakesh Khurana, *The Curse of the Superstar CEO*, 80 Harv. Bus. Rev. 60 (2002); John Gapper, *Superstar Chief Executives Can Self Destruct*, Fin. Times (Aug. 29, 2018). [↑](#footnote-ref-123)
123. Tang, Jianyun, Mary Crossan, and W. Glenn Rowe, *Dominant CEO, Deviant Strategy, and Extreme Performance: The Moderating Role of a Powerful Board*, 48.7 Journal of Management Studies 1479, 1480-81 (2011). [↑](#footnote-ref-124)
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126. *See, e.g.,* Agrawal A., Chadha, S., *Corporate Governance and Accounting Scandals*., 48 J. LAW ECON. 371, 403 (2005); William J. Donoher, *Firm Founders, Boards, and Misleading Disclosures: An Examination of Relative Power and Control*, 21(3) JOURNAL OF MANAGERIAL ISSUES 309, 314 (2009); Patricia M. Decchow, Richard G. Sloan, Amy P. Sweeney, *Causes and Consequences of Earnings Manipulations: An Analysis of Firms Subject to Enforcement Actions by the SEC*, 13 CONTEMP. ACCOUNT. RES. 1, 1 (1996). [↑](#footnote-ref-127)
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128. *Key-person Risk Is Alive and Kicking in Global Business*, The Economist (Nov. 22, 2018), https://www.economist.com/business/2018/11/22/key-person-risk-is-alive-and-kicking-in-global-business (key-person risk occurs when an individual’s presence, absence or behavior disproportionately affects a firm’s value”). [↑](#footnote-ref-129)
129. Steve Blank, *Why Visionary CEOs Never Have Visionary Successors*, Harv. Bus. Rev. (Oct. 8, 2016), https://hbr.org/2016/10/why-visionary-ceos-never-have-visionary-successors. [↑](#footnote-ref-130)
130. For a notable exception, Guhan Subramanian, *Deal Process Design in Management Buyouts*, 130 HARV. L. REV. 590, 619-23 (2016) (hereinafter: Subramanian, *Deal Process Design*) (discussing the impact of valuable management). [↑](#footnote-ref-131)
131. [**add a cross reference**] [↑](#footnote-ref-132)
132. The founder status and his significant equity stake which amounted to 22% in the past was one of the reasons underlying the court’s holding that Musk controlled Tesla. [**Add a cross reference**]. [↑](#footnote-ref-133)
133. See Table 1 above. [↑](#footnote-ref-134)
134. *Id.* [↑](#footnote-ref-135)
135. See, e.g., Zohar Goshen & Assaf Hamdani, *Corporate Control and Idiosyncratic Vision*, 125 YALE L.J. 560, 566-67 (2016) (discussing the importance of enabling a talented founder to freely implement her strategy and utilize her skills to produce superior returns). For empirical evidence on the impact of talented founder on firm value, see, e.g., Renée B. Adams, Heitor Almeida & Daniel Ferreira, *Powerful CEOs and Their Impact on Corporate Performance*, 18 The Review of Financial Studies 1403 (2005). See also [add a cross reference to the above-mentioned studies]. [↑](#footnote-ref-136)
136. [add cross reference to the empirical studies below] [↑](#footnote-ref-137)
137. There is also a link between founder statues and dual class shares that enable founder to retain control for a long period of time. [See recent study by Ofer Eldar et al.] [↑](#footnote-ref-138)
138. [Add reference from Facebook public filings.] [↑](#footnote-ref-139)
139. Even Larry Ellison, who held a relatively large equity stake of 25%, could not exercise a full control over the company he lost the vote on compensation… so it's still contestable] [↑](#footnote-ref-140)
140. [reference to the relevant public filing on Edgar]. [↑](#footnote-ref-141)
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142. Walter Isaacson, Steve Jobs 186-206 (2011); Randal Lane, *John Sculley*

*Just Gave His Most Detailed Account Ever of How Steve Jobs Got Fired from Apple*,

FORBES (Sept. 9, 2013), http://www.forbes.com/sites/randalllane/2013/09/09/john-sculley

-just-gave-his-most-detailed-account-ever-of-how-steve-jobs-got-fired-from-apple [↑](#footnote-ref-143)
143. See, e.g., <https://www.barrons.com/articles/barrons-top-ceos-2020-jpmorgan-chases-jamie-dimon-51593218399>; <https://fortune.com/2020/05/15/most-admired-fortune-500-jamie-dimon-ceo-daily/>; https://ceo-na.com/executive-interviews/one-of-a-kind/. [↑](#footnote-ref-144)
144. https://www.nbcnews.com/business/autos/can-renault-nissan-alliance-survive-without-carlos-ghosn-n1120166 [↑](#footnote-ref-145)
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148. https://www.nbcnews.com/business/autos/can-renault-nissan-alliance-survive-without-carlos-ghosn-n1120166*.* [↑](#footnote-ref-149)
149. https://www.foxnews.com/entertainment/cbs-chief-les-moonves-steps-down-amid-sexual-misconduct-allegations [↑](#footnote-ref-150)
150. https://www.washingtonpost.com/news/arts-and-entertainment/wp/2018/07/27/who-is-leslie-moonves-the-cbs-chief-executive-under-investigation-after-allegations-of-misconduct/ [↑](#footnote-ref-151)
151. *Id.* [↑](#footnote-ref-152)
152. https://www.latimes.com/business/hollywood/la-fi-ct-moonves-severance-investigation-20181129-story.html. [↑](#footnote-ref-153)
153. See, e.g., Renée B. Adams, Heitor Almeida & Daniel Ferreira. "Powerful CEOs and Their Impact on Corporate Performance." The Review of Financial Studies 18.4 (2005): 1403, 1419. [↑](#footnote-ref-154)
154. *Id.* [↑](#footnote-ref-155)
155. https://conferenceboard.esgauge.org/ceosuccession/dashboard/ceoprofile/1/5. [↑](#footnote-ref-156)
156. Add cross reference. [↑](#footnote-ref-157)
157. Humphery-Jenner, Mark & Islam, Emdad & Rahman, Lubna & Suchard, Jo-Ann. (2017). Moderating Powerful CEOs through Improved Governance. SSRN Electronic Journal. 10.2139/ssrn.3090783. [↑](#footnote-ref-158)
158. *Id.* [↑](#footnote-ref-159)
159. https://www.cnbc.com/2021/06/16/microsoft-ceo-satya-nadella-will-also-become-chairman-of-the-board.html. [↑](#footnote-ref-160)
160. **[add a basic reference]** [↑](#footnote-ref-161)
161. Add a cross reference to above. [↑](#footnote-ref-162)
162. The notion that successful CEOs gain leverage over boards was noted by Hermalin & Weisbach. They use this insight to explain why CEOs might have a say on director appointment. *See* Benjamin E. Hermalin & Michael S. Weisbach, *Endogenously chosen boards of directors and their monitoring of the CEO*, 88 Am.Econ. Rev.96, 97 (1998) (“If a CEO keeps his job, then retaining him must be worth more to the directors than replacing him. This means that this CEO is, to some extent, a rare commodity, which gives him bargaining power vis-a-vis the directors. He is, therefore, able to bargain for a board that is more favorable to him”). [↑](#footnote-ref-163)
163. [**Cite**] [↑](#footnote-ref-164)
164. For example, Afra Afsharipour & J. Travis Laster, Enhanced Scrutiny on the Buy-Side, 53 Ga. L. Rev. 443 (2019) (arguing that for a regime that would encourage public companies to subject decisions to acquire other companies to a shareholder vote). [↑](#footnote-ref-165)
165. [↑](#footnote-ref-166)
166. [**Add reference**] [↑](#footnote-ref-167)
167. [**Add reference to the database + on ISS**] [↑](#footnote-ref-168)
168. [to add source] [↑](#footnote-ref-169)
169. [to add source] [↑](#footnote-ref-170)
170. [**Add cross reference**] [↑](#footnote-ref-171)
171. https://www.hollywoodreporter.com/business/business-news/netflix-shareholders-reject-plan-split-710445/ [↑](#footnote-ref-172)
172. Amol Sharma and Joann S Lublin, [*Netflix Shareholders Vote Down Proposal to Split CEO and Chairman Positions*,](https://www.dropbox.com/home/Superstar%20CEOs?preview=Sharma%2C+Amol%3B+Lublin%2C+Joann+S%2C+Netflix+Shareholders+Vote+Down+Proposal+to+Split+CEO+and+Chairman+Positions%2C+Wall+Street+Journal.pdf) **Wall Street Journal.** 10.06.2014. [↑](#footnote-ref-173)
173. https://www.hollywoodreporter.com/business/business-news/netflix-shareholders-reject-plan-split-710445/ [↑](#footnote-ref-174)
174. [**Add reference to the database.**] These proposals were related to matters such as declassifying staggered boards, adopting majority voting, adopting proxy access, reducing supermajority requirements. [↑](#footnote-ref-175)
175. Kobi Kastiel & Yaron Nili, *The Giant Shadow of Corporate Gadflies*, 94 S. Cal. L. Rev. 569, 575 (2021). [↑](#footnote-ref-176)
176. [**add reference to the dataset**]. [↑](#footnote-ref-177)
177. https://www.marketwatch.com/story/netflix-investors-losing-patience-say-company-ignores-them-on-governance-11623257126 [↑](#footnote-ref-178)
178. *Id.* [↑](#footnote-ref-179)
179. *Id.* [add cross reference to above] [↑](#footnote-ref-180)
180. Add reference to the dataset. [↑](#footnote-ref-181)
181. [↑](#footnote-ref-182)
182. Note, this is different from the finding that shareholder say-on-pay votes are determined by the company’s performance. *See* Jill E. Fisch, Darius Palia, and Steven Davidoff Solomon, *Is Say on Pay All About Pay? The Impact of Firm Performance* 8 Harv. Bus. L. Rev. 101 (2018). [↑](#footnote-ref-183)
183. [↑](#footnote-ref-184)
184. <https://courts.delaware.gov/Opinions/Download.aspx?id=270420>; data from Voting Analytics [↑](#footnote-ref-185)
185. *Id.* [↑](#footnote-ref-186)
186. https://www.forbes.com/sites/robinferracone/2018/02/26/oracles-road-to-moving-the-needle-on-say-on-pay-votes/?sh=420f8ee1348a [↑](#footnote-ref-187)
187. https://papers.ssrn.com/sol3/papers.cfm?abstract\_id=3551223 [↑](#footnote-ref-188)
188. https://papers.ssrn.com/sol3/papers.cfm?abstract\_id=3551223 [↑](#footnote-ref-189)
189. [**add a cross reference to the example of Oracle / Tesla cases in which the court relied upon it to determine that directors lacked independence**.] [↑](#footnote-ref-190)
190. [add a cross reference to the Pappa John] [↑](#footnote-ref-191)
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192. 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, 1052-55, 1067 (2010); Ronald W. Masulis, Cong Wang & Fei Xie, *Agency Problems at Dual-Class Companies*, 64 J. FIN. 1697, 1697 (2009). For additional review of the empirical evidence, see Bebchuk and Kastiel, *The Perils of Small Minoirty Controllers*, at 1471-73. These studies focus dual-class companies, though their implication on the incentives generated by large equity stake are relevant also to single-class firms. [↑](#footnote-ref-193)
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199. Kirsch, *Id.* See also Racial Slur Leads to Papa John's Founder Quitting Chairman Post, *supra* note [\_\_]. [↑](#footnote-ref-200)
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201. Tiffany Hsu*, Papa John's Adopts 'Poison Pill' Defense Against Hostile Takeover by Its Founder***,** N.Y.TIMES **(**July 24, 2018), <https://www.nytimes.com/2018/07/23/business/papa-johns-john-schnatter-poison-pill.html> [↑](#footnote-ref-202)
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203. Papa John's Founder Will Not 'Go Quietly' as Company Tries to Push Him away, *supra* note 13. [↑](#footnote-ref-204)
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233. Cross reference from above. [↑](#footnote-ref-234)
234. *See* Goshen & Hamdani (2016). [↑](#footnote-ref-235)
235. Add cross reference to above. Moreover, despite the increasing popularity of a time-cased sunset clause, many dual-class firms still avoid adopting it at the IPO stage. For example, 26% of the dual-class IPOs had time-based sunsets in 2017. This number increased to 32-33% in the two subsequent years, and to 47% in 2020 and to 51% in the first half of 2021. Still, despite investors overwhelming support of sunset provisions, a significant fraction of the dual-class IPOs do not include sunset provisions. https://www.cii.org/files/2020%20IPO%20Update%20Graphs%20.pdf [↑](#footnote-ref-236)
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240. Cross reference to the relevant section. [↑](#footnote-ref-241)
241. *See* Elizabeth Polman, *Startup Governance*. 168 U. Pa. L. Rev. 155, 203-206 (2019). Pollman offers another explanation that is more in line with our view. She argues that startup directors may fail to exercise oversight because they emphasize growth and profits over compliance. *id.* at 202. [↑](#footnote-ref-242)
242. Add cross reference to the examples. [↑](#footnote-ref-243)
243. Although in case the CEO also holds a relatively large (but non-controlling) equity stake, such holding might make it more difficult to oust the CEO. [↑](#footnote-ref-244)
244. Ann Lipton, *The Three Faces of Control*, The Business Lawyer (forthcoming, 2022), at 3 (“[U]nder Delaware doctrine, a single label – controlling shareholder – carries an enormous amount of legal weight”) (hereinafter: Lipton, *Three Faces of Control*). [↑](#footnote-ref-245)
245. *Id.*, at 9-10. Voigt v. Metcalf, No. 2018-0828-JTL, 2020 Del. Ch. LEXIS 55, at \*28-9 (Ch. Feb. 10, 2020). [↑](#footnote-ref-246)
246. Lipton, *Three Faces of Control*, *supra* note 244, at 11 (“Unlike other interested transactions, when the transaction concerns a controlling shareholder, business judgment review cannot be restored by the approval of the disinterested and independent directors or the disinterested (minority) shareholders”). The law on the application of the entire fairness standard to transaction other than freezout mergers is somewhat unclear. For the view that virtually all self-dealing transactions with a controlling shareholder are subject to the entire fairness standard, *see* Vice Chancellor Laster’s opinion in *In re* EZCORP Inc. Consulting Agreement Derivative Litig., 2016 WL 301245, at \*12-15 (Del. Ch. Jan. 25, 2016) (**describe type of transactions).** See also Ams. Mining Corp. v. Theriault, 51 A.3d 1213, 1239 (Del. 2012). For recent cases supporting this approach, see Berteau v. Glazek, C.A. No. 2020-873-PAF, 2021 Del. Ch. LEXIS 141 (Del. Ch. June 30, 2021 (**same)**); In re Tilray, Inc. Reorganization. Litig., C.A. No. 2020-0137-KSM, 2021 Del. Ch. LEXIS 111, at \*31 (Del. Ch. June 1, 2021). For criticism, *see* Lawrence A. Hammermesh, Jack B. Jacobs & Leo E. Strine, Jr., *Optimizing the World’s Leading Corporate Law: A 20-Year Retrospective and Look Ahead* 27-28, 34-37 (U. Penn. Working Paper, 2021) (hereinafter: Hammermesh, Jacobs & Strine) ("we never understood that entire fairness review would be universally required in these common situations, or that the potential for controller self-dealing makes it impossible for the company’s directors to avoid a judicial fairness inquiry. Rather, if one of the traditional cleansing techniques is used… the business judgement rule would apply"). [↑](#footnote-ref-247)
247. In re MFW S’holders Litig., 67 A.3d 496, 499 (Del. Ch. 2013), aff’d sub nom. M&F Worldwide Corp., 88 A.3d 635 (Del. 2014). See also Lipton, *Three Faces of Control*, *supra* note 244, at 11-12 (noting that so far the Delaware Supreme Court has only approved the use of MFW procedures for cleansing transformative transactions, such as freezeouts, but Chancery Courts have used it to cleanse additional types of conflicted transactions, involving a controlling shareholder). [↑](#footnote-ref-248)
248. *See*, *e.g.*, In re PNB Holding Co. S'holders Litig., 2006 Del. Ch. LEXIS 158, 2006 WL 2403999, at \*9 (Del. Ch. Aug. 18, 2006) ("Under our law, a controlling stockholder exists when a stockholder… owns more than 50% of the voting power of a corporation"); Williamson v. Cox Communs., Inc., 2006 Del. Ch. LEXIS 111, 2006 WL 1586375, at \*4 (Del. Ch. June 5, 2006) ("A shareholder is a 'controlling' one if she owns more than 50% of the voting power in a corporation"). [↑](#footnote-ref-249)
249. Hammermesh, Jacobs & Strine, *supra* note 246, at 40. [↑](#footnote-ref-250)
250. Most notably, one decision found a 35% shareholder (close to 40% taking into account stock options and shares held by family members) qualified as the controlling shareholder. *See Cysive* [\_\_] at 552) (“The conclusion that Carbonell possesses the attributes that the Lynch doctrine is designed to address is reinforced when one takes into account the fact that Carbonell is Chairman and CEO of Cysive, and a hands-on one, to boot. He is, by admission, involved in all aspects of the company's business, was the company's creator, and has been its inspirational force.”). But see Hammermesh, Jacobs & Strine, *supra* note 246, at 35-36 (explaining that he controlled approximately 40% of the votes, and that the court’s reasoning remained deeply tied to voting, not just managerial power). [↑](#footnote-ref-251)
251. *Id*, at 35-36 (explaining that "[u]nder Delaware law, it was historically difficult to establish that a stockholder having less than majority ownership was a controlling stockholder" and that "courts have focused on voting rather than managerial power"). [↑](#footnote-ref-252)
252. *Id.* at 35-37 (explaining that court rulings after Cysive "have been cautious in determining that a minority holder with a significant role in the company was a controller" and providing examples of several rulings between 2000 and 2015, which demonstrate this point. The authors also note that "[a]lthough that finding [in the Tesla case] may have been appropriate, we are concerned that the court’s reasoning in applying controlling stockholder doctrine sweeps too broadly"). For a different view and comprehensive analysis and review of cases concerning the definition of control Ann M. Lipton, *After Corwin: Down the Controlling Shareholder Rabbit Hole*, 72 Vand. L. Rev. 1977, 1987-2005 (2019). [↑](#footnote-ref-253)
253. *In re* Tesla Motors, Inc., 2020 Del. Ch. LEXIS 51, 2020 WL 553902 (Del. Ch. Feb. 4, 2020). At the time of the acquisition, Musk held about 22% of SolarCity voting power. [↑](#footnote-ref-254)
254. *Id.*, at 57-8 ("the Complaint pleads sufficient facts to support a reasonable inference that Musk exercised his influence as a controlling stockholder with respect to the Acquisition"). [↑](#footnote-ref-255)
255. *Id.*, at 37 ("[b]ecause I agree the Complaint pleads facts that allow reasonable inferences that Musk was a controlling stockholder and that Plaintiffs’ claims against all Defendants are subject to entire fairness review"). [↑](#footnote-ref-256)
256. *Id.*, at 48-9. [↑](#footnote-ref-257)
257. Hammermesh, Jacobs & Strine, *supra* note 246, at 37. [↑](#footnote-ref-258)
258. *See*, for example, Basho Techs. Holdco B, LLC v. Georgetown Basho Invs., LLC, No. CV 11802-VCL, 2018 WL 3326693, at \*27 (Del. Ch. July 6, 2018), aff'd sub nom. Davenport v. Basho Techs. Holdco B, LLC, 221 A.3d 100 (Del. 2019) (noting that “the ability to exercise outsized influence in the board room, such as through high-status roles like CEO, Chairman, or founder” is one of the indicia of control); FrontFour Cap. Grp. LLC v. Taube, No. CV 2019-0100-KSJM, 2019 WL 1313408, at \*24 (Del. Ch. Mar. 11, 2019) (status as founder listed among indicia of control). In a recent ruling Vice Chancellor Laster provides a comprehensive analysis of the various factors that could *collectively* support a reasonable pleading-stage inference of control: the ability to designate directors; block size; voting rights and restrictions in stockholders agreements; *the roles that an alleged controller or its representatives play in the boardroom*; the existence of relationships between the alleged controller and the key managers or advisors who play a critical role in providing directors with information with repsect to the transaction at stake). *See* Voigt v. Metcalf, No. 2018-0828-JTL, 2020 Del. Ch. LEXIS 55, at \*32-33 (Del. Ch. Feb. 10, 2020). In that case though the shareholder held 35% of the votes. For an earlier case *see*, *In re* Zhongpin Inc. S'holders Litig, 2014 WL 6735457, at \*7 (Del. Ch. Nov. 26, 2014) (viewing a CEO with 17.3% as exercising significant influence that amounts into actual control. In that case though the CEO and the buyout group owned together approximately 26% of the votes). [↑](#footnote-ref-259)
259. *See* Lipton, *Three Faces of Control*, *supra* note 244, at 13-17. [↑](#footnote-ref-260)
260. Another explanation focuses on the threat of retribution by controlling shareholders against minority shareholders. *See*, *Id*, at 12. For a review and criticism of this rationale *see* Hammermesh, Jacobs & Strine, *supra* note 246, at 15-22. [↑](#footnote-ref-261)
261. *See* *supra* Part I. [↑](#footnote-ref-262)
262. Kobi Kastiel & Yaron Nili, *Competing for Votes*, 10 Harv. Bus. L. Rev. 287, 312-314, 319-312 (2020) (providing evidence to the willingness of shareholders to vote against directors and reviewing related literature). [↑](#footnote-ref-263)
263. *See* Bebchuk & Hamdani, *Independent Directors*, *supra* note 2, at *(XX)*; J. Travis Laster, *The Effect of Stockholder Approval on Enhanced Scrutiny*, 40 Wm. Mitchell L. Rev. 1443, 1460 (2014) (“The controller’s influence also undercuts the independence of otherwise independent and disinterested directors, because the controller has the power to determine whether those individuals will remain directors”). [↑](#footnote-ref-264)
264. Lipton, *The Three Faces of Control*, at 13 (“[C]ourts might also consider whether certain founders or CEOs are so closely identified with the company that it would be nearly unthinkable to oust them”). [↑](#footnote-ref-265)
265. See *supra* Section [\_]. [↑](#footnote-ref-266)
266. *See*, *e.g.*, *In re* Loral Space and Commc'ns Inc., 2008 WL 4293781, at \*73 (Del. Ch. Sep. 19, 2008) ([w]ith 36% of the votes, MHR hardly feared a proxy fight, and although it did not have the power to unilaterally vote in charter changes or effect a merger, it had substantial blocking power"). *See* also Hammermesh, Jacobs & Strine, *supra* note 246, at 35-36. [↑](#footnote-ref-267)
267. *See, for example,* the analysis in OTK Associates, LLC v. Friedman (Delaware Chancery Court, C.A. No. 8447-VCL) (February 5, 2014). [↑](#footnote-ref-268)
268. See *supra* Section [\_]. [↑](#footnote-ref-269)
269. For the general concern about independent directors' dependence on the controller for continued service at the company, *see, e.g.,* Bebchuk & Hamdani, *Independent Directors*, *supra* note 2, at 1274. Hammermesh, Jacobs & Strine, however, argue that directors at controlled companies may be motivated to constrain controlling shareholders by their desire to maintain their reputation and get shareholder support in their nomination in other companies, *see* Hammermesh, Jacobs & Strine, *supra* note 246, at 34. [↑](#footnote-ref-270)
270. *See* *supra* Section [\_]. [↑](#footnote-ref-271)
271. *See also* Hammermesh, Jacobs & Strine, *supra* note 246, at 32 ("[a]ppraising a company sold in a conflicted merger with no market test is difficult enough; judicial pricing of compensation packages plans is unmoored in standards that would make any exercise of discretion reviewable in any coherent and consistent way"). [↑](#footnote-ref-272)
272. *See* Goshen & Hamdani, *The Limits of Judicial Review*, *supra* note 4, at 961-74. [↑](#footnote-ref-273)
273. *Id*, at 978-980. *See also* Itai Fiegenbaum, *The Controlling Shareholder Enforcement Gap*, 56 AM. BUS. L.J. 583, 589-92 (2019); Edward B. Rock, *Majority of the Minority Approval in a World of Active Shareholders*, *in* The Law and Finance of Related Party Transactions 105, 115 (Luca Enriques & Tobias Tröger eds., 2019). For an extension of the MFW protections to non-freezeouts transactions, *see* IRA Tr. Bobbie Ahmed v. Crane (NRG Yield), C.A. No. 12742-CB, 2017 WL 6335912 (Del. Ch. Dec. 11, 2017); *In re* Tesla Motors, Inc. Stockholder Litig., C.A. No.12711-VCS, 2018 WL 1560293 (Del. Ch. Mar. 28, 2018). [↑](#footnote-ref-274)
274. For example, Musk's compensation package was approved by 73% of shareholders of Tesla, who were unaffiliated with the company management (see *supra* notes **שגיאה! הסימניה אינה מוגדרת.**, and accompanying text), and about 60% of the holders of Tesla outstanding shares voted in favor of the SolarCity acquisition. *See* *Tesla Motors*, 2018 WL 1560293, at \*26 (Del. Ch. Mar. 28, 2018). Plaintiffs contended that the company made misleading disclosure in connection with the acquisition and that certain mutual funds who held equity positions in both Tesla and SolarCity should have been excluded from the vote tally, as they are allegedly not "disinterested" in the vote due to this cross-ownership. *Id.* We do not address the merit of these arguments, but for noting that "Delaware law does not generally inquire into the motivations of non-controlling shareholders when they are exercising their voting rights." *See* Jill Fisch, Assaf Hamdani & Steven Davidoff Solomon, *The New Titans of Wall Street: A Theoretical Framework for Passive Investors*, 168 U. Pa. L. Rev. 17, 68-69 (2019). [↑](#footnote-ref-275)
275. *See* Dell Inc., Definitive Proxy Statement (Schedule 14A), at XX (May 31, 2013). [↑](#footnote-ref-276)
276. Matthew D. Cain and Steven M. Davidoff, *Form Over Substance? The Value of Corporate Process and Management Buy-Outs*, 36 Del. J. Corp. L. 849 (2011) (hereinafter: Cain & Davidoff); [\_\_] Predatory MBOs, at 1305 (“In contrast to their inside counterparts, outside directors are not full-time employees of the target and thus must rely primarily on management for information”). [↑](#footnote-ref-277)
277. Predatory MBOs, page 1301. [↑](#footnote-ref-278)
278. Cite Cain & Davidoff, *supra* note 276, at [\_\_] (\_\_\_\_). [↑](#footnote-ref-279)
279. Cite Delaware General Corporation Law, Section 262. [↑](#footnote-ref-280)
280. Cite [one of the papers on the appraisal debate] [↑](#footnote-ref-281)
281. *See* Union Ill. 1995 Inv. Ltd. P'shipv. UnionFin. Grp., Ltd., 847 A.2d 340, 358 (Del. Ch. 2004) (merger price is indicative of fair value when it “resulted from a competitive and fair auction, which followed a more-than adequate sales process and involved the broad dissemination of confidential information to a large number of prospective buyers.") [↑](#footnote-ref-282)
282. *Id.* [↑](#footnote-ref-283)
283. *In re* Appraisal of Dell Inc., No. 9322-VCL, 2016 WL 3186538, at \*22 (Del. Ch. May 31, 2016). [↑](#footnote-ref-284)
284. *Id*.,at 1. [↑](#footnote-ref-285)
285. Dell, Inc. v. Magnetar Glob. Event Driven Master Fund Ltd, 177 A.3d 1, 6 (Del. 2017); *See* Charles Korsmo & Minor Myers*, The Flawed Corporate Finance of Dell and DFC Global,* 68 Emory L. J. 221, 251 (2018) (“[A]t the end of the day, the Supreme Court simply saw nothing wrong with the sales process"). [↑](#footnote-ref-286)
286. The Supreme Court remanded the case, and the parties settled thereafter. *In re* Appraisal of Dell Inc., No. 9322-VCL, 2018 WL 2939448 at \*1 (Del.Ch. June 11, 2018). [↑](#footnote-ref-287)
287. *In re* Appraisal of Dell Inc., No. 9322-VCL, 2016 WL 3186538, at \*44 (Del. Ch. May 31, 2016). [↑](#footnote-ref-288)
288. Dell, Inc. v. Magnetar Global Event Driven Master Fund Ltd., 177 A.3d 1, 34 (Del. 2017). [↑](#footnote-ref-289)
289. Subramanian, *Deal Process Design*, *supra* note 130, at 621. [↑](#footnote-ref-290)
290. *Id.*, at 631-47. [↑](#footnote-ref-291)
291. Cite DFC DE case; Lawrence A. Hamermesh & Michael L. Wachter, *Finding the Right Balance in Appraisal Litigation: Deal Price*, *Deal* Process, and Synergies, 73 Bus. L. 961 (2018) (**find page)** [↑](#footnote-ref-292)
292. Another complicating factor is related to whether CEO's threat to leave the company is a credible one and whether it can produce this value at another venture. CEO who founded a company may be reluctant to leave it just before an exit, and if she does so and the value of the company would go down, this does not mean that the CEO would enjoy this lost value elsewhere. [literature on asset-specific investments]. Hart & Moore, Property Rights and Theory of the Firm [↑](#footnote-ref-293)
293. Note: cases where the court adopted a deferential approach when special committees were empowered to control CEO conflicts. For example, *In re* Plains Exploration & Production Company Stockholder Litig., 2013 WL 1909124 (Del. Ch. May 9, 2013); Teamsters Local 237 Welfare Fund. v. AstraZenca Pharmaceuticals LP, 136 A.3d 688 (Del. 2016); Additional Sec. Benefit Fund v. Caruso [↑](#footnote-ref-294)
294. Subramanian, *Deal Process Design*, *supra* note 130, at 622-23. [↑](#footnote-ref-295)
295. Albert H. Choi & Eric Talley, *Appraising the "Merger Price" Appraisal Rule*, 34 J. L. Econ. & Org. 543 (2018); Jonathan Macay & Joshua Mitts, Asking the Right Question: The Statutory Right of Appraisal and Efficient Markets (Eur. Corp. Gov. Inst. Working Paper, Law Working Paper No. 428/2018, 2018). [↑](#footnote-ref-296)
296. Predatory MBOs at 1320 (“The presence of management as a potential acquiror of the target may chill third-party bidding if external bidders perceive a heightened risk of being unable to consummate a transaction that does not involve management participation”). [↑](#footnote-ref-297)
297. Subramanian, *Deal Process Design*, *supra* note 130, at 620. And at 621 (“Management does not have an obligation to work with third-party bidders, but when management chooses not to do so (either implicitly or explicitly), and when management is valuable, a market canvass process is no longer a useful mechanism for price discovery.”) [↑](#footnote-ref-298)
298. We note that this claim assumes that potential bidders include only private equity funds that critically depend on incumbent managers to run the target. Strategic buyers (other companies) and private equity funds that have their own vision about the target’s strategy might value the company regardless of its existing leadership. Kobi's verson: In some situations, however, strategic buyers—and perhaps even private equity buyers—may have different plans for the company as well. In those cases, existence of powerful controller might have little impact, if at all, on the pricing as well as on the effectiveness of the auction. [↑](#footnote-ref-299)
299. Subramanian, *Deal Process Design*, *supra* note 130, at 639 (“In order to mitigate the information-asymmetry problem and the valuable-management problem, boards should insist on cooperation agreements from management as a condition for considering an MBO.”) Yet, the board cannot force managers to cooperate with all potential buyers. *See* Guhan Subramanian & Annie Zhao, *Go-Shops Revisited*, 133 Harv. L. Rev. 1215, 1242 (2020)(hereinafter: Subramanian & Zhao) (“if the CEO is important to the ongoing value of the enterprise, no go-shop bidder would want to partner with a reluctant CEO”). [↑](#footnote-ref-300)
300. See Brian J. Broughman, *CEO Side Payments in Mergers and Acquisitions*, at 76 (2017). [↑](#footnote-ref-301)
301. *Id* at 82 (“[S]ide payments arise more often in settings where the CEO's loss of private benefits creates heightened incentives to otherwise block the merger”). [↑](#footnote-ref-302)
302. Subramanian & Zhao, *supra* note 299, at 1274 (2020) (“Forming a special committee, and making sure that it functions well, would be an important inoculation against defective sell-side processes.”) [↑](#footnote-ref-303)
303. For a review, *see* https://papers.ssrn.com/sol3/papers.cfm?abstract\_id=3544978. [↑](#footnote-ref-304)
304. Cite Ringe, https://papers.ssrn.com/sol3/papers.cfm?abstract\_id=3958960

See, e.g., https://papers.ssrn.com/sol3/papers.cfm?abstract\_id=3798101; <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3630480>). [↑](#footnote-ref-305)
305. https://papers.ssrn.com/sol3/papers.cfm?abstract\_id=3798101; https://papers.ssrn.com/sol3/papers.cfm?abstract\_id=3630480) [↑](#footnote-ref-306)
306. Oliver Hart & Luigi Zingales, *Companies Should Maximize Shareholder Welfare Not Market Value*, J.L. Fin. & Acct. 247 (2017). [↑](#footnote-ref-307)
307. See, e.g., Michal Barzuza, Quinn Curtis, & David H. Webber, *The Millennial corporation* (Working Paper, 2021); Kai; https://corpgov.law.harvard.edu/2021/05/29/shareholder-activism-and-esg-what-comes-next-and-how-to-prepare/]. [↑](#footnote-ref-308)
308. Compare Roe's view [https://papers.ssrn.com/sol3/papers.cfm?abstract\_id=3817788] to Barzuza et al., *id.* [↑](#footnote-ref-309)
309. This analysis is consistent with Lund and Polman view, which explains that "while some … institutional investors have begun to highlight the importance of stakeholder interests, there is no sign that they have abandoned the pursuit of long-term shareholder value." ESSAY: THE CORPORATE GOVERNANCE MACHINE, 121 Colum. L. Rev. 2563, 2591. [↑](#footnote-ref-310)
310. https://papers.ssrn.com/sol3/papers.cfm?abstract\_id=3551223 [↑](#footnote-ref-311)
311. Reference to the dataset. [↑](#footnote-ref-312)
312. https://papers.ssrn.com/sol3/papers.cfm?abstract\_id=2977219 [↑](#footnote-ref-313)
313. [https://papers.ssrn.com/sol3/papers.cfm?abstract\_id=3832698]. [↑](#footnote-ref-314)
314. Https://finance.yahoo.com/news/forget-activism-chronic-underperformance-big-000000083.html [↑](#footnote-ref-315)
315. *See* Genworth Financial, Inc. Consolidated Derivative Litigation (explaining the distinction between failure of oversight and causing the company to violate the law),. *See* DE new case. [↑](#footnote-ref-316)
316. In re Caremark Int’l Derivative Litig., 698 A.2d 959, 967 (Del. Ch. 1996). [↑](#footnote-ref-317)
317. See, e.g., Bainbridge (https://papers.ssrn.com/sol3/papers.cfm?abstract\_id=3899528); Shapira (https://papers.ssrn.com/sol3/papers.cfm?abstract\_id=3732838). [↑](#footnote-ref-318)
318. See Lund, https://papers.ssrn.com/sol3/papers.cfm?abstract\_id=3147130 [↑](#footnote-ref-319)
319. John Armour, Jeffrey Gordon & Geeyoung Min, *Taking Compliance Seriously*, 37 Yale J. Reg. 1, XX (2020) )XX( [↑](#footnote-ref-320)
320. See *supra* notes [\_\_], and accompanying text. [↑](#footnote-ref-321)
321. *See* Polman, *Startup Governance*, *supra* note [\_\_], at 203-206. [↑](#footnote-ref-322)
322. Langevoort & Sale, *supra* note 228 at [\_\_[]e [↑](#footnote-ref-323)
323. See Lund, supra note [\_\_] at <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3147130> [↑](#footnote-ref-324)
324. There is some evidence at the shareholder level—successful CEOs are more likely to get support by institutional investors on ESG-related shareholder proposals. See *supra* note \_\_, and accompanying text. [https://papers.ssrn.com/sol3/papers.cfm?abstract\_id=3551223] [↑](#footnote-ref-325)
325. See, e.g., https://papers.ssrn.com/sol3/papers.cfm?abstract\_id=894921. [↑](#footnote-ref-326)
326. *See* Pollman XX. See also Lund, supra note [\_\_] at 1662 (explaining that when the damage to a firm's value from losing an iconic CEO may be far less than the reputational consequences of a high-profile sexual harassment scandal, members of the board should terminate the CEO). [↑](#footnote-ref-327)