

Dual Class Share Structures: The Ethics of Control & Ownership

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Abstract

This paper presents a critical analysis of dual-class share structures (DCSS) within an ethical and logical framework for ownership and control. Moreover, it contends that the existence of DCSS constitutes a *de facto* infringement on the ownership rights of shareholders. By adopting a conceptual approach rooted in symbolic logic, the paper demonstrates that DCSS falls short of the ethical precept of “one share, one vote” and is therefore an unjust and inefficient equity arrangement. The paper contributes to the existing literature on DCSS by focusing on the ethical and logical basis of such share structures.

1 Introduction

Dual class share structures (DCSS) are equity arrangements where companies have two classes of shares, each conferring different voting rights on shareholders. In general, one class of shares, often held by the founders of the company or insiders therein, carries significantly more voting power than the other class, which is generally available to public investors [7].

One of the main justifications for DCSS is to allow visionary founders to retain control of a company so that they can realize their *idiosyncratic vision* while having the opportunity to raise public capital [5]. In some cases, shareholders agree to a compromise through sunset provisions, which limit the duration of DCSS. Such provisions reduce the

risks associated with long-term control and are typically designed to terminate dual-class voting on the basis of certain events, time periods or changes in ownership [10].

The current literature on DCSS primarily focuses on the performative implications and robustness of companies that adopt this particular equity arrangement, yielding mixed results. For example, Sonnenfeld & Tian argued that companies with DCSS could outperform their single-class peers in situations where the founder (or descendants thereof) have substantial expertise in their chosen industry [11]. On the contrary, Bebchuk & Kastiel offered a more critical appraisal by pointing out that the net benefits yielded by DCSS tend to diminish over time and thus a perpetual dual-class structure is virtually untenable due to the substantial risks it creates for corporate governance [1]. Yet, another line of research examines the resilience of DCSS across various stock exchanges and how institutional safeguards for minority shareholders in different countries affect the firm-specific advantages or disadvantages rendered by these structures [6].

This paper contends that the existing research on DCSS fails to incorporate meaningful discussions on the logical and ethical frameworks of ownership and control. The notion that voting rights should reflect economic interests is not merely a principle of corporate governance but also an ethical precept. Contemporary debates surrounding the length of DCSS, as implied by the existence of sunset provisions, fail to capture whether such structures are inherently legitimate or compatible with fundamental ethical values.

2 Conceptual Preliminaries

In traditional, single-class share structures (SCSS), voting power is proportionate to share ownership; those with the most economic stake have the greatest influence on corporate decisions. For over half a century, SCSS was the norm at the New York Stock Exchange (NYSE), and the doctrine *one vote, one share* is widely acknowledged as a core tenet in corporate governance [4].

From a conceptual perspective,¹ the preferential nature of SCSS can be viewed as a theorem that is partially derived from the fundamental axioms of rational preference,

¹An elementary understanding of symbolic logic would be of use for this section.

namely, completeness, transitivity and reflexivity.

Proof. As is standard in set theory: by *preference relation*, we are referring to a set of 2-tuples that satisfy the following assumptions:

Definition 2.1 (Completeness). *A preference relation \succsim is said to be complete if, for any two alternatives x and y , the following holds:*

$$(x \succsim y) \vee (y \succsim x)$$

Definition 2.2 (Transitivity). *A preference relation \succsim is transitive if, for any three alternatives x , y , and z , the following condition holds:*

$$[(x \succsim y) \wedge (y \succsim z)] \rightarrow (x \succsim z)$$

Definition 2.3 (Reflexivity). *A preference relation \succsim is reflexive if, for any alternative x , the following holds:*

$$x \succsim x$$

Consider the balance between control and ownership. Let there be $n \in \mathbb{N}^+$ investors in the set of all investors $\{A_i\}_{i=1}^n$. For all $1 \leq i \leq n$, there exists a finite set of property rights, Π_{A_i} . In general, it is assumed that rights confer on investors the ability to utilize such resources for their own gain. However, given the fundamental distinction between ownership and control, which is central to our discussion on DCSS: for all $1 \leq i \leq n$, there exists a finite set \mathbb{A}_{A_i} , which serves as the domain of all property rights that can be *acted upon* or controlled by each investor. We may now consider the following two propositions, each of which prescribes that every single property right π is (1) uniquely controlled and therefore uniquely owned or (2) uniquely owned and therefore uniquely controlled by an economic agent:

$$(C \rightarrow O) \stackrel{\text{def}}{=} (\forall \pi) \left[\bigoplus_{i=1}^n (\pi \in \mathbb{A}_{A_i} \rightarrow \pi \in \Pi_{A_i}) \right] \quad (1)$$

$$(O \rightarrow C) \stackrel{\text{def}}{=} (\forall \pi) \left[\bigoplus_{i=1}^n (\pi \in \Pi_{A_i} \rightarrow \pi \in \mathbb{A}_{A_i}) \right] \quad (2)$$

We may now turn to the normative assumption which forms the ethical precept of *one share, one vote*. Suppose we have four different regimes that reflect different structures of ownership and control:

Regimes	$(C \rightarrow O)$	$\neg(C \rightarrow O)$
$(O \rightarrow C)$	Just & Efficient	Unjust & Efficient
$\neg(O \rightarrow C)$	Just & Inefficient	Unjust & Inefficient

Figure 1: Normative Outcomes Based on Regimes of Ownership & Control

Definition 2.4 (Just & Unjust Outcomes). *An outcome is defined as being just if everything that is uniquely controlled by an agent is also uniquely owned by the same agent: otherwise, it is defined as being unjust.*

Definition 2.5 (Efficient & Inefficient Outcomes). *An outcome is defined as being efficient if everything that is uniquely owned by an agent is also uniquely controlled by the same agent: otherwise, it is defined as being inefficient.*

Philosophically, our notions of justice and efficiency originate from the fundamental distinction between ownership and control. To control something that we do not legitimately own or is otherwise uniquely owned by someone else would constitute a *de facto* infringement on their rights and perhaps more broadly our sense of justice. Yet the existence of an infringement could also imply that we have reached a *Pareto optimal* state, where no agent can be made better-off without injuring the interests of some other party. Regardless of the infringement, insofar as all resources are controlled and therefore being utilized by *some* party, then a Pareto efficient outcome is reached. However, this is not the same kind of efficiency that was have mentioned before. In the previously defined sense, *efficiency* refers to the individualistic notion that every agent can *at least* control everything that they own.²

²I contend that the definition is appropriate from a methodologically individualistic perspective. [8] A more radical view would be that the conceptual existence of Pareto efficiency is objectionable because

In general, the following 2-tuples would be present in a rational agent's preference relation \succsim for regimes:³

$$\text{Just \& Efficient} \succsim \text{Unjust \& Efficient} \quad (3)$$

$$\text{Unjust \& Efficient} \succsim \text{Just \& Efficient} \quad (4)$$

$$\text{Just \& Inefficient} \succsim \text{Unjust \& Inefficient} \quad (5)$$

$$\text{Unjust \& Inefficient} \succsim \text{Just \& Inefficient} \quad (6)$$

$$\text{Unjust \& Efficient} \succsim \text{Just \& Inefficient} \quad (7)$$

By the axioms of rational preferences we can infer the following:

- I. Every regime is at least as good as itself (2.1 & 2.3).
- II. A rational agent would be indifferent between just and unjust outcomes, insofar as they are efficient. (3 & 4).
- III. Likewise, a rational agent would be indifferent between just and unjust outcomes, insofar as they are both inefficient. (5 & 6).
- IV. Efficient outcomes are preferred over inefficient outcomes, regardless of whether they are just or unjust. (2.2, 7, II. & III.).

If an agent controls something at the expense of another agent's property rights, as is the case for DCSS, then the regime is *unjust* (2.4), and, since it infringes on what another agent owns, the regime is *inefficient* (2.5). On the contrary, since every agent controls what they own and owns what they control, SCSS constitutes a *just* and *efficient* regime. By IV., a just and efficient outcome is preferred over an unjust and inefficient outcome, thus, $\text{SCSS} \succsim \text{DCSS}$. □

it does not treat the notion of a *socially preferable outcome* as something that can be ascertained on an individualistic level, thereby allowing it to be used as an argument in favor of policies that restrict individual freedom (for example, theft can result in a Pareto efficient distribution of resources, but is inefficient from a rights-based perspective).

³Evidently, this section is incomplete as we have previously indicated that one's preference for each regime could be entirely subjective and dependent on the cardinality of the set \mathbb{A}_{A_i} for each agent. There is possibly no consistent way to determine the preferences of each agent for every given regime.

3 DCSS & Sunset Provisions

Having demonstrated the conceptual reasons as to why SCSS is at least as good, if not better than DCSS, we may find it difficult to reconcile this intensely philosophical, set-theoretic approach to efficiency and ownership with a few key observations about the real world:

- The NYSE reinstated DCSS in 1986 after facing growing competition from the American Stock Exchange and NASDAQ, both of which were allowing dual-class stock with minimal to no restrictions, as more firms were using this equity arrangement to fend off hostile takeovers [2].
- In 2024, the Financial Conduct Authority announced that it would allow companies with multiple class stock structures admission to the London Stock Exchange, subject to the sunset provision that the enhanced voting rights of Pre-IPO institutional investors expire after a decade [3].

Setting aside the methodological objection that a theory of rational behavior should not be expected to account for the outcomes of irrational behavior, the general consensus on companies with DCSS is that they should be regulated, since allowing them to be listed would run the risk of entrenchment and disenfranchise shareholders.

One of the most prominent arguments for allowing DCSS while introducing sunset provisions is that such structures allow the managers of “highly innovative tech firms” to focus on long-term strategies without the pressures of short-term market focus [9]. But the need to utilize a grossly *unjust* and *inefficient* technique like DCSS raises serious questions about the ostensibly innovative activities of the firm. Common sense dictates that as opposed to viewing an influx of public capital as a necessary trade-off to control, a compelling visionary could win the hearts and minds of its investors, whereas extortionists demand recognition by compelling its investors to divorce the ownership of their shares from the control of their company. By their own admission, most analysts in the field of corporate governance implicitly acknowledge the problematic nature of DCSS by recommending sunset provisions.

3.1 Formal Treatment

We have previously defined an *unjust* and *inefficient* regime as one where agents are able to control property which they do not own, and own property which they have no control over. Sunset provisions attempt to mitigate the harm caused by this evidently problematic arrangement, but they do not address the fundamental issue that occurs during the period in which DCSS remains in effect; these provisions serve as a tacit admission that the DCSS regime is ethically untenable, and that only through the eventual restoration of equality in voting rights can fairness be reestablished.

The only conceivable, formal justification for the existence of DCSS is that it would be rational to have a non-standard preference relation over each regime. For example, a super-majority of rational agents may have a preference relation which includes the following 2-tuple:

$$\text{Unjust \& Inefficient} \succsim \text{Just \& Efficient} \quad (8)$$

By extension, only when a reversal of this preference occurs, does the sunset provision obtain the requisite momentum to be enforced. Nevertheless, the economic desirableness of an unjust and inefficient outcome over a just and efficient one, however temporary, does not contradict the fact that DCSS is an unethical equity arrangement.

4 A Practical Conclusion

Though it is impractical to consider the weight of ethics when faced with a more than commensurate economic benefit, it is dishonest to portray DCSS as something that it is not, namely, an effective solution to the problem of enabling innovative companies to enjoy the benefits of the capital market. This view is naive at best and fails to probe into the fundamental schism it introduces to ownership and control. At most, it is a method of financing for companies that tread a fine line between visionaries and extortionists.

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