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Dual-Class Share Structure: A Challenge for Contemporary Corporate Law



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Dual-Class Share Structure: A Challenge for Contemporary Corporate Law

A share is a security of a joint-stock company. It confirms the contribution of a partner (shareholder) in the capital of a joint-stock company and legally establishes its holder's positions and rights. There are different classes of shares that differ from each other in terms of legal status. One of them entitles a shareholder to managerial control (i.e. common share) and the other does not and is limited to provide property rights only (i.e. preferred share).

According to the existing trend in the present world, large corporations are distinguished by a diverse capital structure i.e. they issue two (or more) classes of shares simultaneously: both common and preferred, as well as several classes of common shares with different voting rights. This is especially true for high-tech companies like Google, Facebook, Snap Inc., etc. They are called Dual-Class Companies. When a company issues shares of two or more classes, it is accompanied by great risks and difficulties. It causes differences of opinion among scholars and investors whether the issuance of different classes of shares is harmful or beneficial for a company. In general, why do corporations resort to this path? What positive or negative impact can classes of shares have on corporate governance? Also, what is the role of a shareholder in the management of a company? In the present paper, the named issues will be discussed; What approaches exist in countries with developed economies and what methods do they use to improve corporate governance.

Keywords: *Classes of shares, single-class share structure, dual-class share structure, "one share, one vote", corporate governance, "Sunset Provision", stock exchanges.*

1. Introduction

A dual-class share structure as a corporate governance mechanism has taken root in the present world, leading to differences of opinion among scholars and investors.

As of December 2021, 31.7% of the initial public offerings made on the leading US stock exchanges belonged to companies with a dual-class structure.¹

Given the current trend, large corporations, especially well-known high-tech companies such as Facebook², Google³, LinkedIn, Zoom, etc. choose the dual-class share structure. In addition to high-tech companies, a similar structure is popular with media companies (such as The New York Times Co., The Washington Post Co., Dow Jones & Co., News Corp.), and family-ow-

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¹ Ritter J. R., IPO Statistics for 2021 and Earlier Years, Table 23: Dual Class IPOs, by Tech and Non-tech, 1980-2021, University of Florida Warrington College of Business, 67, <<https://site.warrington.ufl.edu/ritter/files/IPO-Statistics.pdf>> [02.02.2022].

² Following the company's rebranding in October, 2021 Facebook CEO Mark Zuckerberg announced that the company's new name would be "Meta". However, for more clarity, in the present paper, the company will be referred to as "Facebook", <<https://about.fb.com/news/2021/10/facebook-company-is-now-meta/>> [09.03.2022].

³ Following a reorganization in 2015, the company was renamed Alphabet Inc. However, for more clarity, in the present paper, the company will be referred to as Google. See Sharma R., Why "Google" Became Alphabet, Investopedia, <<https://www.investopedia.com/articles/investing/081115/why-google-became-alphabet.asp>> [02.02.2022].

ned companies (such as Ford Motor Co., one of the largest automaker companies in the world, led by the Ford family). Warren Buffett's Berkshire Hathaway is also known for its dual-class structure.⁴

A dual-class structure involves the issuance of two (or more) classes of shares in which corporations place low voting or non-voting shares for public trade on stock exchanges. And, the shares with voting rights (be it superior voting or one voting) are not intended for public offerings and are owned only by the corporation's insiders (founders, executives).

Dual-class share structure develops a wedge between the voting and economic rights. Minority shareholders (usually the founders), even though they own a minority of the shares in the company and therefore their participation in the equity is small, retain the control of the company as they hold a majority of the votes. Thus, the voting right is not proportional to the cash-flow rights. This contradicts the universally accepted principle in corporate law – “one share = one vote”.

Dual class share structure is the result of flexible legislation. It is an issue of the day and can be considered as one of the major challenges in the contemporary corporate law. The Georgian reality is interesting against the background of this world trend.

On January 1, 2022, the new Law of Georgia on Entrepreneurs came into force. The adoption of the new law was aimed at improving the Georgian entrepreneurial legislation and bringing it closer to international standards. At the stage of development of entrepreneurial law, Georgia took the path to American law, as a result of which, according to national law, corporations enjoy freedom in terms of defining the capital structure.

National law recognizes two classes of shares – common shares and preferred shares, which can be considered as basic classes. However, the provision is of *dispositivum* nature in relation to the classes of shares and a company can otherwise determine the control or economic rights related to the classes of shares by the statute.⁵ However, in this respect Georgia is not distinguished by diverse practices. It is therefore interesting to consider examples from experienced countries.

The purpose of this paper is to discuss the matter of issuing shares of different classes, its significance and the reason why corporations apply this method. Also to consider the positive and negative impacts of the dual-class share structure on corporate governance; What benefits or difficulties can deviate from the basic rule bring?

It should be noted that the object of the research of this paper is a joint-stock company (a public company or corporation), which has a large number of shareholders, publicly trades its shares in the securities market and is responsible for transparency, accountability and disclosure.⁶

⁴ See Kang S. Y., Taking Voting Leverage and Anti-Director Rights More Seriously: A Critical Analysis of the Law and Finance Theory, Peking University School of Transnational Law Research Paper No. 15-3, 2015, 20, <<https://ssrn.com/abstract=2669420>> [02.02.2022].

⁵ According to the first sentence of Article 158 (1) of the Law of Georgia on Entrepreneurs “Unless otherwise provided for by the statute, shares may be common or preferred.” And according to Article 158 (4) of the given law “A joint-stock company may issue classes of shares other than those determined by this article.” Law of Georgia on Entrepreneurs, the official website of Legislative Herald of Georgia, 04/08/2021 (in Georgian).

⁶ Chanturia L., Corporate Governance and the Responsibility of Managers in Corporate Law, Tbilisi, 2006, 79 (in Georgian).

In Georgia, corporate governance is based on international experience. It is important to research and analyze current issues, experiences, trends, practices or dogmatic problems in the world in order to increase their practical relevance. The experience of corporate governance in the present world and the search for better models gives great hope for the introduction of sound corporate governance practices in the Georgian reality, for the improvement of the corporate governance culture, for the development of the securities market and for the further development of entrepreneurship.

2. First Dual-Class Companies

Dual-class share structure has recently become particularly popular with high-tech companies. However, it should be noted that the structure of this type is not new. The history of dual-class shares dates back to the 1920s. And, the first non-voting shares are found in the late 19th century.

In 1898, the International Silver Company was the first company to issue non-voting shares in the United States.⁷ It was this fact that laid the groundwork for the allocation of voting rights and cash flow rights by companies between common and preferred shares in the United States.⁸ Previously, both classes provided for voting rights.⁹

In the 1920s, companies began to successfully implement such a structure to attract additional investment. In 1925, the Dodge Brothers publicly traded non-voting common shares, bonds, and preferred shares on the New York Stock Exchange.¹⁰ The controlling shareholder in the company owned a majority of voting rights, despite a small portion of participation in the capital.¹¹ The practice of Dodge Brothers had been shared by other companies. The main reason why they implemented this mechanism, the companies named the following: the application of unequal voting rights helped them reduce agency costs and control the management in an era where there was no leverage to demand disclosure and the protection of the rights of small investors.¹² This was followed by criticism from Harvard University Professor William Z. Ripley.¹³ He believed that the rights of shareholders were being violated, while the management, despite the increase in capital and the increase in the number of investors, invariably retained control, without diluting

⁷ *Howell J. W.*, The Dual Class Stock Structure in the United States: A New Dataset and an Examination of Firms Who Leave the Structure, Ph.D. Dissertation, The University of Georgia, Athens, Georgia, 2010, 2, <https://getd.libs.uga.edu/pdfs/howell_jason_w_201005_phd.pdf> [03.02.2022].

⁸ Ibid.

⁹ Ibid.

¹⁰ See *Seligman J.*, Equal Protection in Shareholder Voting Rights: The One Common Share, One Vote Controversy, *George Washington Law Review*, Vol. 54, No. 5, 1986, 694-697, <<https://heinonline.org/HOL/LandingPage?handle=hein.journals/gwlr54&div=36&id=&page=>> [03.02.2022].

¹¹ See *ibid.*

¹² *Lund D. S., Pollman E.*, The Corporate Governance Machine, *Columbia Law Review*, Vol. 121, 2021, University of Pennsylvania, Institute for Law & Economics Research Paper No. 21-05, European Corporate Governance Institute - Law Working Paper No. 564/2021, USC CLASS Research Paper No. CLASS21-15, USC Law Legal Studies Research Paper Series No. 21-15, 2624, <<https://ssrn.com/abstract=3775846>> [05.02.2022].

¹³ See *Ripley W. Z.*, Main Street and Wall Street, 1927, <<https://archive.org/stream/mainstreetandwal00riplrich/djvu.txt>> [05.02.2022].

their voting rights.¹⁴ The New York Stock Exchange banned the listing of companies that offered non-voting common shares or more than one class of common shares, although exceptions were made for few companies (one of which was the Ford Motor Company).¹⁵ Since the 1980s, the New York Stock Exchange and the NASDAQ as well have again allowed the listing of shares by companies with a dual-class share structure.¹⁶

3. The Relevance of Dual-Class Shares

Since 2004, dual-class shares have become even more relevant when Google, in its initial public offering, offered common shares, which provided for one vote, while the shares that were held by the founders had superior voting rights (meaning that one share of the founders provided for ten votes). Technology companies tended to use less of a dual-class share structure. However, since Google, it has become conventional for other similar companies.¹⁷ Therefore, the revival of the dual-class shares and the establishment of a new trend for technology companies is associated with the name of Google.

When referred to dual-class shares, it is usually implicated the coexistence of two different classes of common share (e.g., shares with superior voting and standard (one) voting rights). However, in practice, we also encounter companies that issue more than two classes of common shares (i.e. Multi-Class Shares). For example, Snap Inc. was the first corporation to list only non-voting shares in the US stock market in March 2017 for public trading.¹⁸ Before Snap Inc. would become a reporting company i.e. before it became a public company, it had provided its shareholders with two classes of common shares. Earlier investors and executives owned common shares (one share = one vote), while the founders owned common shares with a superior voting rights (one share = ten votes).¹⁹ As mentioned above, until 2017, Snap Inc. was a private company. And in 2017, when it became a public company and listed its shares on the stock exchange, it offered its new, outside investors only common shares that did not provide for voting rights.

¹⁴ See *Lel U., Netter J. M., Poulsen A. B., Qin Zh.*, Dual Class Shares and Firm Valuation: Evidence from SEC Rule 19c-4, June 1, 2020, European Corporate Governance Institute – Finance Working Paper No. 807/2021, 7, <<https://ssrn.com/abstract=3729297>> [05.02.2022].

¹⁵ See *Gilson R. J.*, Evaluating Dual Class Common Stock: The Relevance of Substitutes, *Virginia Law Review*, Vol. 73, 1987, 807, <https://scholarship.law.columbia.edu/faculty_scholarship/987> [05.02.2022].

¹⁶ Committee On Capital Markets Regulation (CCMR), The Rise of Dual Class Shares: Regulation and Implications, Report, April 2020, 2, <<https://www.capmktreg.org/wp-content/uploads/2020/04/The-Rise-of-Dual-Class-Shares-04.08.20-1.pdf>> [05.02.2022].

¹⁷ See *Fisch J. E., Davidoff-Solomon S.*, The Problem of Sunsets, *Boston University Law Review*, Vol. 99, 2019, University of Pennsylvania, Institute for Law & Economic Research Paper No. 19-04, 1067-1068, <<https://ssrn.com/abstract=3305319>> [05.02.2022].

¹⁸ See *Sharfman B. S.*, A Private Ordering Defense of a Company’s Right to Use Dual Class Share Structures in IPOs, *Villanova Law Review*, Vol. 63, No. 1, 2018, 19-21, <<https://ssrn.com/abstract=2986164>> [05.02.2022].

¹⁹ *Descovich K., Conroy M. A., Dixon C., Odoner E.*, Voting Rights Gone in a Snap – Unequal Voting Rights Back in the Spotlight, Public Company Advisory Group of Weil, Gotshal & Manges LLP, Governance and Securities Alert, April 3, 2017, <<https://governance.weil.com/insights/voting-rights-gone-in-a-snap-unequal-shareholder-voting-rights-back-in-the-spotlight/>> [05.02.2022].

It is true that before Snap Inc., Google listed non-voting shares for public trade on the stock exchange in 2004.²⁰ However, the difference between these two cases is that Google did it during the secondary public offering, while Snap Inc. did it during the initial public offering. Despite all this, investors were very enthusiastic about Snap Inc.'s shares.²¹

Therefore, following the example of Snap Inc., it is also possible for a dual-class share structure to involve the issuance of three different classes of common shares²² - a) one share provides for one vote; b) one share provides for multiple votes; c) a share that does not provide for voting rights at all. However, it should be noted that this is a relatively new phenomenon.

4. The Right to Vote as a Mechanism of Control

There are two main aspects to corporate governance: investor ownership and delegated governance.²³

According to popular opinion expressed in the legal literature²⁴, the term “equity ownership” has two characteristics: 1. The right to a share in the income received from the entrepreneurial activity of the company; 2. The right to have a control over the company. The right of control basically means “the right of investors (shareholders) to elect directors and to vote to confirm major transactions.”²⁵ The control right, as well as the right to receive a share of the company's income or profits - the cash flow right, is proportional to the contribution in the capital of the company. It should be noted, however, that such allocation (based on the principle of proportionality) of control and share of profits is mainly regulated by provisions of laws governing corporations that have the character of *jus dispositivum*.²⁶

The highest body of a joint-stock company is the General Meeting of Shareholders. That is why it is entrusted to solve the main issues of the company's activities.²⁷

Voting right is one of the means of exercising management control by shareholders. Control over the management can be achieved through various combinations of voting rights, e.g. classification of common shares as voting and non-voting shares from which voting shares (or a major part of them) are held by company insiders.²⁸

²⁰ Ibid.

²¹ See *Sharfman B. S.*, A Private Ordering Defense of a Company's Right to Use Dual Class Share Structures in IPOs, *Villanova Law Review*, Vol. 63, No. 1, 2018, 19, <<https://ssrn.com/abstract=2986164>> [05.02.2022].

²² In the legal literature, this case, even though we are no longer dealing with two classes of shares but with three classes, is still referred to as a dual-class share structure, or possibly a multi-class share structure.

²³ See *Kraakman R., Armour J., Davies P., Enriques L., Hansmann H., Hertig G., Hopt K., Kanda H., Pargendler M., Ringe W.-G., Rock E.*, *The Anatomy of Corporate Law: A Comparative and Functional Approach*, 3rd ed., *Kochiashvili A., Maisuradze D. (Translators)*, Tbilisi, 2019, 74 (in Georgian) <http://lawlibrary.info/ge/books/2019giz-ge_anatomy_of_corporate_law.pdf> [05.02.2022].

²⁴ Ibid., 19.

²⁵ Ibid.

²⁶ Ibid.

²⁷ *Chanturia L., Ninidze T.*, *Commentary on the Law on Entrepreneurs*, Tbilisi, 2002, 348 (in Georgian).

²⁸ Ibid., 123.

The right of a shareholder to control is a powerful incentive for the existence of conscientious management. The duty of constant accountability of management deprives the director and other executives of the ability to express their arbitrariness.²⁹

Within a dual-class structure, the shareholder gains influence not at the expense of owning a majority of the shares but at the expense of owning a majority of the votes. Consequently, it is possible for a shareholder to hold a majority of the votes, despite a small portion of participation in the capital. Those who hold majority of votes impose a financial burden on those who do not. Financial risk for those who own a minority of votes are higher. This is what causes a negative attitude towards the dual-class share structure.

The main reason why companies apply a dual class share structure is to maintain control in a narrow circle as the company expands.

The original owners of companies want to raise capital, expand, but are reluctant to cede control. When a private company becomes a public company, that is, it becomes a “reporting company”³⁰, it means that it has to place the shares for public trading on the stock exchange i.e. new co-owners are entering the company, with whom both control and ownership must be allocated. The company, wants to expand and increase capital i.e. agrees to split ownership but disagrees to split control rights. That is why it offers non-voting shares or common shares (one share = one vote) to outside investors and retains multi-vote shares (usually one share = ten votes) for its insiders. Such an approach is typical for media companies to maintain their editorial independence, as well as for high-tech companies and family-owned companies. Also important is the following: A dual-class share structure is particularly prevalent in founder-led companies, when the company is associated with their founder.

However, different cases have also been observed in practice: it should be noted that not all dual-class companies are the same. Although the legal literature views dual-class companies primarily as a single monolithic “type” in which control is concentrated in a narrow circle of founders, in reality, the nature of control varies in different dual-class companies.³¹ In particular, the controlling shareholders may also be directors or managers who are not the founders of the company;³² Also, the controlling shareholder may be a parent company or a holding company that

²⁹ *Lazarashvili L.*, Shareholders’ rights to control the receipt of information and the duty of care, in *Collected Articles: Duty of care and responsibility in the joint-stock company under Georgian and German law: Symposium Materials, II German-Georgian Symposium in Corporate Law*, Tbilisi, 2003, 263-264 (in Georgian), <<http://www.library.court.ge/upload/giz2003-ge-de-symposium-company-law.pdf>> [05.02.2022].

³⁰ According to Article 9 (1) of the Law of Georgia on Securities Market, “A reporting company (issuer of publicly held securities) is a legal person established under the Law of Georgia on Entrepreneurs, which has issued publicly held securities (except for covered bonds).” *Law of Georgia on Securities Market*, Legislative Herald of Georgia, 1(8), 14/01/1999 (in Georgian).

³¹ *Aggarwal D., Eldar O., Hochberg Y. V., Litov L. P.*, The Rise of Dual-Class Stock IPOs (November 23, 2021), NBER Working Paper 28609; Duke Law School Public Law & Legal Theory Series No. 2020-78, European Corporate Governance Institute – Finance Working Paper No. 806/2021, 3, <<https://ssrn.com/abstract=3690670>> [06.02.2022].

³² For example, in Skysat Communications Network, which became a public company in 1994, the controlling stake was owned by directors and managers who were not the company’s founders. See *ibid.*, 11.

has issued shares in its subsidiary;³³ The family that headed the company for generations, or even Private Equity Investors, who chose this structure to retain control of the company even after the initial public offering (IPO). In addition, sometimes a dual class structure is chosen not for the maintenance of control but for regulatory and tax purposes.³⁴

5. Peculiarities of Dual-Class Share Structure

The class and number of securities issued by the corporation determines the formation of the capital.³⁵

Whether the corporation decides to issue only preferred shares, only common shares or different classes of common shares, it affects not only the capital structure, but also the corporate governance.³⁶

Under German law, dual-class shares are not allowed for listed companies.³⁷ That is why when discussing the issuance of shares of different classes by a corporation under German law, the simultaneous issuance of common and preferred shares is meant.³⁸ Georgian corporate law, similar to American corporate law, is not aware of such a prohibition, and therefore, the resolution of this issue is entrusted to the company itself. Therefore, the second case mentioned above (division of common shares into separate classes) is found in countries whose law does not prohibit the issuance of multi-vote shares. The dispositive (discretionary) norm of the Law of Georgia on Entrepreneurs regarding the legal definition of classes of shares allows for the establishment of a different rule. It is possible to issue both multi-vote shares and shares with restricted voting rights.

However, some scholars believe that dual-class share structure is different from that of the capital structure, which provides for both the common shares and the preferred shares.³⁹ The reason is the different economic rights of the common share compared to the preferred one, as well as different control rights (one provides for voting right, the other – does not). Holders of preferred share typically have limited or no voting rights, but in return enjoy economic benefits in

³³ For example, when the fast food chain Chipotle became a reporting company in 2006 (that is, a public company that publicly traded its shares on a stock exchange), the controlling stake was not owned by Steve Eells, its founder, but by McDonald's subsidiary company. McDonald's owned a multi vote shares: it owned 87% of the vote while there was a 22% wedge between the voting rights and the stake in the capital. See *ibid*.

³⁴ *Ibid*.

³⁵ *Burduli I.*, Foundations of the Corporate Law, Vol. I, Tbilisi, 2010, 341 (in Georgian).

³⁶ *Ashton D. C.*, Revisiting Dual Class Stock, Saint John's Law Review, Vol. 68, 1994, 866, <<https://scholarship.law.stjohns.edu/lawreview/vol68/iss4/2/>> [06.02.2022].

³⁷ *Burduli I.*, Foundations of the Corporate Law, Vol. I, Tbilisi, 2010, 336 (in Georgian).

³⁸ See *Rydqvist K.*, Dual-Class Shares: A Review, Oxford Review of Economic Policy, Vol. 8, No. 3, 1992, 46, <www.jstor.org/stable/23606245> [06.02.2022].

³⁹ Compare *Kang S. Y.*, Taking Voting Leverage and Anti-Director Rights More Seriously: A Critical Analysis of the Law and Finance Theory, Peking University School of Transnational Law Research Paper No. 15-3, 2015, 21, <<https://ssrn.com/abstract=2669420>>. see also, *Fisch J. E.*, *Davidoff-Solomon S.*, The Problem of Sunsets, Boston University Law Review, Vol. 99, 2019, University of Pennsylvania, Institute for Law & Economic Research Paper No. 19-04, 1064, <<https://ssrn.com/abstract=3305319>> and *Rydqvist K.*, Dual-Class Shares: A Review, Oxford Review of Economic Policy, Vol. 8, No. 3, 1992, 46, <www.jstor.org/stable/23606245>.

the form of dividends and liquidation. A preferred share is considered a hybrid of share and bond. In addition, if the preferred shares are rarely issued by companies (rarely sold to investors), then it cannot be used by insiders who want to gain a superior position by voting rights.⁴⁰

In the United States, under §6.01 (a) - (c) of the MBCA (Model Business Corporation Act)⁴¹, as well as Title 8, §151 (a), §212 (a) of the Delaware Code⁴² and also if we take into account the practice of public companies, it is possible to differentiate common shares according to the scope of voting and economic rights. Common shares can be further divided into separate “classes” e.g. one share of Class A provides one vote, while one share of Class B provides ten votes. There may also be a third class of common share (Class C) that does not provide voting rights at all, even though it is a common share.

Dual-class structure is permitted by the laws of many countries. These include Canada, Denmark, Finland, the Netherlands, Sweden and Switzerland.⁴³ At the same time, the laws of some countries restrict or prohibit the use of a dual-class structure by public companies. Belgium, Germany, Luxembourg, Poland and Spain restrict the use of a dual-class structure.⁴⁴ It should be noted that in Germany, a division of common shares into multi-voting and non-voting shares is generally prohibited. Therefore, the structure of dual-class shares in this sense is not only limited but also inadmissible in Germany.

6. The Positive Impact of Dual-Class Share Structure

Proponents of the dual-class share structure believe that this structure enables company insiders to focus on their long-term vision for the company. The founders (or executives) know better the purpose and the aim of the company. Therefore, they know the means of accomplishing the goals. Their focus is not solely on making a profit, but they also want to expand the company. It is important for them that the company withstands time and is able to cope with present-day challenges. This requires special knowledge. That is why the proponents of a dual-class share structure believe that entrusting the founders to manage the company and protecting them from the investors with short-term incentives, as well as protecting them from the capital market pressure, will bring the most optimal results.

Often, the vision of the founder is incomprehensible and unacceptable to investors, although it is beneficial for the company. A dual-class structure is a kind of a tool to isolate (insulate) the

⁴⁰ Kang S. Y., Taking Voting Leverage and Anti-Director Rights More Seriously: A Critical Analysis of the Law and Finance Theory, Peking University School of Transnational Law Research Paper No. 15-3, 2015, 21, <<https://ssrn.com/abstract=2669420>> [02.02.2022].

⁴¹ Model Business Corporation Act, 2016 Revision, December 9, 2017, American Bar Association, <https://www.americanbar.org/content/dam/aba/administrative/business_law/corplaws/2016_mbca.au_thecheckdam.pdf> [10.03.2022].

⁴² The Delaware Code, Title 8: Corporations, Legislative Council, General Assembly State of Delaware, the Delaware Code Online, <<https://delcode.delaware.gov/title8/title8.pdf>> [10.03.2022].

⁴³ See *Bebchuk L. A., Kastiel K.*, The Untenable Case for Perpetual Dual-Class Stock (April 18, 2017), Virginia Law Review, Vol. 103, 2017; Harvard Law School John M. Olin Center Discussion Paper No. 905, Harvard Law School Program on Corporate Governance Discussion Paper 2017-6, 599, <<https://ssrn.com/abstract=2954630>> [06.02.2022].

⁴⁴ Ibid.

founder and the management from the people (the investors) who question the founder's vision.⁴⁵ In this regard, it is interesting to note the initial public offering letter from the founders of Google to investors, which explains why they decided to adopt a dual-class share structure when their company became public.⁴⁶ In addition to focusing on their long-term plans, innovative approach, technology and business environment specifics, they emphasize that "Google has prospered as a private company. We believe a dual class voting structure will enable Google, as a public company, to retain many of the positive aspects of being private."⁴⁷ Indeed, when a public company uses a dual-class share structure, it does take the characteristics of a private company as most of the voting rights that can have influence, or in other words the control rights, are concentrated in a narrow circle of shareholders.

Dual-class share structure ensures the protection of "Idiosyncratic Vision"⁴⁸ the Entrepreneur has for the development of the company. Typically, founders have their own goals and plans. They may have long-term plans and developed mechanisms to implement those plans, and that is why they need to be protected from the pressure from investors who have only economic interests and want short-term returns.

Professors Zohar Goshen and Assaf Hamdani point out in their paper⁴⁹ that the purpose of using a dual-class structure is for the entrepreneur to maintain unrestricted and inevitable control over the corporation. In their view, investors and entrepreneurs both value (consider of great importance) the right to control, however, for different reasons. An entrepreneur must maintain control in order to carry out her/his plan, follow her/his vision, and investors want to reduce agency costs.⁵⁰

The information asymmetry between the ordinary market participant (meaning outside investor) and the company insider, can have a negative impact on the value of the share.⁵¹ It is expected that someone will take advantage of it and come to the head of the company at unreasonably low costs.⁵² It is a case of the hostile takeover of the enterprise, against which a dual-class share structure is considered to be one of the most effective mechanisms. Hostile takeover is a

⁴⁵ See *Fisch J. E., Davidoff-Solomon S.*, The Problem of Sunsets, Boston University Law Review, Vol. 99, 2019, University of Pennsylvania, Institute for Law & Economic Research Paper No. 19-04, 1069, <<https://ssrn.com/abstract=3305319>> [05.02.2022].

⁴⁶ See *Page L., Brin S.*, 2004 Founders' IPO Letter <<https://abc.xyz/investor/founders-letters/2004/ipo-letter.html>> [05.02.2022].

⁴⁷ See *ibid.*

⁴⁸ The term "Idiosyncratic Vision", used by professors Zohar Goshen and Assaf Hamdani, is interesting to point out. Idiosyncratic means peculiar or individual. The professors, as they explain themselves, do not consider the entrepreneur's vision to be innovative or any new discovery, the main thing is for her/him to have a business plan and the belief that this plan will bring success to her/his company. This is what is meant by this word. See *Goshen Z., Hamdani A.*, Corporate Control and Idiosyncratic Vision, Yale Law Journal, Vol. 125, 2016, 567, <<https://www.yalelawjournal.org/article/corporate-control-and-idiosyncratic-vision>> [04.02.2022].

⁴⁹ See *Goshen Z., Hamdani A.*, Corporate Control and Idiosyncratic Vision, Yale Law Journal, Vol. 125, 2016, <<https://www.yalelawjournal.org/article/corporate-control-and-idiosyncratic-vision>> [04.02.2022].

⁵⁰ See *ibid.*, 566.

⁵¹ See *Dimitrov V., Jain P. C.*, Recapitalization of One Class of Common Stock into Dual-Class: Growth and Long-Run Stock Returns, September 1, 2004, 2, <<https://ssrn.com/abstract=422080>> [04.02.2022].

⁵² *Ibid.*

case where one company (the acquiring company) acquires the other company (the target company) by negotiating directly with the shareholders, bypassing the management (board of directors).⁵³ During hostile takeovers, such a transaction is against the will of the management of the target company. This is why the acquiring company is trying to achieve its goal by convincing shareholders. The purpose of hostile takeover is to establish control over the target company by the acquiring company, which can only be achieved by obtaining an adequate number of voting shares. Dual-class structure is an effective mechanism for protecting a company from hostile takeover. At a time like this, the company has publicly traded common shares (one share, one vote) or non-voting shares, and the multi-voting shares or controlling shares are owned by a narrow circle of the company and therefore the acquiring company will not be able to establish control over the target company.

In the legal literature, regarding the advantages and disadvantages of issuing shares of different classes by corporations, whether it is a discussion of dual-class or multi-class share structures, there are more or less similar views with both proponents and opponents. In this respect, the paper⁵⁴ by Professor Dorothy S. Lund is different, offering a novel perspective on the above-mentioned debate. It is also important to note that the professor discusses the issue in the light of US experience and the legal and business environment.

In her paper, Professor Lund discusses specifically the benefits of a non-voting share and how it can be used to improve corporate governance of a company. According to Professor Lund, the key is in the shareholders themselves: who owns the share and what interest does she/he have. Shareholders are different and not everyone has the same motive. Non-voting share allows companies to allocate voting rights between informed shareholders (to whom their voting rights are of great importance) and uninformed, “weakly motivated” shareholders (who do not give much importance to their voting rights), and when such sorting occurs, agency and transaction costs are reduced.⁵⁵ In the legal literature, the prevailing view is that dual-class share structure increases agency costs. However, Professor Lund argues that by issuing non-voting shares, a company will reduce its agency costs. She believes that informed investors will pay more in voting shares that will not be diluted by the voting rights of uninformed, weakly motivated investors.⁵⁶ A company can persuade informed investors to make an investment by offering them two classes of shares, and weakly motivated investors will seek out shares that do not impose on them the costs associated with voting.⁵⁷ Moreover, non-voting shares can be purchased at a discount, unlike voting shares.

Voting rights are not equally important for all shareholders. Some of them do not appreciate it to the extent that they do not use it at all. Professor Lund considers such to be retail or individual investors. Voting right is important for informed investors who are motivated to maximize the

⁵³ See *Chanturia L.*, *Corporate Governance and the Responsibility of Managers in Corporate Law*, Tbilisi, 2006, 231 (in Georgian).

⁵⁴ See *Lund D. S.*, *Nonvoting Shares and Efficient Corporate Governance*, *Stanford Law Review*, Vol. 71, 2019, <<https://www.stanfordlawreview.org/print/article/nonvoting-shares-and-efficient-corporate-governance/>> [04.02.2022].

⁵⁵ *Ibid.*, 695-697.

⁵⁶ *Ibid.*

⁵⁷ *Ibid.*

value of the company.⁵⁸ Non-voting shares should be issued by the company precisely because those who value voting should have the relevant share, and those who do not value it should have the non-voting one.⁵⁹

When potential investors are convinced that management is accountable to informed investors, who hold voting shares, they are more likely to want to invest in such a company.⁶⁰ The issuance of non-voting shares, for the reason that voting power is divided between informed and weakly motivated investors (the informed have the voting shares and the others do not) has not yet taken place and the professor hopes that it will happen soon in the future.⁶¹

By giving the non-voting shares to weakly motivated voters, the company will give more power to the voice of informed investors and, to some extent, management will be more accountable to them.⁶²

Professor Lund believes that the potential for non-voting shares has not yet been fully explored, even though the non-voting shares have been in use for more than a century. Innovation (meaning high-tech companies) is a novelty for a dual-class structure. Recent corporate governance trends and financial market changes have made the non-voting shares more attractive.⁶³ Shareholder activity has increased significantly: they have the opportunity and desire to intervene directly and discuss various corporate issues; The number of institutional investors as shareholders of a company has also increased.⁶⁴ Weakly motivated shareholders vote and exercise their voting rights, and their lack of information suggests that their contributions may not necessarily be beneficial for the company. Thus, Professor Lund believes that non-voting shares are a good way to avoid suboptimal decisions.⁶⁵

7. The Negative Impact of Dual-Class Share Structure

The ISS (Institutional Shareholder Services group of companies)⁶⁶ described dual-class share structure as an “autocratic model of corporate governance”.⁶⁷

⁵⁸ See *Lund D. S.*, Nonvoting Shares and Efficient Corporate Governance, *Stanford Law Review*, Vol. 71, 2019, <<https://www.stanfordlawreview.org/print/article/nonvoting-shares-and-efficient-corporate-governance/>> [04.02.2022].

⁵⁹ Ibid.

⁶⁰ See *ibid.*, 698.

⁶¹ See *ibid.*

⁶² In this regard, it is interesting to note the example discussed by Professor Lund. She compared the specifics of the operation of companies with a single-class share structure and a dual-class share structure. See *Lund D. S.*, Nonvoting Shares and Efficient Corporate Governance, *Stanford Law Review*, Vol. 71, 2019, 719-723, <<https://www.stanfordlawreview.org/print/article/nonvoting-shares-and-efficient-corporate-governance/>> [04.02.2022].

⁶³ See *ibid.*, 737.

⁶⁴ Ibid.

⁶⁵ Ibid.

⁶⁶ Institutional Shareholder Services group of companies (ISS) - Institutional Shareholder Services Group is one of the leading shareholder advisory groups in the world. Provides consulting services in areas such as: corporate governance, investment solutions, capital market analysis, etc. It is also a “Proxy Firm” which means that it is authorized by companies and participates in general meetings of shareholders as their representative (proxy voting). See <<https://www.issgovernance.com/about/about-iss/>> [30.04.2020].

Institutional investors do not support a dual-class structure. They argue that the concentration of control within a small group of shareholders reduces the value of the company. The majority of shareholders at this time are unable to exercise proper supervision and control over those accountable to them. Dual-class structure stimulates managers, directors to breach their fiduciary duties to shareholders and act not in the interests of the company but for their private benefits.⁶⁸

Dual-class share structure may be accompanied by a weakening of accountability of the management of the company to shareholders, an increase in agency costs⁶⁹, arbitrariness on the part of controlling (holding majority of voting shares) shareholders - these are the most frequently discussed issues in the legal literature.

In general, the separation of ownership and control entails agency costs between shareholders and management, even within the single-class structure (where the “one share, one vote” principle is followed). But, within the dual-class share structure, since the right of control is concentrated in a narrow circle of shareholders, the accountability of the management to other, outside shareholders is also weakened. In addition, this may also result in agency costs between insider and outsider or majority and minority shareholders. This is why it is noted in the legal literature that the dual-class share structure leads to an increase in agency costs.

The main negative feature that characterizes a dual-class share structure is the powerlessness of the outside shareholders. When insiders fail to turn out to be good managers and their decisions fail, outside shareholders cannot use coercive and disciplinary mechanisms because they do not have adequate voting rights. In addition, the risk bearers of wrong decisions are the outside shareholders, because from an economic point of view, their equity shareholding is larger, and the insiders, in this case, do not suffer much because of the small share in the capital.

“Management Entrenchment” - as the majority of votes in the corporation are in the hands of insiders, minority shareholders or outside investors, are deprived of the opportunity to monitor the management. Consequently, it becomes difficult for them to demand accountability (e.g. impose disciplinary liability) from management. This in turn weakens management’s accountability to shareholders. On the one hand, management is committed to implementing its long-term plan. On the other hand, there is an increased risk of arbitrariness on their part.

In general, shareholders, including controlling shareholders, always try to protect themselves from the arbitrariness of managers, which manifests itself in the abuse of their position.⁷⁰

⁶⁷ See *Bebchuk L. A., Kastiel K.*, The Untenable Case for Perpetual Dual-Class Stock, April 18, 2017, *Virginia Law Review*, Vol. 103, 2017; Harvard Law School John M. Olin Center Discussion Paper No. 905; Harvard Law School Program on Corporate Governance Discussion Paper 2017-6, 599, <<https://ssrn.com/abstract=2954630>> [06.02.2022].

⁶⁸ See *Lund D. S.*, Nonvoting Shares and Efficient Corporate Governance, *Stanford Law Review*, Vol. 71, 2019, 714, <<https://www.stanfordlawreview.org/print/article/nonvoting-shares-and-efficient-corporate-governance/>> [04.02.2022].

⁶⁹ Agency Costs are the internal costs of the company, which provides for the remuneration of the representation made by the agent to the principal. These types of costs occur when a conflict of interest or disagreement arises between the shareholders and the management.

⁷⁰ *Jibuti M.*, State control over the protection of the interests of shareholders (investors) by the governing bodies of corporations, in *Collected Articles: Duty of care and responsibility in the joint-stock company under Georgian and German law: Symposium Materials, II German-Georgian Symposium in Corporate Law*, Tbilisi, 2003, 207 (in Georgian), <<http://www.library.court-ge/upload/giz2003-ge-de-symposium-company-law.pdf>> [05.02.2022].

On the other hand, it is important for minority shareholders to avoid embezzlement from controlling shareholders and to protect themselves from situations where management can align its own interests with those of controlling shareholders, which would be detrimental to the corporation and minority shareholders.⁷¹

The right of a shareholder to control is incentive for managers to fulfill their obligations to the company in good faith. Shareholders may not support the decisions made by management. For shareholders who are not insiders of the corporation (and they are quite a lot because the right of control is concentrated in a narrow circle), exercising this right is difficult or almost impossible within the dual-class share structure.

Over time, dual-class share structure becomes inefficient for the company. If it plays a positive role in the initial stage of a company's operation, in the maturing stage it may lead to an increase in agency costs, as well as a decrease in labor productivity, innovation, the number of employees, etc.⁷²

Some scholars believe that a dual-class structure is effective over a period of time rather than for an indefinite period. With time, a dual-class structure loses its effectiveness and only creates problems. If it is effective during the initial public offering period, there is a great risk that it will not be so for years to come.⁷³ Nevertheless, controlling shareholders have a desire to keep the management in their hands perpetually, thus maintaining a dual-class share structure even when it is no longer effective.⁷⁴ This could turn out to be harmful for a company.

8. Mechanisms for Regulation

In most of the jurisdictions of the world, the matter of classes of shares is regulated by the provisions of the law that have the character of *jus dispositivum*. The laws do not explicitly prohibit deviations from the "one share, one vote" rule, thus, self-regulatory organizations have undertaken upon themselves to address the risks associated with a dual-class structure.

Institutional investors, leading stock exchanges, and other influential institutions strongly support a single-class share structure (where the principle of "one share = one vote" is maintained) and oppose the violation of shareholder equality (democracy) within a dual-class share structure. However, they do not have the power to completely ban this structure. That is why they have developed mechanisms to ensure the balancing of risks arising from dual-class share structure.

⁷¹ *Jibuti M.*, State control over the protection of the interests of shareholders (investors) by the governing bodies of corporations, in *Collected Articles: Duty of care and responsibility in the joint-stock company under Georgian and German law: Symposium Materials, II German-Georgian Symposium in Corporate Law*, Tbilisi, 2003, 207 (in Georgian), <<http://www.library.court.-ge/upload/giz2003-ge-de-symposium-company-law.pdf>> [05.02.2022].

⁷² See *Kim H., Michaely R.*, Sticking around Too Long? Dynamics of the Benefits of Dual-Class Voting, *European Corporate Governance Institute (ECGI) - Finance Working Paper No. 590/2019*, *Swiss Finance Institute Research Paper No. 19-09*, 2019, 4, <<https://ssrn.com/abstract=3145209>> [05.02.2022].

⁷³ See *Bebchuk L. A., Kastiel K.*, The Untenable Case for Perpetual Dual-Class Stock (April 18, 2017), *Virginia Law Review*, Vol. 103, 2017; *Harvard Law School John M. Olin Center Discussion Paper No. 905*; *Harvard Law School Program on Corporate Governance Discussion Paper 2017-6*, 590, <<https://ssrn.com/abstract=2954630>> [06.02.2022].

⁷⁴ *Ibid.*

The Council of Institutional Investors (CII)⁷⁵ has been calling on US stock exchanges and indices since 2012 to introduce the “one share, one vote” principle.⁷⁶ Moreover, the CII went beyond the United States and called on the stock exchanges of London, Hong Kong and Singapore not to allow companies with a dual-class structure for listing.⁷⁷ The CII also addressed the SEC Investor Advisory Committee.⁷⁸ SEC representative Robert Jackson supports a dual-class structure only if it is to be limited in time.⁷⁹ In his February 2018 speech⁸⁰, he noted that he hopes stock exchanges will oblige dual-class companies to include a special clause - Sunset Provision – in their statutes and regulate unequal voting rights over time.⁸¹ The SEC Investor Advisory Committee has issued a recommendation⁸² according to which the Division of Corporation Finance⁸³ shall require from dual-class companies to strictly follow the disclosure obligation and to provide detailed information about risks.⁸⁴

In 1988, the Securities and Exchange Commission (SEC) enacted Rule 19c-4 in its Securities Regulatory Rules, which required U.S. stock exchanges to refuse to list corporations that used dual-class recapitalizations which nullified, restricted or disparately reduced the voting rights of existing shareholders.⁸⁵ The SEC’s action was challenged by the influential U.S. business

⁷⁵ Council of Institutional Investors (CII) - an association of nonprofit, pension, charitable, and other foundations that protects the interests of institutional investors in the United States. CII supports effective corporate governance, shareholder protection, and sensible financial regulation that promotes a fair, vibrant capital markets. See <<https://www.cii.org/about>> [06.02.2022].

⁷⁶ *Lund D. S.*, Nonvoting Shares and Efficient Corporate Governance, *Stanford Law Review*, Vol. 71, 2019, 708, <<https://www.stanfordlawreview.org/print/article/nonvoting-shares-and-efficient-corporate-governance/>> [04.02.2022].

⁷⁷ *Ibid.*, 708.

⁷⁸ *Ibid.*, 709.

⁷⁹ *Ibid.*, 711.

⁸⁰ *Commissioner Robert J. Jackson Jr.*, Perpetual Dual-Class Stock: The Case Against Corporate Royalty, Speech, San Francisco, California, February 15, 2018 <<https://www.sec.gov/news/speech/perpetual-dual-class-stock-case-against-corporate-royalty>> [04.02.2022].

⁸¹ *Lund D. S.*, Nonvoting Shares and Efficient Corporate Governance, *Stanford Law Review*, Vol. 71, 2019, 711, <<https://www.stanfordlawreview.org/print/article/nonvoting-shares-and-efficient-corporate-governance/>> [04.02.2022].

⁸² Recommendation of the Investor Advisory Committee Dual Class and Other Entrenching Governance Structures in Public Companies <<https://www.sec.gov/spotlight/investor-advisory-committee-2012/recommendation-on-dual-class-shares.pdf>> [04.02.2022].

⁸³ The Division of Corporation Finance shares the mission of the Securities and Exchange Commission to protect investors, maintain fair, orderly and efficient markets, and facilitate capital formation. The Division of Corporation Finance strives to provide investors with accurate and complete information to help them make informed investment decisions. When a company initially offers its securities to the public and also on an ongoing basis as it continues to provide information to the market. The Division also advises companies on the rules and forms established by the SEC. For its part, makes recommendations to the SEC regarding both for the adoption of new rules and for the revision of existing rules. See <<https://www.sec.gov/divisions/corpfin/cfabout.shtml>> [04.02.2022].

⁸⁴ *Lund D. S.*, Nonvoting Shares and Efficient Corporate Governance, *Stanford Law Review*, Vol. 71, 2019, 711, <<https://www.stanfordlawreview.org/print/article/nonvoting-shares-and-efficient-corporate-governance/>> [04.02.2022].

⁸⁵ See *Bainbridge S. M.*, The Short Life and Resurrection of SEC Rule 19C-4, *Washington University Law Quarterly*, Vol. 69, 1991, 566, <http://openscholarship.wustl.edu/law_lawreview/vol69/iss2/6/> [06.02.2022].

association Business Roundtable, which argued that regulating corporate governance issues, including the determination of shareholder rights, was the responsibility of the state and the company itself, not the SEC.⁸⁶ In 1990, the United States Court of Appeals for the District of Columbia ruled that the SEC had exceeded its authority and therefore invalidated Rule 19c-4.⁸⁷

In the United States, the Securities Exchange Act does not give the Securities and Exchange Commission (SEC) the power to regulate corporate governance issues.⁸⁸ The SEC is entitled to regulate trade and pricing.⁸⁹ It is the authority of the state legislature and the company itself to regulate corporate governance issues.⁹⁰

The New York Stock Exchange and NASDAQ impose a restriction that dual-class companies are not allowed to significantly reduce the voting rights of already issued shares (e.g., by issuing a new class of shares that includes superior voting rights).⁹¹ In other words, recapitalization that reduces the voting rights of already issued shares is prohibited. According to the New York Stock Exchange listing rules, a company shall have a dual-class capital structure from the outset when making its initial public offering. It is not allowed to recapitalize a company listed on a stock exchange with a single-class share structure, i.e. to transform it into a dual-class company, thus nullifying, restricting or reducing the voting rights of existing shareholders. It should be noted, however, that the above rules are of discretionary nature and, in exceptional cases, may be regulated differently. The New York Stock Exchange has chosen to develop flexible rules given that the capital market as well as the circumstances and needs of companies are volatile over time.⁹²

“One share, one vote” is a universally recognized principle for stock exchanges as well. However, due to the high level of competition, stock exchanges have to make certain concessions.⁹³ In 2016, for example, Alibaba, a Chinese e-commerce company, listed its shares on the New York Stock Exchange after the Hong Kong Stock Exchange refused to list its shares because it strongly adhered to the “one share, one vote” principle.⁹⁴ From April 2018, Hong Kong has made an

⁸⁶ See *Bainbridge S. M.*, The Short Life and Resurrection of SEC Rule 19C-4, *Washington University Law Quarterly*, Vol. 69, 1991, 567, <http://openscholarship.wustl.edu/law_lawreview/vol69/iss2/6/> [06.02.2022].

⁸⁷ See *The Business Roundtable v. S.E.C.*, 905 F.2d 406 (D.C. Cir. 1990)

⁸⁸ *Bainbridge S. M.*, The Scope of the SEC’s Authority Over Shareholder Voting Rights, *UCLA School of Law Research Paper No. 07-16*, 2007, 14, <<https://ssrn.com/abstract=985707>> [06.02.2022].

⁸⁹ *Ibid.*

⁹⁰ *Ibid.*

⁹¹ *Committee On Capital Markets Regulation (CCMR)*, The Rise of Dual Class Shares: Regulation and Implications, Report, April 2020, 12, <<https://www.capmksreg.org/wp-content/uploads/2020/04/The-Rise-of-Dual-Class-Shares-04.08.20-1.pdf>> [05.02.2022].

⁹² See NYSE, Voting Rights Interpretations Under Listed Company Manual Section 313 (01.15.13) <https://www.nyse.com/publicdocs/nyse/regulation/nyse/voting_right_interpretations_under_listed_company_manual_section_313.pdf> [05.02.2022].

⁹³ See *Committee On Capital Markets Regulation (CCMR)*, The Rise of Dual Class Shares: Regulation and Implications, Report, April 2020, 12, <<https://www.capmksreg.org/wp-content/uploads/2020/04/The-Rise-of-Dual-Class-Shares-04.08.20-1.pdf>> [05.02.2022].

⁹⁴ See *Kraakman R., Armour J., Davies P., Enriques L., Hansmann H., Hertig G., Hopt K., Kanda H., Pargendler M., Ringe W.-G., Rock E.*, The Anatomy of Corporate Law: A Comparative and Functional Approach, Third Edition, *Kochiashvili A., Maisuradze D. (Translators)*, Tbilisi, 2019, 126 (in Georgian) <http://lawlibrary.info/ge/books/2019giz-ge_anatomy_of_corporate_law.pdf> [05.02.2022].

exception under which it will allow a company with a dual-class structure to trade publicly only if that company meets certain criteria: it must be innovative, high-profile, etc.⁹⁵ Like Hong Kong, the Singapore Stock Exchange has allowed listing of companies with a dual-class share structure since 2018. In 2012, Manchester United PLC did not list its shares on the Singapore Stock Exchange and it was after that that the Singapore Stock Exchange changed its listing rules and from 2018 has already allowed listing of dual-class companies, although, like Hong Kong, with some restrictions.⁹⁶

At the London Stock Exchange, companies with a dual-class share structure could only place their shares under the standard listing regime, whereas, under the premium listing regime⁹⁷, it was not allowed. In February 2017, the FCA (Financial Conduct Authority)⁹⁸ issued a Discussion Paper⁹⁹ proposing admission to a premium listing of companies with a dual-class share structure in the field of science and technology, with the main purpose of maintaining the attractiveness and competitiveness of the London Stock Exchange. Under the amendment of December 3, 2021, companies with a dual-class structure are allowed on the premium segment of the London Stock Exchange, although with certain restrictions, namely the dual-class structure may be valid for up to 5 years after the initial placement of shares on the stock exchange. Extension or otherwise restoration of this period is not allowed.¹⁰⁰

Companies with a dual-class structure are also allowed on the Silicon Valley's Long-Term Stock Exchange.¹⁰¹ Long-Term Stock Exchange (LTSE) - A new, innovative stock exchange in

⁹⁵ See *Baker McKenzie Lawyers*, The Revival of Dual Class Shares, Publication, 19 March 2020, 3, <<https://www.bakermckenzie.com/en/insight/publications/2020/03/the-revival-of-dual-class-shares>> [05.02.2022].

⁹⁶ Restrictions imposed by the Singapore and Hong Kong stock exchanges can be found here: *CFA Institute*, Dual-Class Shares: The Good, the Bad, and the Ugly, A Review of the Debate Surrounding Dual-Class Shares and Their Emergence in Asia Pacific, Survey Report, 2018, 50-51, <<https://www.cfainstitute.org/-/media/documents/survey/apac-dual-class-shares-survey-report.ashx>> [06.02.2022].

⁹⁷ The London Stock Exchange Premium Listing is a prestigious segment that sets high standards for corporate governance, transparency and disclosure. See *Baker McKenzie Lawyers*, The Revival of Dual Class Shares, Publication, 19 March 2020, 4, <<https://www.bakermckenzie.com/en/insight/publications/2020/03/the-revival-of-dual-class-shares>> [05.02.2022].

⁹⁸ FCA (Financial Conduct Authority) – Financial Regulatory Authority in the United Kingdom. Acts independently of the government. It regulates the financial services industry in Great Britain and its main function is to protect consumers, maintain industry stability and effective competition between financial service providers. See <<https://www.fca.org.uk/about/the-fca>> [05.02.2022].

⁹⁹ See Financial Conduct Authority, Review of the Effectiveness of Primary Markets: The UK Primary Markets Landscape, Discussion Paper: DP17/2, 8, <<https://www.fca.org.uk/publication/discussion/dp17-02.pdf>> [05.02.2022].

¹⁰⁰ *Morland C., Norton Ph., Hoffman K., Marshal A.*, New Rules for Listing on the London Stock Exchange Could Ease the Path to IPO, 2021 <<https://humancapital.aon.com/insights/articles/2021/new-rules-for-listing-on-the-london-stock-exchange-could-ease-the-path-to-ipo>> [05.02.2022].

¹⁰¹ *Wang E., DiNapoli J.*, Long-Term Stock Exchange CEO says dual-class stock critics “lost the argument”, Reuters, 2021 <<https://www.reuters.com/business/long-term-stock-exchange-ceo-says-dual-class-stock-critics-lost-argument-2021-07-02/>> [05.02.2022]. Also, *Doherty K.*, Silicon Valley Exchange Lists First Two Companies in ESG Push, Bloomberg, 2021 <[139](https://www.bloom-</p></div><div data-bbox=)

the US, launched in 2020. It is noteworthy that the first companies to list their shares on this stock exchange (Asana Inc. and Twilio Inc.) were dual-class companies.¹⁰²

In Sweden, dual-class companies are not only allowed on the stock exchanges, but it has been around for about 100 years, making up a significant part of the capital market.¹⁰³

Dual-class companies are also allowed on the Toronto Stock Exchange (TSX) and many European stock exchanges, such as e.g. Euronext (European New Exchange Technology).¹⁰⁴

One of the most common and recognized mechanism for balancing the risks arising from the dual-class share structure is the inclusion of a special clause in a statute/registration application, known as Sunset Provision¹⁰⁵. A company can include a special clause in the charter / registration statement, according to which a company will use a dual-class structure for a certain period of time (mainly such a period is considered 10 or 15 years, some scholars believe that this period should be less, e.g. 5-7 years). And then transform, usually to a single-class share structure, where the “one share = one vote” principle will be followed. When this clause is entered into force, the multi-voting shares will automatically be converted into common shares and the second class of common shares will cease to exist.

In 2011, Groupon¹⁰⁶, an American e-commerce company, included the clause in its statute that stated that the company would use a dual-class structure for a period of 5 years from the initial public offering, and in 2016, it transformed into a single-class structure company.¹⁰⁷

The clause may be based on time or a specific event (e.g., the founder becoming incapacitated, her/his death or her/him reaching retirement age, etc.).¹⁰⁸ Such a clause prevents the founder from having the control over the company for an indefinite period of time, and also prevents the founder from passing on this authority to her/his successor, who may not necessarily be a good manager.¹⁰⁹

“Sunset Provision” does not explicitly prohibit a dual-class share structure, nor does it allow its perpetual use.¹¹⁰

berg.com/news/articles/2021-08-26/silicon-valley-exchange-lists-first-two-companies-in-esg-push> [05.02.2022].

¹⁰² Ibid.

¹⁰³ See *Lidman E., Skog R. R.*, London Allowing Dual Class Premium Listings: A Swedish Commentary (April 14, 2021). European Corporate Governance Institute - Law Working Paper 580/2021, Nordic Journal of Company Law (NTS), Forthcoming, 2, <<https://ssrn.com/abstract=3826174>> [05.02.2022].

¹⁰⁴ Ibid., 4.

¹⁰⁵ Sunset Provision or Sunset Clause - “Part of a law or contract that states when it will end, or the conditions under which it will end.” Cambridge Business English Dictionary © Cambridge University Press.

¹⁰⁶ Groupon is an American, global e-commerce marketplace that connects subscribers to local merchants. It offers its customers the following services: travel, purchase of goods and services, etc. See <<https://www.groupon.com/>> [06.02.2022].

¹⁰⁷ *Bebchuk L. A., Kastiel K.*, The Untenable Case for Perpetual Dual-Class Stock (April 18, 2017), Virginia Law Review, Vol. 103, 2017, Harvard Law School John M. Olin Center Discussion Paper No. 905, Harvard Law School Program on Corporate Governance Discussion Paper 2017-6, 619, <<https://ssrn.com/abstract=2954630>> [06.02.2022].

¹⁰⁸ See *ibid.*, 620.

¹⁰⁹ See *ibid.*

¹¹⁰ See *Fisch J. E., Davidoff-Solomon S.*, The Problem of Sunsets, Boston University Law Review, Vol. 99, 2019, University of Pennsylvania, Institute for Law & Economic Research Paper No. 19-04, 1062, <<https://ssrn.com/abstract=3305319>> [05.02.2022].

There are differences of opinion regarding the mandatory nature of Sunset Provision. Professors Lucian A. Bebchuk and Kobi Castiel advocate the mandatory nature of time-based Sunset Provision as an effective safeguard against the risks posed by a dual class structure.¹¹¹ Professors Jill E. Fisch and Steven Davidoff Solomon offer contrary view in their paper¹¹². They point out that it is true that “Sunset Provision” can be considered as a kind of insurance mechanism against the founder’s crooked, wrong intentions, however, a tool that ensures the replacement of such a founder after 7 or 10 years is a rather unsuitable and potentially cost-effective mechanism (Professors, in this case, pay particular attention to innovative, “new economy” companies (meaning high-tech companies) and point out that this is a long period for such companies).¹¹³

Professors Fisch and Davidoff-Solomon believe that the main problem with Sunset Provision is the pre-determination of accurate time (according to the practice of existing public companies, this time is a minimum of 3 years and a maximum of 20 years).¹¹⁴ Professors argue that the period specified in the Sunset Provision is random and has nothing to do with the fact that this time is required for the founder to carry out and run a company according to her/his own plan.¹¹⁵ Professors believe that Sunset Provision should not be mandatory and that there is no one-size-fits-all approach to it, as the timeframe for achieving the company’s goals is likely to vary according to a number of characteristics of a company (e.g. the maturity of a company for the initial public offering phase, the duration of its business model, the time it takes to develop its products or services and bring them to market).¹¹⁶

Nowadays, it is not mandatory for companies with a dual-class share structure to include Sunset Provision in their statutes in the United States (nor in any other jurisdiction). US stock exchanges do not oblige dual-class companies to include Sunset Provision in their registration statements. It depends on the will of companies. Some of them include it, some of them do not. However, it should be noted that most of the scholars, as well as influential institutions that represent the interests of investors, support the mandatory nature of “Sunset Provision”, because in terms of protecting the rights of investors, as well as to prevent the arbitrariness of founders and for the prosperity of a company and the capital market, it is considered to be one of the most effective mechanisms, in a reality where a dual-class stock structure is permitted.

¹¹¹ See *Bebchuk L. A., Kastiel K.*, The Untenable Case for Perpetual Dual-Class Stock (April 18, 2017), *Virginia Law Review*, Vol. 103, 2017; Harvard Law School John M. Olin Center Discussion Paper No. 905; Harvard Law School Program on Corporate Governance Discussion Paper 2017-6, <<https://ssrn.com/abstract=2954630>> [06.02.2022].

¹¹² See *Fisch J. E., Davidoff-Solomon S.*, The Problem of Sunsets, *Boston University Law Review*, Vol. 99, 2019, University of Pennsylvania, Institute for Law & Economic Research Paper No. 19-04, <<https://ssrn.com/abstract=3305319>> [05.02.2022].

¹¹³ See *ibid.*, 1063.

¹¹⁴ See *ibid.*, 1080.

¹¹⁵ For example, professors discuss the case of the company Workday. Workday Inc. is an American cloud-based, on-demand, financial and human resource management software company. See <<https://www.workday.com/>>. Workday, which became a public company in 2012, has included a 20-year Sunset Provision in its registration application. At the time of initial public offering, its founders were 71 and 46 years old, which means that by the time this clause will come into force they will be 91 and 66 years old. In addition, professors discuss examples of Facebook and Google. The founders still manage the company well and bring benefits to it. See *ibid.*, 1081.

¹¹⁶ See *ibid.*, 1082.

9. Conclusion

Dual-class share structure is a challenge of present times and is “the most important issue in corporate governance today”¹¹⁷, around which the debate continues. Most of the scholars, institutional investors and other influential institutions believe that protecting the rights of investors is important. It is true that business development should be encouraged, but it is important to maintain high standards of corporate governance. That is why it is necessary to maintain a certain balance and find a golden mean.

The Georgian legal reality is interesting in this regard. In the present paper, we have discussed that Georgian legislation theoretically allows for a deviation from the general principle - one share, one vote. It does not prohibit multi-voting shares. Consequently, the existence of a dual-class share structure in the Georgian reality is possible. However, the Georgian reality is unfamiliar with dual-class share structures.

There is no ideal corporate governance system. Each system has its weaknesses and strengths, and it is difficult to identify which governance method is more successful and efficient. There are both theoretical and empirical studies that prove the positive impact of dual-class share structure and consequently the increase in the value of a company, as well as the opposite - the negative impact and the decrease in the value of a company.¹¹⁸

Dual-class share structure should be used in companies that have appropriate mechanisms in place to monitor management. For companies where effective controlling mechanisms are not implemented, a dual-class share structure can be harmful.¹¹⁹

Professor Aurelio Gurrea-Martínez believes that the appropriateness of each regulation model for a dual-class share structure depends on a number of factors, especially on factors of local importance, in particular the level of development of the capital market in a country, the level of protection of minority investors, the level of development of regulatory bodies and the judiciary in specific jurisdictions.¹²⁰

In countries with developed markets and regulatory bodies, where minority investors are guaranteed strong legal protections and the possibility of abuse of control is minimized, regulators should allow companies to adopt a dual-class share structure without restrictions. Also, minor interference by the regulator is allowed (e.g. setting an event-based “Sunset Provision”). In contrast, in countries where the capital market is underdeveloped, where the legal protections of minority investors are weak, and the potential for abuse of control is high, regulators should not

¹¹⁷ *Coffee J. C. Jr.*, Dual Class Stock: The Shades of Sunset, November 19, 2018, The CLS Blue Sky Blog <<https://clsbluesky.law.columbia.edu/2018/11/19/dual-class-stock-the-shades-of-sunset/>> [06.02.2022].

¹¹⁸ See *Lidman E., Skog R. R.*, London Allowing Dual Class Premium Listings: A Swedish Commentary (April 14, 2021). European Corporate Governance Institute - Law Working Paper 580/2021, Nordic Journal of Company Law (NTS), Forthcoming, 2, <<https://ssrn.com/abstract=3826174>> [05.02.2022].

¹¹⁹ See *Lel U., Netter J. M., Poulsen A. B., Qin Zh.*, Dual Class Shares and Firm Valuation: Evidence from SEC Rule 19c-4 (June 1, 2020), European Corporate Governance Institute – Finance Working Paper No. 807/2021, 29, <<https://ssrn.com/abstract=3729297>> [05.02.2022].

¹²⁰ See *Gurrea-Martínez A.*, Theory, Evidence, and Policy on Dual-Class Shares: A Country-Specific Response to a Global Debate, Harvard Law School Forum on Corporate Governance, 2019 <<https://corpgov.law.harvard.edu/2019/07/15/theory-evidence-and-policy-on-dual-class-shares-a-country-specific-response-to-a-global-debate/>> [05.02.2022].

allow companies to adopt a dual-class share structure. It should be prohibited or if not, relatively strict restrictions may apply (e.g. setting a time-based “Sunset Provision”, developing strict corporate governance rules).¹²¹

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¹²¹ See *Gurrea-Martínez A.*, Theory, Evidence, and Policy on Dual-Class Shares: A Country-Specific Response to a Global Debate, Harvard Law School Forum on Corporate Governance, 2019 <<https://corpgov.law.harvard.edu/2019/07/15/theory-evidence-and-policy-on-dual-class-shares-a-country-specific-response-to-a-global-debate/>> [05.02.2022].

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