SHAREHOLDER CULTIVATION AND NEW GOVERNANCE

BY TAMARA C. BELINFANTI*

ABSTRACT

Several formal proposals have been made to address shareholder short-termism and speculative behavior. These include the imposition of a financial transaction tax, changes to the U.S. capital gains tax rate, and the adoption of an Investor Stewardship Code in the United Kingdom. This Article reverses the focus from top-down solutions and instead, focuses on bottom-up grass root solutions that corporations can employ, and in some cases do already employ to achieve substantially the same effect of rewarding certain types of shareholder behavior while discouraging others—a process I refer to as "Shareholder Cultivation." While many of the techniques and strategies discussed in this Article are not new and in fact many have been used by companies and investor relation professionals for years, the Article is the first to conceptualize a prescriptive framework for assessing which techniques and strategies should be allowed. Additionally, the Article utilizes new governance theory to examine the concept of Shareholder Cultivation with a fresh lens: as a corporate governance benefit.

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*Associate Professor, New York Law School; Aspen Ideas Scholar. I am grateful for the support of my colleagues at New York Law School. This Article benefited greatly from the insights and comments of corporate governance practitioners, institutional investors, shareholder relation firms, in-house investor relation departments, and business policy institutions. Most notably, I must thank the Aspen Business & Society Program; Gary Kraut, President of G.A. Kraut Company Inc.; Brian Walsh, Executive Director of Liquidnet For Good; and Marjorie Kelly, author of *Owning Our Future: The Emerging Ownership Revolution*, for their selfless and valuable feedback. Special thanks for the useful comments received from attendees at the Emerging Approaches to Corporate Governance session at the 2013 Law & Society annual meeting and fellow members of the New York Areas Scholars Group. Jennifer Wang provided truly exceptional research assistance. Finally, special and (ironic?) thanks to the "cultivated" shareholder who told me "corporate governance is b***s**t; if companies really want governance they go out and get people like me to help hold the ship steady." And from that, this Article began.

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I. INTRODUCTION

In a 2012 article in the *Harvard Business Review*, the authors asked: "What good are shareholders?"[1] The traditional response to this question is that shareholders are the owners of the firm, they contribute financial capital, in addition to which they serve a monitoring and disciplining function that in theory controls managerial shirking.[2] Post 2008, however, there has been an intense focus on the role of shareholders in the 2008 financial crisis and a recognition that short-termistic speculative behavior played a key role in the global financial market demise.[3] As a result, several formal proposals have been made to address these short-termistic and speculative tendencies.[4] These include the imposition of a financial transaction tax, changes to the United States ("U.S.") capital gains tax rate, and the adoption of an Investor Stewardship Code in the United Kingdom ("UK").[5]

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[1] *See* Justin Fox & Jay W. Lorsch, *What Good are Shareholders?*, HARV. BUS. REV., July-Aug. 2012.

[2] *See id.*

[3] *See infra* Part II.

[4] *See infra* note 5 and accompanying text.

[5] *See France Wants Changes to EU Financial Transaction Tax*, REUTERS: UK EDITION (July 11, 2013), http://uk.reuters.com/article/2013/07/11/france-tax-eu-idUKL6N0FH2I320130711; JOHN C. BOGLE ET AL., ASPEN INST., OVERCOMING SHORT-TERMISM: A CALL FOR A MORE RESPONSIBLE APPROACH TO INVESTMENT

While these formal proposals have tremendous merit, this Article reverses the focus from looking to top-down solutions, and instead, focuses on bottom-up grass root solutions that corporations can employ, and in some cases do already employ, to achieve substantially the same effect of rewarding certain types of shareholder behavior while discouraging others—a process I refer to as "Shareholder Cultivation." As more fully developed herein, the aim of Shareholder Cultivation is to identify, attract, and cultivate a core of committed shareholders stewards who understand the firm's purpose and value proposition, rather than settling for a shareholder base composed entirely of "faceless members of an ever-shifting crowd."[6] While many of the techniques and strategies discussed herein are not new, and in fact many have been used by companies and investor relation professionals for years, the Article is the first to conceptualize a prescriptive framework for assessing which techniques and strategies should be allowed. Additionally, the Article utilizes new governance theory to examine the concept of Shareholder Cultivation with a fresh lens: as a corporate governance benefit.[7]

For public corporations that care about developing and achieving long-term value, Shareholder Cultivation will become increasingly important. As a leading report on the importance of stewardship argues, "the success of companies and the societies in which they operate depends on the exercise of 'stewardship.'"[8]

Public corporations express this desire to cultivate shareholder stewards in many ways.[9] For example, in its 2004 Owner's Manual for

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AND BUSINESS MANAGEMENT, 2 (2009), http://www.aspeninstitute.org/sites/default/files/content/docs/bsp/overcome_short_state0909.pdf; *The UK Stewardship Code*, FIN. REPORTING COUNCIL (2012), http://www.frc.org.uk/getattachment/e2db042e-120b-4e4e-bdc7-d540923533a6/UK-Stewardship-Code-September-2012.aspx.

[6]WARREN E. BUFFETT, AN OWNER'S MANUAL 1 (1996), http://www.berkshirehathaway.com/ownman.pdf (describing that Berkshire Hathaway Inc. shareholders are not viewed as "faceless members of an ever-shifting crowd," but rather potential life-long co-venturers).

[7]*See infra* Part III.

[8]MARK GOYDER & DONALD MACDONALD, TOMORROW'S OWNERS: STEWARDSHIP OF TOMORROW'S COMPANY 3 (2008), http://tomorrowscompany.com/tomorrows-owners-stewardship-of-tomorrows-company. Although the report's definition of "steward" was limited to a shareholder who "promote[s] sustainable, long-term, performance," the larger point is that a focus on ownership design is integral to a company's long-term success. *Id.*

[9]*See, e.g.*, ANITA SKIPPER ET AL., INVESTOR STEWARDSHIP WORKING PARTY, 2020 STEWARDSHIP: IMPROVING THE QUALITY OF INVESTOR STEWARDSHIP (2012), https://www.icsa.org.uk/assets/files/pdfs/Policy2/2020_Stewardship_Final_L.pdf ("I believe you get the shareholders you deserve. There are a lot of shareholders with whom you could never have a dialogue. The long-term investors tend to behave consistently, they're available and they are those that tell you things as they are." (quoting the Chairman of a FTSE 100

Shareholders, Google Inc.'s founders, Larry Page and Sergey Brin, included a plea to their shareholders to avoid a short-term and impatient mindset saying,

> [i]n our opinion, outside pressures too often tempt companies to sacrifice long term opportunities to meet quarterly market expectations. . . . If opportunities arise that might cause us to sacrifice short term results but are in the best long term interests of our shareholders, we will take these opportunities. . . . We would request that our shareholders take the long term view.[10]

Similarly, Berkshire Hathaway Inc., in a letter to its shareholders, stated that the firm tries to attract investors who "understand [its] operations, attitudes and expectations. . . . [a]nd, fully as important, . . . dissuade those who won't."[11]

Admittedly, the notion of cultivating some subset of loyal shareholders causes intellectual unease. It raises significant concerns such as entrenchment, abuse, diminished monitoring, creation of a class of lapdog shareholders, and unequal treatment for shareholders not deemed worthy of cultivation.[12] The cultivation framework developed in this Article attempts to minimize and temper these concerns and on balance, the Article argues that any perceived costs of Shareholder Cultivation are outweighed by the benefits of having an engaged core of shareholder stewards.[13]

In his article *Shareholder Eugenics in Public Corporations*, Professor Edward Rock argues that there is "a link between the shareholders of a company and its cost of capital."[14] Based on this premise, Professor Rock investigates traditional capital market tools for engineering the shareholder base "[f]rom the perspective of financial economics."[15] While some of the traditional capital market tools discussed by Professor Rock are also referenced herein, this Article is

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Company in Executive Summary)).

[10]Google Inc., Amendment No. 9 to Form S-1 Registration Statement (Form S-1/A), 27 (Aug. 18, 2004).

[11]Letter from Warren E. Buffett to the Shareholders of Berkshire Hathaway Inc. (Mar. 14, 1984), http://www.berkshirehathaway.com/letters/1983.html.

[12]*See infra* Part V.B.

[13]*See infra* Part V.B.

[14]Edward B. Rock, *Shareholder Eugenics in the Public Corporation*, 97 CORNELL L. REV. 849, 851 (2012).

[15]*Id.*

distinct in at least two respects. First, in terms of approach, this Article anchors Shareholder Cultivation in the new governance school, and in doing so provides a theoretical frame for conceptualizing and assessing Shareholder Cultivation as a corporate governance practice.[16] Second, this Article expands the frontier for future cultivation strategies and directly connects the promise of Shareholder Cultivation to the increasing calls for stewardship.[17]

The remainder of the Article proceeds as follows. Part II first examines some of the practical dynamics of shareholder behavior that have led to calls for shareholder stewardship, but at the same time make stewardship challenging.[18] These dynamics include an increasingly heterogeneous and transient shareholder pool; the presence of third-party intermediaries like proxy advisors that can change the tenor of the relationship between a firm and its shareholder base; the increased prevalence of activist investors; and the use of automated trading algorithms, which make the benefits of personal outreach from management to shareholders all the more necessary.[19] Most of these dynamics have not been addressed by corporate governance regulations, such as the Sarbanes-Oxley Act of 2002 and the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010.[20] Part II posits that Shareholder Cultivation bridges the gap between top-down corporate governance rules and the changing realities of share ownership on one hand, and the actualization of stewardship, on the other.[21]

Part III employs new governance theory to unpack the corporate governance benefits of Shareholder Cultivation and develops a framework for assessing which cultivation techniques and strategies should be allowed.[22] The term "new governance" captures a range of regulatory activities and processes, which challenge the conventional wisdom that effective regulation should involve top-down regulation and command-and-control rules, while simultaneously rejecting a complete shift from top-down regulation towards pure market or self-regulation.[23]

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[16] *See infra* Part III.

[17] *See generally The UK Stewardship Code*, *supra* note 5 (outlining principles of effective investor stewardship in the United Kingdom); SKIPPER ET AL., *supra* note 9 (detailing current challenges in investor stewardship and proposing strategies for improving stewardship going forward).

[18] *See infra* Part II.

[19] *See infra* Part II.

[20] *See infra* Part II.

[21] *See infra* Part II.

[22] *See infra* Part III.

[23] *See infra* Part III.

The new governance paradigm seeks to identify both regulatory failures and market failures in a given space, and from this, devises complementary or "third-way" approaches that address these failures and enhance outcomes.[24] Additionally, recognizing that Shareholder Cultivation could be subject to abuse, Part III employs the Ayers-Gertner "immutable rule-default rule" construct to develop a prescriptive framework for determining the bounds and limits of acceptable Shareholder Cultivation activity.[25] As developed herein, the outward limits of cultivation would consist of immutable corporate law rules (inviolate rules that the parties cannot contract around), such as the rule that shareholders have a right to elect directors.[26] These immutable rules would be off limits to cultivation experimentation, and at the risk of stating the obvious, a violation of any of them would be considered illegal. By contrast, all default rules of corporate law (rules that the parties can contract around within the bounds of the rules—for example, the rules related to quorum whereby quorum can be increased or decreased beyond the statutory default, but in no event can it be less than one third) would be open to experimentation up to the point that they are limited by one or more of the immutable rules.[27]

Part IV transitions from theory to practice and provides a comprehensive analysis of actual *and* potential Shareholder Cultivation strategies.[28] Specifically, Part IV develops a taxonomy of cultivation tools and dissects the legal framework that makes deployment of these cultivation tools possible.[29] As described in Part IV, Shareholder Cultivation strategies can be visualized as falling along a cultivation

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[24]Orly Lobel, *New Governance as Regulatory Governance*, *in* THE OXFORD HANDBOOK OF GOVERNANCE 65, 65 (David Levi-Faur ed., 2012).

[25]*See* Ian Ayres & Robert Gertner, *Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules*, 99 YALE L.J. 87, 87 (1989).

[26]*See, e.g.*, DEL. CODE ANN. tit. 8, § 141(d) (2011) (permitting shareholders of a corporation to elect its directors for staggered terms); N.Y. BUS. CORP. LAW § 603 (McKinney 2003) (providing provisions for shareholders to elect directors in the event of a failure to elect a sufficient number of directors under normal circumstances).

[27]*See, e.g.*, DEL. CODE ANN. tit. 8, § 216 (2011), which reads in full:

> [T]he certificate of incorporation or bylaws of any corporation authorized to issue stock may specify the number of shares and/or the amount of other securities having voting power the holders of which shall be present or represented by proxy at any meeting in order to constitute a quorum for, and the votes that shall be necessary for, the transaction of any business . . . .

Id.

[28]*See infra* Part IV.

[29]*See infra* Part IV.A-F.

spectrum.[30] The first point on the cultivation spectrum consists of "pre-cultivation" activities, which include the firm's articulation of its purpose and value proposition.[31] The second spectrum point consists of identification tools, which assist firms in identifying potential shareholder stewards,[32] and the third point consists of "enlistment and re-enforcement tools," which include cultivation techniques to attract and enlist stewardship shareholders.[33]

In addition to providing a comprehensive treatment of *current* activities in which companies engage and which serve a cultivation purpose, Part IV also proposes *future* Shareholder Cultivation strategies that firms could employ to cultivate shareholder stewards.[34] Among the strategies proposed in Part IV are (i) the issuance of shares that have superior voting rights and economic rights, and which could be issued to targeted shareholders who commit to fulfilling certain mission-sustaining criteria (what I term "MY Shares" or "Mission-Yield Shares");[35] (ii) the implementation of a "time-weighted dividend" policy whereby the dividends that a shareholder receives would be dependent on the length of time that the shareholder owns stock in the company, so that long-term shareholders would be rewarded more than short-term shareholders;[36] (iii) the implementation of a "mission-weighted" dividend policy, which would be similar to a time-weighted dividend policy, except that the amount of dividend received would be contingent on whether the shareholder fulfilled certain mission-sustaining criteria;[37] (iv) a shareholder loyalty rewards point program, whereby shareholders could earn points based on their length of time as shareholders or on the basis of satisfying specified mission-sustaining criteria, and such points could be "redeemed" for additional shares or for certain products or services produced by the firm;[38] (v) a transaction tax as incentive for stewardship;[39] (vi) integrated reporting of financial, environmental, and social performance;[40] and (vii) within the confines of existing law, the suspension of shareholder voting rights for the *extreme* case where

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[30] *See infra* Part IV.A.
[31] *See infra* Part IV.B.
[32] *See infra* Part IV.C.
[33] *See infra* Part IV.D.
[34] *See infra* Part IV.F.
[35] *See infra* Part IV.F.1.
[36] *See infra* Part IV.F.2.
[37] *See infra* Part IV.F.3.
[38] *See infra* Part IV.F.7.
[39] *See infra* Part IV.F.6.
[40] *See infra* Part IV.F.5.

shareholders abuse their status *qua* shareholders.[41] For each of the proposed cultivation strategies discussed, Part IV analyzes the legal framework across state law, federal law, and stock exchange listing rules and provides an outline for implementation.[42]

Part V assesses the benefits and costs of Shareholder Cultivation both to individual firms and in the aggregate.[43] Key benefits of Shareholder Cultivation include the encouragement of stewardship capital,[44] enhanced thought-partnering between shareholders and managers,[45] and the use of Shareholder Cultivation as a potential anti-takeover device.[46] Simultaneously, however, Part V recognizes that the arguments put forth in this Article are subject to critique, such as whether Shareholder Cultivation will lead to entrenched interests;[47] whether Shareholder Cultivation will increase the transaction costs of share ownership;[48] suspicion about the effectiveness of Shareholder Cultivation for a large public corporation, especially in light of the fact that most shares are held through institutional intermediaries;[49] and whether Shareholder Cultivation runs afoul of agency theory by diminishing the monitoring function that corporate governance wants shareholders to serve.[50] Part V addresses each of these critiques in turn and demonstrates that corporate law's existing package of immutable rules and default rules help to constrain these costs and risks of abuse, and that on balance, Shareholder Cultivation could enhance governance outcomes.[51]

In conclusion, Shareholder Cultivation is poised to play an active role in future governance design. It represents a bottom-up, collaborative, "third-way" approach to governance design, which can help overcome some of the market failures and regulatory failures that have proven problematic for traditional corporate governance approaches.[52]

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[41] *See infra* Part IV.F.4.

[42] *See infra* Part IV.F.1-7.

[43] *See infra* Part V.

[44] *See infra* Part V.A.1.

[45] *See infra* Part V.A.5.

[46] *See infra* Part V.A.3.

[47] *See infra* Part V.B.2.

[48] *See infra* Part V.B.1.

[49] See *infra* Part V.B.3 for further discussion on the need for institutional investor-specific cultivation strategies.

[50] *See infra* Part V.B.2.

[51] *See infra* Part V.B.3.

[52] *See infra* Part III.

II. THE CURRENT STATE OF PLAY

The Organisation for Economic Co-operation and Development (the "OECD") defines corporate governance as "the system by which business corporations are directed and controlled," and notes that a "corporate governance structure specifies the distribution of rights and responsibilities among different participants in the company, such as the board, managers, shareholders, and other stakeholders, and spells out the rules and procedures for making . . . decisions on corporate affairs."[53] One of the goals of corporate governance is to design governance structures and systems which encourage boards and managers to make decisions that benefit the long-term interests of the firm and its shareholders.[54] However, recurrent episodes of firm actions that proved detrimental to the long-term interests of both the firm and its shareholders (and oftentimes, to the economy as a whole) highlight the need for constant re-evaluation of the efficacy of corporate governance rules and policies.[55] Examples of such episodes include the 1980s saving and loan crisis; the catastrophic demises of companies like Enron, Worldcom, and Global Crossing in 2001-2002, largely blamed on abuses of power and lack of accountability, transparency, and oversight of corporate executives; and the 2008 financial crisis.[56] As the OECD

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[53]ORG. FOR ECON. CO-OPERATION & DEV., CORPORATE GOVERNANCE OF NON-LISTED COMPANIES IN EMERGING MARKETS 15 n.2 (2006), http://www.ifc.org/wps/wcm/connect/582f0a804af4b8b8a5cfb5b94e6f4d75/oecd_nonlist.pdf?MOD=AJPERES.

[54]*See* Shlensky v. Wrigley, 237 N.E.2d 776, 780 (Ill. App. Ct. 1968) (holding the board's considerations of community effects are rational business decisions that support the long-term viability of the company); Adrian Cadbury, *Report of the Committee on the Financial Aspects of Corporate Governance*, EUR. CORP. GOVERNANCE INST. § 6.6 (Dec. 1, 1992), http://www.ecgi.org/codes/documents/cadbury.pdf (stating that boards are accountable to shareholders who comply with the code because the board acts as stewards on behalf of the shareholders); ASPEN INST., LONG-TERM VALUE CREATION: GUIDING PRINCIPLES FOR CORPORATIONS AND INVESTORS §§ 1-2 (2007), http://www.aspeninstitute.org/sites/default/files/content/docs/bsp/FinalPrinciples.pdf (presenting that a company's and an investor's implementation of long-term incentives and measures benefit one another); ROBERT CHARLES CLARK, CORPORATE LAW 18 n.46 (Little, Brown & Company, 1986) (explaining that maximizing profits means accounting for the "long-range results" of a business); ORG. FOR ECON. CO-OPERATION & DEV., OECD PRINCIPLES OF CORPORATE GOVERNANCE 58-61 (2004) [hereinafter OECD PRINCIPLES], http://www.oecd.org/corporate/ca/corporategovernanceprinciples/31557724.pdf (discussing the responsibilities of the board to include acting in good faith and with due diligence and high ethical standards for the benefit of the company and the shareholders).

[55]*See infra* note 56 and accompanying text.

[56]*See* Davita Silfen Glasberg & Dan Skidmore, *The Dialectics of White-Collar Crime: The Anatomy of the Savings and Loan Crisis of Silverado Banking, Savings and Loan*

acknowledged in its "Principles of Governance," "[t]he [2008] financial crisis revealed severe shortcomings in corporate governance. When most needed, existing standards failed to provide the checks and balances that companies need in order to cultivate sound business practices."[57] In response to these "revealed shortcomings" the OECD developed an "ambitious action plan" which identified four "priority areas" for improvement—"remuneration, risk management, board practices, and the exercise of shareholder rights."[58]

Additionally, several voices from both the public and private sectors have drawn attention to other simmering problems, which regulators have either not addressed or have been slow to address.[59] Such problems include: absentee share ownership, which manifests in the form of empty voting;[60] the perceived abuses of shareholder privileges by some activist investors;[61] the unease with the practices and influence of third-party proxy advisors;[62] the increased presence of short-term arbitrageurs;[63] and the vulnerabilities created by high-speed trading platforms.[64]

Association, 57 AM. J. ECON. & SOC. 423, 445 (1998) (discussing that the savings and loan crisis was the result of a lack of corporate oversight); *see also* Joseph A. Petrick & Robert F. Scherer, *The Enron Scandal and the Neglect of Management Integrity Capacity*, 18 AM. J. BUS. 37, 38 (2003) (stating at the core of the Enron crisis was the neglect of managerial integrity); *WorldCom: Accounting for Change*, ECONOMIST, June 29, 2002, http://www.economist.com/node/1200748 (stating that the misdeeds at Enron, Global Crossing and WorldCom are examples of abuse).

[57]OECD PRINCIPLES, *supra* note 54, at 58-61.

[58]*Id.*

[59]*See infra* notes 60-64 and accompanying text.

[60]*See* Henry T. C. Hu & Bernard Black, *Empty Voting and Hidden (Morphable) Ownership: Taxonomy, Implications, and Reforms*, 61 BUS. LAW. 1011, 1069-70 (2006) (concluding that hedge-fund shareholders participate in new vote buying, which leads to empty voting); *see also* Proxy System, Exchange Act Release No. 34-62495, July 14, 2010 (discussing empty voting).

[61]*See* Iman Anabtawi & Lynn Stout, *Fiduciary Duties for Activist Shareholders*, 60 STAN. L. REV. 1255, 1307 (2008) (concluding that activist investors engage in leveraging schemes on behalf of shareholders).

[62]*See* Tamara C. Belinfanti, *The Proxy Advisory and Corporate Governance Industry: The Case for Increased Oversight and Control*, 14 STAN. J.L. BUS. & FIN. 384, 438 (2009) (arguing that third-party proxy advisors are less accountable and more problematic to corporate management); *see also* Proxy System, Exchange Act Release No. 34-62495 (explaining that third-party proxy advisors do not always possess the requisite vote information for shareholders).

[63]*See* BOGLE ET AL., *supra* note 5, at 2 (presenting the problems associated with short-term investors).

[64]*See* Nathaniel Popper, *Knight Capital Says Trading Glitch Cost It $440 Million*, N.Y. TIMES, Aug. 2, 2012; Jenny Strasburg & Jacob Bunge, *Loss Swamps Trading Firm: Knight Capital Searches for Partner as Tab for Computer Glitch Hits $440 Million*, WALL ST. J., Aug. 3, 2012 (reporting that high-speed computer trading systems caused a corporation

Furthermore, the notion of shareholders as owners has become more nebulous and attenuated as shareholders become more heterogeneous and transient.[65] For example, a single company's shareholder base could include individual shareholders who invest because they like the company's goods or services; institutional investors such as pension funds or mutual funds, whose primary duty is to their respective investors; index funds whose managers may not necessarily care about the individual company's performance, but are more concerned about matching the index; short-term speculators who benefit from market fluctuations and instability; and "tape readers," who trade in bursts and have minimal interest in understanding the business of the companies behind the shares.[66] Thus the concern for companies is that share ownership has become disembodied from the long-term health and interests of the firm.[67] Shareholder Cultivation attempts to reconnect ownership to the firm, so that ownership becomes what Marjorie Kelly terms more "rooted" in the values and interests of the firm, rather than being connected solely in the intangible realm of the Committee on Uniform Securities Identification Procedure ("CUSIP") and stock registers.[68]

Moreover, a larger point emerges from the above picture: the fast-paced, interconnected, and dynamic nature of today's capital markets and share ownership place corporate governance policymakers in the uncomfortable position of having constantly to play regulatory catch-up.[69] The capital market landscape, like the broader society of which it is

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millions of dollars because of a slight glitch).

[65] *See infra* note 66 and accompanying text.

[66] *See, e.g.*, James Sterngold & Jenny Strasburg, *For SAC, a Shift in Investing Strategy Later Led to Suspicions: After Steven Cohen's Hedge Fund Turned Focus to Market-Moving Info, Regulators Grew Wary*, WALL ST. J., July 24, 2013 (discussing how short-term, stock-trading companies have little vested interest in the companies in which they invest).

[67] *See infra* note 68 and accompanying text.

[68] MARJORIE KELLY, OWNING OUR FUTURE: THE EMERGING OWNERSHIP REVOLUTION 104-05, 167-68 (2012) (stating that firms engaging in rooted membership create an environment in which employees' work and stewardship become a tangible connection to the success of the firm). The CUSIP is a nine character alphanumeric code assigned to all North American financial securities that facilitates the clearance and settlement of security trades. *See* LOAN SYNDICATION & TRADINGS ASS'N CUSIP GUIDELINES 3 (2011), http://www.lsta.org/WorkArea/DownloadAsset.aspx?id=15110. While CUSIPs obviously serve an important clearance and settlement function, the point is that stewardship share ownership should involve a more tangible and meaningful connection to the underlying company and its mission. *See id.*

[69] *Cf.* Cary Coglianese et al., HARV. UNIV., *The Role of Government in Corporate Governance*, 6 (2004), http://www.hks.harvard.edu/var/ezp_site/storage/fckeditor/file/pdfs/centers-programs/centers/mrcbg/programs/rpp/reports/RPPREPORT8.pdf (finding that the government is often playing

a part, is more interconnected, more digitized, more virtual, and more dynamic with the result of a gulf widening between regulatory prescriptions and present reality.[70] As new technologies, new investment vehicles, and new trading strategies emerge, one can only expect that the gap between regulatory responses and perceived on-the-ground problems will continue to widen in an unprecedented way.[71]

One solution to filling the gap between problem and response lies in engaging private parties and bottom-up, collaborative initiatives that respond to a given problem. Shareholder Cultivation arguably serves this gap-filling function and normatively meshes with the new governance paradigm, which advocates for a complementary approach in interconnected and dynamic environments, such as the corporate governance space.

III. NEW GOVERNANCE AND A FRAMEWORK FOR CULTIVATION

New Governance is "a school of thought that focuses on the significance of institutional design and culture for effective and legitimate regulation."[72] New governance scholars simultaneously challenge the conventional wisdom that effective regulation should involve top-down and command-and-control rules, while rejecting a complete shift from top-down government toward pure market or self-regulation.[73] In doing so, new governance provides a "third-way approach" that bridges the divide between self-governance and unregulated markets on one hand, and top-down government controls on

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catch-up to organizations).

[70] *See id.*

[71] *See id.*

[72] Lobel, *supra* note 24, at 65.

[73] *Id. See generally* IAN AYRES & JOHN BRAITHWAITE, RESPONSIVE REGULATION: TRANSCENDING THE DEREGULATION DEBATE (1992) (discussing the government's need to adopt a new approach to deregulation to increase market efficiency); Cristie Ford, *New Governance in the Teeth of Human Frailty: Lessons from Financial Regulation*, 2010 WIS. L. REV. 441, 445 (arguing for the adoption of a pragmatist approach involving empirical experiences, flexibility, and humility); Orly Lobel, *The Renew Deal: The Fall of Regulation and the Rise of Governance in Contemporary Legal Thought*, 89 MINN. L. REV. 342, 466-67 (2004) (arguing for the adoption of the Renew Deal approach requiring economic efficiency, political legitimacy, and social democracy); Charles F. Sabel & William H. Simon, *Destabilization Rights: How Public Law Litigation Succeeds*, 117 HARV. L. REV. 1015, 1100-01 (2004) (arguing that the adoption of the experimentalist approach avoids the defects of rule-bound intervention and is responsive to judicial concerns); Joanne Scott & Susan Sturm, *Courts as Catalysts: Re-thinking the Judicial Role in New Governance*, 13 COLUM. J. EUR. L. 565, 567 (2007) (arguing for the adopting of a catalyst approach, as used by European courts, to promote legitimate-and-effective governance decisions).

the other.[74] In analyzing a given context, new governance scholars often begin with a critical examination of both market failures and governance failures that exist in a given space, with the hope of developing a systematic map of the "range of possibilities in the interaction between regulation and regulated actors . . . ."[75] While "new governance strategies spring from a discontent with the results produced by traditional [top-down] techniques . . . . [i]n their willingness to synthesize an emerging social vision, [new governance] scholars and policy-makers move beyond entrenched and failed government structures while resisting simplistic attacks on the role of government intervention."[76]

In a new governance frame, regulated entities are not simply regulatory *objects*, but instead are recognized and become engaged as "norm-generating *subjects*."[77] In doing so, new governance aims to create a participatory, cooperative, and collaborative form of governance that responds to the failures of both markets and regulators, and which is both effective and legitimate.[78] New governance can be conceptualized as a governance paradigm that "attempts to renew and intervene in otherwise stalemated debates."[79]

One schema for conceptualizing the new governance approach was developed by noted new governance scholar, Orly Lobel.[80] Professor Lobel "describe[s] the new governance model of regulation as consisting of eight clusters of approaches[:] . . . (1) increased participation of non-state actors; (2) public–private collaboration; (3) diversity and competition within the market; (4) decentralization; (5) integration of policy domains; (6) non-coerciveness ('soft law'); (7) adaptability and constant learning; [and] (8) coordination."[81] First, the new governance frame explicitly requires the participation of private actors in the creation, implementation, and enforcement of regulatory norms and rules because it "challenges the conventional assumptions" that traditional regulatory bodies have "superior knowledge, information, and expertise" than the private actors which they seek to regulate.[82] The second approach of public–private collaboration is a natural corollary to the first

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[74]Lobel, *supra* note 24, at 68-69.
[75]*Id.* at 65.
[76]*Id.* at 70.
[77]*Id.* at 67 (emphasis added).
[78]*See* Lobel, *supra* note 24, at 67.
[79]*Id.* at 69.
[80]*See infra* notes 81-91 and accompanying text.
[81]Lobel, *supra* note 24, at 66.
[82]*Id.*

and furthers the recognition that cooperation and collaboration between regulatory bodies and regulated entities should lead to enhanced governance outcomes.[83] Similarly, the "diversity and competition" approach refers to the idea "that a sustainable legal regime must encompass a multitude of values, account for conflict and compromise, acknowledge the diversity and changing interests of many participants, and recognize the legitimacy of private economic interests while appealing to public values."[84] Relatedly, the concept of decentralization reflects the notion that the locus of regulation is not solely the state, but that the private sector has regulatory agency in the creation and promotion of governance norms and values.[85] The fifth approach in new governance—"integration of policy domains"—attempts to connect seemingly dispersed issues across seemingly distinct domains with the view that often these issues are "nonetheless connected at the level of those who are most influenced by them . . . ."[86] Thus, for example, in a traditional regulatory model, laws are fragmented into different domains, such as securities regulation, environmental regulation, and food and safety.[87] In a new governance frame, the involvement of private actors, the collaboration between public and private, the decentralization of agency, and the principle of diversity and competition, "all potentially lead to revealing the ways in which dispersed issues . . . are nonetheless connected at the level of those who are most influenced by them."[88] Continuing the theme of collaboration, the principle of non-coerciveness refers to new governance's aim to create a more flexible, open, and collaborative environment that is "more conducive to participation and

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[83] *See id.* at 67. The recognition of the importance of input from private actors and the benefits of public–private collaboration are not unique to the new governance frame. *See, e.g.*, *Rulemaking, How It Works*, U.S. SEC. & EXCH. COMM'N, http://www.sec.gov/answers/rulemaking.htm (last modified Apr. 6, 2011). For example, administrative agencies like the SEC often invite collaboration and private-actor input in their rulemaking process through their "notice and comment" framework, which allows any interested party to formally contribute their thought to the proposed rule. *See id.* Where the new governance frame differs, however, is that new governance views the "different sectors" of society—"state, market, and civil society—as part of one comprehensive, interlocking system. . . . [in which] individuals are . . . involved in the process of developing and changing the norms of behavior, in contrast to [a top-down model], under which private actors are the objects of regulation." Lobel, *supra* note 24, at 67.

[84] Lobel, *supra* note 24, at 67.

[85] *See id.*

[86] *Id.*

[87] *See id.*

[88] Lobel, *supra* note 24, at 67.

dialogue."[89] The adaptability and constant learning strand echoes this notion of flexibility and recognizes that questions of "what works and what fails . . . must be constantly examined and re-examined."[90] Finally, the eighth approach of coordination primarily refers to a key role of the state and regulatory agencies in the new governance frame, which is to facilitate "the communication of local knowledge and the structured interactions of separate groups[,]" both to "foster a culture of compliance within regulated industries," and to "promote and standardize innovations that began locally and privately."[91]

A. *New Governance in Corporate Governance*

In applying new governance learning to the corporate governance space we confront the question of identifying market and governance failures that occupy the space.[92] Examples of market failures include the aforementioned savings and loans crisis in the 1980s;[93] the accounting scandals that led to the demise of several large corporations in the early 2000s;[94] the subprime mortgage crisis, which has been blamed on unscrupulous lending practices by banks;[95] and the 2008 financial crisis.[96] In each of these instances of market failure, government intervened with new laws and regulations intended to prevent a recurrence of market breakdown.[97]

In identifying regulatory failures in the corporate governance space, the description espoused by Professor Saule Omarova is

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[89] *Id.*

[90] *Id.*

[91] *Id.* at 67, 71.

[92] *See infra* notes 93-97 and accompanying text.

[93] *See generally* FED. DEPOSIT INS. CORP., THE SAVINGS AND LOAN CRISIS AND ITS RELATIONSHIP TO BANKING, ch. 4 (1997) [hereinafter S&L CRISIS], *available at* http://www.fdic.gov/bank/historical/history/167_188.pdf ("The vast number of actual and threatened insolvencies of savings and loan associations in the 1980s was predictable because of the interest-rate mismatch of the institutions' balance sheets.").

[94] *See* Petrick & Scherer, *supra* note 56, at 38.

[95] *See* Charles W. Calomiris, *The Mortgage Crisis: Some Inside View*, WALL ST. J., Oct. 27, 2011, http://online.wsj.com/news/articles/SB10001424053111903927204576574433454435452.

[96] *See* Glasberg & Skidmore, *supra* note 56, at 445.

[97] *See, e.g.*, Sarbanes-Oxley Act of 2002, 15 U.S.C. § 7243 (2006); Troubled Asset Relief Program, 12 U.S.C. § 5211 (Supp. 2008); Dodd-Frank Wall Street Reform and Consumer Protection Act 15 U.S.C. § 78j-4 (Supp. IV 2011); S&L CRISIS, *supra* note 93, ch. 4.

particularly helpful.[98] Professor Omarova categorizes regulatory failures as the "inability [of government] to design appropriately sophisticated and effective legal and policy instruments to address complex social problems (instrument failure), inadequate implementation of the rules (implementation failure), and failure to motivate the regulated entities and individuals to comply with the rules (motivational failure)."[99] With respect to instrument failure in the corporate space, one might point to the 2003 U.S. Securities and Exchange Commission ("SEC") rule—which in an effort to encourage mutual funds to exercise their fiduciary duties in a more responsible way, mandated that mutual funds publicly disclose how they vote.[100] The SEC did not, however, anticipate that the effect of this rule would be to incentivize mutual funds to further outsource voting logistics to third-party proxy advisor intermediaries, who in turn have brought a whole new slew of governance problems.[101]

Similarly, the reaction by regulated entities to the 1993 federal tax law amendments is illustrative of implementation failure.[102] The amended tax provisions were intended to curb perceived excesses in executive compensation and provided that companies could not deduct, as a business expense, compensation paid to an executive in excess of one million dollars unless such compensation was linked to an objective measure of corporate performance.[103] Instead of curbing the amount of compensation, the 1993 tax amendments simply had the effect of limiting the salary portion to one million dollars, while the incentive pay portion skyrocketed.[104] Of the three regulatory failures articulated by Omarova, motivational failure is most difficult to measure.[105] However, indicators of motivational failure, such as a failure to comply with insider

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[98]*See infra* note 99 and accompanying text.

[99]Saule T. Omarova, *Rethinking the Future of Self-Regulation in the Financial Industry*, 35 BROOK. J. INT'L L. 665, 672 (2010).

[100]Disclosure of Proxy Voting Policies, Investment Company Act Release No. 25,739, Sept. 20, 2002.

[101]*See* Belinfanti, *supra* note 62, at 393-94. While mutual funds and other registered management investment companies are required to disclose their proxy voting records on an annual basis on Form N-PX, the concern here is not with disclosure but with the potential influence that proxy advisors may have on the mutual funds' voting decision. Annual Report of Proxy Voting Record of Registered Management Investment Company (Form N-PX), *available at* http://www.sec.gov/about/forms/formn-px.pdf.

[102]*See* Tod Perry & Marc Zenner, *CEO Compensation in the 1990s: Shareholder Alignment or Shareholder Expropriation?*, 35 WAKE FOREST L. REV. 123, 127 (2000).

[103]*See id.* at 128-29.

[104]*See id.* at 131.

[105]*See* Omarova, *supra* note 99, at 672.

trading rules, may also be symptomatic of both implementation and instrument failures.[106]

More broadly speaking, corporate governance may have a "stalemate" problem both in terms of approach and in terms of the inability of its regulated constituents, i.e., corporate executives and shareholders, to agree on what is needed to enhance governance outcomes.[107] In general, shareholders view the solution as more "shareholder rights" and "shareholder democracy," while executives view the solution as controlling abusive shareholder practices and honoring corporate law's default choice that assigns the power to manage the "business and affairs" to the board and officers.[108] Thus, while corporate governance aims to design rules that encourage alignment between the interests of shareholders and those of managers, the current relationship between managers and shareholders in general can hardly be described as aligned or effective.[109] There is mutual mistrust between both groups and this mistrust may be further aggravated by corporate governance rules and policies that do not necessarily address the realities of the relationship (what new governance's "diversity and competition" approach would view as a failure to "acknowledge the diversity and changing interests of [a multitude of] participants . . . .").[110] Moreover, the accusations that shareholders and managers levy at each other have not changed significantly—shareholders accuse managers of being greedy, unmotivated, and self-interested, while managers accuse shareholders of both being self-interested and not understanding the company's business (the aforementioned "stalemate" problem).[111] Top-down corporate governance policies, such as Sarbanes-Oxley and Dodd-Frank, while in many ways necessary to address certain market failures, have formalized and sanitized the shareholder–manager

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[106]*See id.*

[107]*See* Stephen M. Bainbridge, *The Board of Directors as Nexus of Contracts*, 88 IOWA L. REV. 1, 5-6 & n.16 (2002).

[108]*See id.* at 25; Lisa M. Fairfax, *The Future of Shareholder Democracy*, 84 IND. L.J. 1259, 1260 (2009); *see also* DEL. CODE ANN. tit. 8, § 141 (2011) ("The business and affairs of every corporation organized under this chapter shall be managed by or under the direction of a board of directors, except as may be otherwise provided in this chapter or in its certificate of incorporation.").

[109]*See* Fox & Lorsch, *supra* note 1, at 50.

[110]Lobel, *supra* note 24, at 67.

[111]*See* Fox & Lorsch, *supra* note 1, at 50, 56; *see also supra* note 107 and accompanying text.

relationship, but have arguably done very little to improve the underlying quality of the relationship.[112]

B. *Shareholder Cultivation as New Governance*

While the new governance paradigm often focuses on the interplay between the regulators and the regulated, Shareholder Cultivation primarily involves the interplay between a firm and its shareholders. Nonetheless, viewing Shareholder Cultivation through a new governance frame has analytical currency. In new governance parlance, Shareholder Cultivation is an example of an "innovation[ ]that began locally and privately"[113] in response to this stalemate problem and in response to the changing dynamics of share ownership.[114] Similarly, Shareholder Cultivation can be conceptualized as part of the "norm generating process," which in turn can then inform and influence how firms and policymakers think about corporate governance design. It potentially offers a "third-way approach" in corporate governance design, whereby managers leverage the heterogeneous dynamics of a firm's shareholder base to identify and cultivate a core of committed shareholders.[115]

More specifically, Shareholder Cultivation activates all "eight clusters" of the new governance approach described above[116]—first, it engages private actors and, through their collaboration, an innovative means of actualizing corporate governance can emerge;[117] second, it invites public or private collaboration;[118] third, it is arguably born out of the realization of the "diversity and competition" in capital markets, and as such, it recognizes the "diversity and changing interests of many stakeholders" and seeks to legitimize the private interests of the parties

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[112]*See* Fox & Lorsch, *supra* note 1, at 56-57; *see also* Lobel, *supra* note 24, at 76.

[113]Lobel, *supra* note 24, at 67.

[114]*See id.* at 69 (explaining that new governance tries to "renew and intervene" in disputes that are at a standstill as well as respond to the changes in the type of goods, commerce, work, and additional threats).

[115]*See id.* ("[P]olicymakers and scholars are focusing their attention on new governance as a set of legal strategies outside the traditional command-and-control toolbox that has the potential to increase the effectiveness and legitimacy of social regulation.").

[116]*See infra* Part III.

[117]*See, e.g.*, Lobel, *supra* note 73, at 371, 373-74 ("Increased participation [of private actors] permeates the many levels and stages of legal process . . . . [I]t enhances the ability of citizens to participate in political and civic life."); *see also* Lobel, *supra* note 24, at 66-67.

[118]*See* Lobel, *supra* note 73, at 376-77 ("It signifies a move to partnership, to horizontal relationships, and to two-way communications. The goal is to create microsystems of open communication in which policy is imagined, managed, and maintained.").

"while appealing to public values," such as long-term value creation and sustainability;[119] fourth, it decentralizes corporate governance practices and activities from state agencies back to the affected private parties;[120] fifth, in terms of "integration of policy domains," collaboration and knowledge-sharing between shareholder stewards and firm management could lead to enhanced thinking on how seemingly dispersed issues are connected and can be solved;[121] sixth, Shareholder Cultivation embodies new governance's "non-coerciveness approach" in that successful Shareholder Cultivation "create[s] an environment more conducive to participation and dialogue[]";[122] finally, the seventh and eighth approaches of "adaptability and constant learning" and "legal coordination" highlight the need to constantly assess Shareholder Cultivation practices and costs, as well as the role of regulatory bodies in capitalizing on—and scaling—successful cultivation practices and innovations.[123] As discussed in Part IV.D.3., there are various levers, such as communication rules or reporting best practices, that regulatory agencies can utilize to "promote and standardize" these cultivation practices and innovations.[124]

C. *The Cultivation Framework*

As previously noted, a necessary role of government under a new governance approach is to "foster a culture of compliance within regulated industries,"[125] and to "promote and standardize innovations that

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[119]*See id.* at 379-80.

[120]*See id.* at 381-85 (discussing four functions of decentralization including the following: encouraging governance interests, confirming the concept of subsidiarity, producing "relational density and synergy," and maintaining a setting conducive to democratic involvement).

[121]*See id.* at 385. The new governance theory considers the interrelationships of the multiple legal areas when faced with resolving an issue. *See id.* at 385-86.

[122]*See* Lobel, *supra* note 73, at 388 ("The [non-coerciveness approach] aims to create a flexible and fluid policy environment that fosters 'softer' processes that either replace or complement the traditional 'hard' ordering of the regulatory model.").

[123]For discussion on the seventh approach, see *id.* at 395-96, which stresses the need to continue learning in governance. For discussion on the eighth approach, see *id.* at 400-01, which notes that "[s]caling up, facilitating innovation, standardizing good practices, and researching and replicating success stories from local or private levels are central goals of government."

[124]*See infra* Part IV.D.3.

[125]Lobel, *supra* note 24, at 71 (explaining the various ways in which government agencies encourage compliance with the rules).

began locally and privately."[126] This Sub-Part contemplates how this could be achieved in the corporate governance space.[127] Chief among the concerns is how to determine which cultivation efforts on the part of private firms will be allowed and which ones are off limits. To facilitate this exercise of delineating the boundaries of cultivation and permissible cultivation practices (which can be visualized as a "cultivation zone" or "cultivation playing field"), the Ayres-Gertner construct of immutable rules and default rules is particularly helpful.[128]

In a 1989 law review titled *Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules*, Professors Ayres and Gertner argue that "[t]he legal rules of contracts and corporations [could] be divided into two distinct classes"—immutable rules and default rules.[129] "Immutable" rules consist of those rules that the parties could not "change by contractual agreement."[130] "Default" rules, on the other hand, consist of those classes of rules that "parties can contract around by prior agreement . . . ."[131] Ayres and Gertner conceptualize default rules as "fill[ing] the gaps in incomplete contracts," i.e., these default rules will "govern unless the parties contract around them."[132] As Ayers and Gertner note, corporate law rules can also be divided between these two classes of immutable rules and default rules.[133] For immutable rules, the authors cite, as an example, the rule regarding the rights of shareholders to "elect directors annually"; however, a default rule prescribes that most corporate statutes "allow the articles of incorporation to contract around the default rule of straight voting."[134] Other immutable corporate rules include the rule that shareholders have a right to vote on an amendment to the corporation's articles of incorporation and the rule that shareholders have a right to vote on a transaction that will result in the

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[126] *Id.* at 67; *see also supra* Part III.

[127] *See infra* Part III.C.

[128] *See* Ayres & Gertner, *supra* note 25, at 87-88 (describing the differences between immutable rules and default rules and including examples of each rule).

[129] *Id.* at 87.

[130] *Id.*

[131] *Id.*

[132] Ayres & Gertner, *supra* note 25, at 87.

[133] *See id.* at 91 (explaining that default rules can be divided into three categories: (1) penalty defaults, created to encourage at least one party to contract around the default rules; (2) tailored defaults, created to afford the parties with exactly what they would have asked for in the contract; and (3) untailored defaults, created to offer the parties to a contract a generic standard that is intended to represent what most parties to a contract would desire).

[134] *Id.* at 87-88.

sale or change of control of the firm.[135] Examples of other default corporate rules include rules regarding the setting of a record date, rules regarding the reimbursement of proxy expenses, and rules regarding special shareholder meetings.[136]

While Ayres' and Gertner's analysis centers on how lawmakers should choose among various default rules, it is beyond the scope of this article to question corporate law's choice of existing default rules.[137] The argument here is simply that an immutable-default rule construct is a useful analytical tool for thinking about the outer boundaries of Shareholder Cultivation and relatedly, the creation of permissible cultivation zones.[138] Thus, immutable corporate law rules would demarcate the outer boundaries of cultivation activities, while default corporate law rules would be within the zone of play.[139]

Finally, in a new governance frame, the immutable-default rule construct provides both regulators and regulated private parties with an operable framework for assessing the appropriateness of a given cultivation activity. A key role of regulators would consist of promoting and coordinating appropriate cultivation activities—through such actions as policy statements, SEC "no-action" letters, or best practice

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[135]*See* DEL. CODE ANN. tit. 8, § 242(b)(1) (2011) ("At the meeting a vote of the stockholders entitled to vote thereon shall be taken for and against the proposed amendment."); *Id.* § 271(a) ("[C]orporation[s] may at any meeting . . . sell, lease or exchange all or substantially all of its property and assets . . . when and as authorized by a resolution adopted by the holders of a majority of the outstanding stock of the corporation entitled to vote thereon . . . .").

[136]Section 213(a) of the Delaware General Corporation Law provides:

> If no record date is fixed by the board of directors, the record date for determining stockholders entitled to notice of and to vote at a meeting of stockholders shall be at the close of business on the day next preceding the day on which notice is given, or, if notice is waived, at the close of business on the day next preceding the day on which the meeting is held.

Id. § 213(a); *see also id.* § 113(a) ("The bylaws may provide for the reimbursement by the corporation of expenses incurred by a stockholder in soliciting proxies in connection with an election of directors, subject to such procedures or conditions as the bylaws may prescribe . . . ."); *Id.* § 211(d) ("Special meetings of the stockholders may be called by the board of directors or by such person or persons as may be authorized by the certificate of incorporation or by the bylaws.").

[137]*See* Ayres & Gertner, *supra* note 25, at 89, 91 (discussing the need to confirm the theory utilized when faced with selecting default rules).

[138]*See infra* Part III.C.

[139]For both immutable and default rules, such rules include not only "hard" rules formalized by statute or regulation, but would also include soft law, general norms, and policies, which, although not formalized, are generally recognized to be inviolate. *See* Lobel, *supra* note 73, at 388.

prescriptions—to create a safe zone for companies to engage in Shareholder Cultivation.

IV. FROM THEORY TO PRACTICE: SHAREHOLDER CULTIVATION TOOLS AND STRATEGIES

To be clear, the suggestion is not that a public corporation could cultivate its entire shareholder base. Rather, Shareholder Cultivation is about leveraging existing market conditions and legal rules to cultivate a stabilizing core of committed shareholders.[140] Several CEOs recognize this and openly express their views on the types of shareholders that are welcomed in their base and those who are not.[141] Warren Buffett, chairman of Berkshire Hathaway, is a prime example of a manager who explicitly embraces a Shareholder Cultivation ethos.[142] In June 1996, Buffett issued a manifesto to Berkshire's stockholders titled "An Owner's Manual" which laid out the company's business principles and managerial approach as well as the expectations Berkshire had of its shareholders.[143] The first principle outlined addressed Berkshire's view of the relationship it aspired to have and maintain with its shareholders.[144] Buffett wrote:

> [We] think of our shareholders as owner-partners . . . . [We] hope that you [the shareholder] do not think of yourself as merely owning a piece of paper whose price wiggles around daily and that is a candidate for sale when some economic or political event makes you nervous. We hope you instead visualize yourself as part owner of a business . . . . For our part, we do not view Berkshire shareholders as faceless members of an ever-shifting crowd, but rather as co-venturers . . . . Obviously, [we] can't control Berkshire's price. But by our policies and communications, we can

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[140] *See infra* Part IV.D.

[141] *See, e.g.*, BUFFETT, *supra* note 6, at 1 (1996), http://www.berkshirehathaway.com/ownman.pdf (explaining the expectations Buffett has for his shareholders).

[142] *See id.*

[143] *See id.*

[144] *See id.*

> encourage informed, rational behavior by owners that, in turn, will tend to produce a stock price that is also rational.[145]

Similarly, in his 1983 annual letter to shareholders, Buffett wrote, "Through our policies and communications . . . we try to attract investors who will understand our operations, attitudes and expectations. (And, fully as important, we try to dissuade those who won't)."[146]

Buffett's expressed sentiment of striving to "attract investors who will understand [Berkshire's] operations, attitudes and expectations" and of seeking out "co-venturers" is precisely what Shareholder Cultivation is about.[147] What counts as a "co-venturer" will differ from firm to firm, but it captures the concept of a shareholder steward. There is not, and there cannot be, one homogenous set of specific characteristics. Two characteristics of a shareholder steward, however, that should be invariable and constant across firms include: (1) the shareholder's investment behavior meshes with the firm's vision and operational strategy; and (2) the shareholder understands and is supportive of the firm's mission and management's long-term strategy. As discussed below, there are various techniques and heuristics that firms use to identify potential co-venturers.[148]

Conversely, for purposes of Shareholder Cultivation, it is equally important for a firm to determine and identify those shareholders whose investment behavior and belief system tend to indicate *non*-co-venturer characteristics. Indicators of non-co-venturer characteristics will also differ from firm to firm, but generally speaking, firms seem to have a preference for limiting shareholder arbitrageurs,[149] shareholders who engage in empty voting,[150] and activist shareholders who seek to impose their personal business judgment on management.[151] While some amount

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[145]BUFFETT, *supra* note 6, at 1, 4.

[146]Letter from Warren E. Buffett to Berkshire Hathaway Inc., *supra* note 11.

[147]*Id.*; BUFFETT, *supra* note 6, at 1 ("[We] view Berkshire shareholders as . . . co-venturers who have entrusted their funds to us for what may well turn out to be the remainder of their lives.").

[148]*See infra* Part IV.C.

[149]*See* Iman Anabtawi, *Some Skepticism About Increasing Shareholder Power*, 53 UCLA L. REV. 561, 580 & n.88 (2006) (noting that arbitrageurs take short-term gains at the expense of long-term performance to attract and retain investors).

[150]*See* Anabtawi & Stout, *supra* note 61, at 1280 ("[A] hedge fund can buy . . . stock and vote the shares while simultaneously entering a derivatives contract that hedges away its economic interest in stock. . . . and then seek to profit from using its power as a formal shareholder to push for business policies that drive the stock price *down*.").

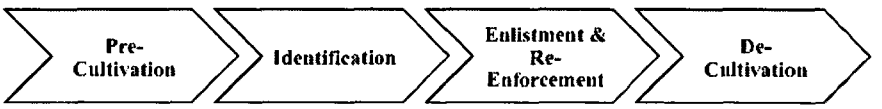
[151]*See id.* at 1270 (concluding a minority shareholder imposes its personal business

of short-term trading is beneficial to the firm in terms of, *inter alia*, increased liquidity and visibility for the firm's stock, as discussed below, firms tend to prefer a lower turnover rate to a higher one.[152]

A. *The Cultivation Spectrum*

Shareholder Cultivation tools can be conceptualized as falling along a spectrum—starting with pre-cultivation activities such as the art of effectively using narrative to engage a firm's mission;[153] through the identification and selection of potential shareholder stewards;[154] employing strategies to recruit potential stewards and in many cases, re-enforce or activate stewardship norms among existing shareholders;[155] and to de-cultivation efforts that attempt to shake or limit the attractiveness of the firm's shareholder base to gamblers and non-co-venturers.[156] Thus, in general one could visualize a cultivation spectrum as follows:

Cultivation Spectrum:



The assignment of tools to specific segments of the cultivation spectrum should be thought of as liminal rather than fixed. As discussed below, certain tools such as the adoption of a time-weighted dividend policy, for example, serve different purposes for different shareholders or would-be investors.[157] Thus, they occupy multiple points along the spectrum at any given period in time, or vacillate across different points of the spectrum at different points in time.[158]

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judgment on management when it substitutes its own judgment for the board of directors).

[152] *See, e.g.*, Fox & Lorsch, *supra* note 1, at 52 (finding the more influence short-term traders have on the market prices the more volatile those prices will be since short-term traders are less interested in the fundamental value of the corporation they are trading).

[153] *See infra* Part IV.B.

[154] *See infra* Part IV.C.

[155] *See infra* Part IV.D.

[156] *See infra* Part IV.E.

[157] *See infra* Part IV.F.2.

[158] *See infra* Part IV.F.2.

B. *Pre-Cultivation Tools: Defining Narrative and Embodying Mission*

The first step in the cultivation process is for the firm to define its mission and to systematically strive to ensure that its practices and policies embody and reflect that mission.[159] The firm's mission or purpose is its "*raison d'etre*."[160] A corporate purpose or mission should serve as a blueprint for the firm's decisions and actions.[161] State corporate laws give firms wide latitude in defining their purpose and mission.[162] For example, the Delaware General Corporation Law ("DGCL") provides that "[a] corporation may be incorporated or organized under this chapter to conduct or promote any lawful business or purposes . . . ."[163] Similarly, the Pennsylvania Business Corporations Act provides that "every business corporation has as its corporate purpose the engaging in lawful business for which corporations may be incorporated under the BCL."[164] Thus, state corporate laws leave a wide zone of play for firms to define their mission and purpose.[165]

The attendant benefits of defining a corporation's purpose and mission have been robustly dealt with in the managerial literature.[166] Those benefits can be summarized as "provid[ing] direction to strategy . . . bring[ing] meaning to the work of others . . . infus[ing] the

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[159]*See* PETER F. DRUCKER, MANAGEMENT: TASKS, RESPONSIBILITIES, PRACTICES 75 (1974) [hereinafter DRUCKER, MANAGEMENT] ("Only a clear definition of the mission and purpose of the business makes possible clear and realistic business objectives.").

[160]RICHARD R. ELLSWORTH, LEADING WITH PURPOSE: THE NEW CORPORATE REALITIES 4 (2002). "*Raison d'etre*" means "overriding reason for existing." *Id.*

[161]*See, e.g.*, DRUCKER, MANAGEMENT, *supra* note 159, at 75.

[162]*See infra* notes 163-64 and accompanying text.

[163]DEL. CODE ANN. tit. 8, § 101(b) (2011).

[164]19 PA. CODE § 23.4(b) (2013).

[165]Although the terms "mission" and "purpose" are often used interchangeably, in practice a firm's "purpose" can be found in its articles of incorporation and is often more terse and concise than its "mission", which is often put forth in its mission statement and which tends to be more expansive than the "purpose" stated in the firm's articles of incorporation. *See* ELLSWORTH, *supra* note 160, at 97 ("Purpose defines the cause. The mission gives it depth and richness.").

[166]*See generally* CHESTER I. BARNARD, THE FUNCTIONS OF THE EXECUTIVE 42 (Harvard Univ. Press, 30th Anniversary ed. 1966) ("A formal system of cooperation requires an objective, a purpose, an aim."); PETER F. DRUCKER, CONCEPT OF THE CORPORATION 176 (Harper & Row, 2d rev. ed. 1983) ("If the corporation does not have a clear policy and a definite organ of policy decision, its actions and behavior become unpredictable."); DRUCKER, MANAGEMENT, *supra* note 159, at 74 ("A clear, simple, and penetrating theory of the business rather than intuition characterizes the truly successful . . . organization that can endure and grow . . . ."); ELLSWORTH, *supra* note 160, at 2 ("[L]eadership's failure to define a clear purpose . . . explains much of the tension, conflict, and ambivalence that inflict American companies today.").

organization with value, and consequently . . . stimulat[ing] commitment and action."[167]

One chief executive officer expressed the sentiment as such:

> I believe a clear purpose is an essential building block in the foundation of a more responsible capitalism. You can't achieve your purpose in a quarter, or a year. It serves as a statement of why a company exists, and more fundamentally why a company merits having a corporate charter and receive the protections of society.[168]

For Shareholder Cultivation, "a clear purpose is an essential building block" for attracting and recruiting shareholder stewards —but for it to serve this role, the firm's purpose must actually become embodied in its practices and policies.[169]

A firm's mission should then inform the narrative that the firm develops to explain its value proposition and operational strategies to shareholders, other stakeholders, and society at large.[170] For many corporations their narrative is often memorialized in their mission statements.[171] However, to be an effective cultivation tool, it should also carry through to communications with shareholders and other stakeholders, the company's annual reports, sell-side-analyst calls, executive compensation practices, and any other points of interface that the company has with stakeholders and external constituents which provide an opportunity for the company to reiterate its story and its value proposition.[172]

PepsiCo, Inc.'s interwoven approach to mission and narrative provides a case in point. PepsiCo divides its narrative into three component parts: (1) "Our Mission"; (2) "Our Vision"; and (3)

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[167]ELLSWORTH, *supra* note 160, at x.

[168]David H. Langstaff, President and CEO of TASC, Inc., Address at the Kellogg School of Management/Aspen Institute Business and Society Conference: Rethinking 'Shareholder Value,' the Purpose of the Corporation (March 7-8, 2013), http://www.aspeninstitute.org/sites/default/files/content/upload/Tomorrow%27s%20Corporation-March%207%202013.pdf?width=100.

[169]*See id.*

[170]Telephone Interview with Julie Tracy, Senior Vice President and Chief Commc'ns Officer, Wright Med. Grp. (Jan. 14, 2013).

[171]*See infra* notes 173-75 and accompanying text.

[172]*See* ELLSWORTH, *supra* note 160, at 327-28 (finding the leader is responsible for presenting the firm's characteristics, including its mission, to the marketplace, customers, employees, shareholders, and communities).

"Performance With Purpose."[173] The details of its narrative are found in its mission statement, which, under the "Performance With Purpose" subheading, states that:

> At PepsiCo, we're committed to achieving business and financial success while leaving a positive imprint on society - delivering what we call Performance with Purpose.
>
> Our approach to superior financial performance is straightforward - drive shareholder value. By addressing social and environmental issues, we also deliver on our purpose agenda, which consists of human, environmental, and talent sustainability.[174]

The company's mission is thus embedded in its narrative, and in turn, its narrative threads through to its annual report, which repeatedly uses terms such as "organic revenue," "growth," "sustainability," and "long-term," which all capture and convey the spirit of Pepsi's mission statement and signal to the market that Pepsi is about "shareholder value" *and* value to society.[175] Similarly, Pepsi's narrative of financial success, along with societal benefit, is reflected in its approach to executive compensation where at least some portion of compensation is tied to non-financial metrics.[176]

As pre-cultivation tools, mission-embodying and successfully weaving a narrative are important for attracting and retaining shareholder stewards in several ways and can be effective along different points of the cultivation spectrum.[177] First, mission and narrative can serve as recruiting tools to explain the firm's value proposition and vision to potential shareholders.[178] In this regard, they serve both a framing and benchmarking function in that they provide target shareholders with a reference point and framework for thinking about and assessing the

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[173] *Our Mission & Values*, PEPSICO.COM, http://www.pepsico.com/Purpose/Our-Mission-and-Values (last visited Oct. 19, 2013).

[174] *Id.*

[175] *See* PepsiCo, Annual Report (Form 10-K), at 2, 7 (Feb. 21, 2013).

[176] *See Pepsico 2011/2012 GRI Report*, PEPSICO.COM, 23-24 (2011-2012), http://www.pepsico.com/Download/PEP_RPT12_GRI%20Report_v5.pdf.

[177] *See* Langstaff, *supra* note 168, at 9.

[178] *See* DRUCKER, MANAGEMENT, *supra* note 159, at 75 (emphasizing only a clear definition of the mission will make possible realistic business objectives).

firm's financial and non-financial value.[179] Similarly, for the firm's agents (for example, managers, directors, or its investor-relations department), a tightly written mission and narrative provide a rhetorical frame that can be used to shape discussion with both current shareholders and potential investors, and advance the firm's goals and value proposition in a consistent and effective way.[180] As is well-documented in the behavioral literature, the way we frame and name things affect how they are perceived by others.[181] A classic example is that when an identical scenario is framed as a loss rather than as a gain, people are more incentivized to avoid the scenario because the fear of loss has a more powerful grip over a person's psyche than the possibility of gain.[182]

Secondly, mission and narrative can also serve as identification tools because when successfully executed, they can incentivize self-identification and self-selection by potential shareholder stewards with whom the firm's mission and narrative resonate. Moreover, because self-identifying by shareholders involves significantly less cost outlay on the part of the company compared to the cost of the company engaging in separate identification strategies (as discussed below), mission and narrative that result in shareholder self-identification have the benefit of lowering transaction costs to the firm.[183]

Finally, in terms of the immutable and default rule construct developed in Part I, pre-cultivation tools of mission and narrative operate within a wide zone of latitude with the outward bounds being defined by immutable rules such as the requirement that the firm be operated for a "lawful" purpose.[184]

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[179] *See* GEORGE LAKOFF, DON'T THINK OF AN ELEPHANT!: KNOW YOUR VALUES AND FRAME THE DEBATE 3-4 (2004); Amos Tversky & Daniel Kahneman, *The Framing of Decisions and the Psychology of Choice*, 211 SCI. 453, 453 (1981); *see also* George Lakoff, *Simple Framing: An Introduction to Framing and Its Uses in Politics*, ROCKRIDGE INST., (Apr. 3, 2007) http://archives.evergreen.edu/webpages/curricular/2006-2007/languageofpolitics/files/languageofpolitics/Simple%20Framing%20Rockridge%20Institute.pdf ("Communication itself comes with a frame. The elements of the Communication frame include: A message, an audience, a messenger, a medium, images, a context, and especially, higher-level moral and conceptual frames. The choice of language is, of course, vital, but it is vital because language evokes frames—moral and conceptual frames.").

[180] *See* Lakoff, *supra* note 179.

[181] *Id.* For an example of framing techniques in corporate law, see Tamara C. Belinfanti, *Beyond Economics in Pay for Performance*, 41 HOFSTRA L. REV. 91, 149-50 (2012), which explores the potential use of framing to encourage certain outcomes in executive compensation policies.

[182] *See* Belinfanti, *supra* note 181, at 150.

[183] *See infra* Part VI.B.1.

[184] DEL. CODE ANN. tit. 8, § 101(b) (2011).

C. *Identification and Sorting: Separating Stewards from Gamblers*

Once a corporation has defined its mission and narrative (as discussed above), it is in a position to narrow the universe of investors that it seeks to target and cultivate.[185] Thus, the logical next step in the Shareholder Cultivation process is sorting the investor base and identifying a target group of potential shareholder stewards to cultivate. To borrow Buffett's terminology, a firm should be looking for shareholders who exhibit "co-venturer" characteristics that mesh with the firm's vision, mission, and strategy.[186]

Traditional identification techniques run the gamut, from combing through stock ledger lists to identifying retail versus institutional investors, to segregating investors by fund type (e.g., growth fund, value fund, index fund), to the application of more complex analytical tools that seek to gauge and predict shareholders' investment behavior and average length of ownership in the firm's stock.[187] Firm size, firm industry, and the firm's view of its value proposition are three of the key factors that will determine how a firm defines its co-venturers and the tools that the firm can employ to attract and recruit these co-venturers.[188] According to Julie Tracy, Senior Vice President and Chief Communications Officer at Wright Medical Group, the size of the firm (whether large cap, mid cap, small cap, or microcap), will "determine the levers you can pull . . . and the levers that one can pull to try and attract [the right shareholders] are not equally available to everyone."[189]

Similarly, in terms of firm industry, different industries are thought to attract different types of investors.[190] For example, slow-growth industries like utilities and manufacturing are generally thought to attract so-called "income" investors who focus primarily on the stream of dividends a given stock is likely to generate.[191] In contrast,

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[185] *See supra* Part IV.B.

[186] BUFFETT, *supra* note 6, at 1.

[187] *See* Yakov Amihud & Haim Mendelson, *Asset Pricing and the Bid-Ask Spread*, 17 J. FIN. ECON. 223, 224, 246 (1986).

[188] Telephone Interview with Julie Tracy, Senior Vice President and Chief Commc'ns Officer, Wright Med. Grp. (Jan. 14, 2013).

[189] *Id.*

[190] *See generally* Aswath Damodaran, *Investing Basics Analyzing Stocks*, N.Y. UNIV. STERN SCH. OF BUS., http://pages.stern.nyu.edu/~adamodar/New_Home_Page/articles/valbasics.htm (categorizing investors as either "value," "growth," "income," "GARP," or "quality," and discussing the kind of company qualities each type of investor will seek).

[191] *Id.*

high-growth industries, such as emerging technologies or green-building construction, tend to attract "growth" investors, who focus primarily on the underlying quality of the business and the rate of expected growth, as opposed to immediate value and so-called "GARP" ("growth at a reasonable price") investors, who combine the approaches of value investors and growth investors to identify companies with "solid growth prospects and current share prices that do not reflect the intrinsic value of the business . . . ."[192] Finally, in terms of the firm's value proposition, the story a firm tells about its business and its future will determine the types of investors the firm attracts. A story of future growth and no immediate payoff, for example, would detract income investors but attract growth and some GARP investors.

Another identification technique that corporations employ to identify potential co-venturers is to compare their shareholder base with that of peer firms with the hope of (1) identifying potential shareholders to target; and (2) being able to compare the company's shareholder base turnover profile to that of its competitors.[193] For example, after going through a series of financial restatements, in 2007 Canadian-based Nortel Networks embarked on a peer review and benchmarking process, which compared Nortel's shareholder base and level of shareholder engagement with that of other S&P 500 and S&P/TSX 60 companies.[194] Nortel compared its shareholder base and its processes for communicating with shareholders to those of peer firms, with a particular focus on "benchmarking Nortel's schedule of one-on-ones, investor conferences and analyst days" against those of its peers.[195] Similarly, consider the case of Advanced Micro Devices ("AMD"), an innovative technology company who wanted to attract more long-term investors and decided to "monitor[ ] and measur[e] the 'quality' of AMD's institutional investor base."[196] According to AMD, the company "had a crummy shareholder base. . . . [t]here were a lot of fast-money hedge funds and momentum investors actively trading the stock and [they] were not attracting long-term investors."[197] AMD came to this conclusion after "monitoring and

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[192] *Id.*

[193] Telephone Interview with Julie Tracy, Senior Vice President and Chief Commc'ns Officer, Wright Med. Grp. (Jan. 14, 2013).

[194] *See* Neil Stewart, *Extreme Measures: How to Measure Success in IR*, IR MAG. (Oct. 1 2008), http://www.irmagazine.com/articles/sell-side/15336/extreme-measures-how-measure-success-ir/.

[195] *Id.*

[196] *Id.*

[197] *Id.*

measuring the quality of [its] institutional investor base," which included calculating "[t]he weighted average turnover of AMD's top 50 mutual fund holders[,]" which turned out to be 107 percent.[198] This translated to a holding period of approximately eleven months.[199] When AMD compared this number to peer firms, it realized that peer companies had a more patient shareholder base with an average holding period of "between 15 and 30 months."[200] AMD then targeted shareholders whose turnover profile matched its story of long-term growth and value and was able to increase its weighted average holding period from eleven months to twenty-seven months in the space of five years—a feat that AMD viewed as a success.[201]

More contemporary identification tools attempt to drill down further beyond the conventional shareholder categorizations of retail versus institutional, and long-term versus short-term, and catalog shareholders using different dimensions such as "intrinsic" or "dedicated" shareholders versus "transient" shareholders.[202] A recent study by Professor Brian Bushee on institutional investor behavior and the relationship between observed behaviors and the types of companies in which certain investors choose to commit capital, is illustrative of the kinds of insight that can emerge from moving beyond traditional shareholder categorizations.[203] In his work, Professor Bushee identifies three categories of institutional investors: (1) "transient" institutional investors, who exhibit a high rate of portfolio turnover and hold a small stake in portfolio companies; (2) "dedicated" investors, who take large

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[198]Stewart, *supra* note 194 (internal quotations omitted).

[199]*Id.*

[200]*Id.*

[201]*Id.*

[202]*See* Brian Bushee, *Identifying and Attracting the "Right" Investors: Evidence on the Behavior of Institutional Investors*, 16 J. APP. CORP. FIN. 28, 29 (2004); Juerg Vogt, *The Fight for Intrinsic Capital*, IR MAG. (Mar. 5, 2013), http://www.irmagazine.com/articles/shareholder-targeting-id/19354/fight-intrinsic-capital/; Jesse M. Fried, *The Uneasy Case for Favoring Long-Term Shareholders*, (European Corp. Governance Inst. Law Working Paper No. 200, 2013), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2227080; Robert N. Palter et al., *Communicating with the Right Investors*, *in* MCKINSEY ON FINANCE: THE ENDURING VALUE OF FUNDAMENTALS, 40 MCKINSEY&CO. 57, 58-59 (2011) http://www.mckinsey.com/Client_Service/Corporate_Finance/Latest_thinking/McKinsey_on_Finance/~/media/McKinsey/dotcom/client_service/Corporate%20Finance/MoF/PDF%20issues/MoF_Issue_40_Summer%2011.ashx.

[203]*See generally* Bushee, *supra* note 202, at 35 ("[C]hanges in disclosure practices have the potential to shift the composition of a firm's investor base away from transient investors and toward more patient capital.").

stakes in portfolio companies and exhibit more stable ownership patterns; and (3) "quasi-indexers," which are institutions that also own small stakes but exhibit infrequent trading behavior.[204] According to Professor Bushee, as might be expected, "[t]he disproportionate presence of transient institutions in a company's investor base appears to intensify pressure for short-term performance while also resulting in excess volatility in the stock price."[205]

Similarly, the consulting firm McKinsey & Company classifies shareholders in three categories—intrinsic investors, mechanical investors, and traders.[206] For each of these classifications, McKinsey then analyzes the trading behavior of shareholders along six axes—(1) trading characteristics; (2) percentage of total (publicly listed) U.S. equity; (3) percentage of total trading volume in U.S. equity markets; (4) portfolio concentration; (5) average holding period; and (6) average number of portfolio positions monitored by analyst.[207] The ultimate takeaway for McKinsey is that management should "dedicate" its "engagement efforts" to "intrinsic investors," which McKinsey defines as those shareholders that "[s]upport the . . . management and strategy through short-term volatility."[208]

To summarize, identification techniques run the gamut from the traditional to more contemporary and nuanced modes of analysis. At base, such techniques seek to dissect and mine a company's shareholder base to provide management with insight on shareholder behavior patterns. This insight can reveal points of departure in shareholder characteristics and behavior, which in turn allows for a more informed approach to cultivation. From a cultivation standpoint, more nuanced breakdowns of shareholder behavior like that of McKinsey's is helpful because such analysis when mapped onto a company's shareholder base reveals more sophisticated pathways for exploiting shareholder heterogeneity to cultivate shareholder stewards.[209]

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[204] *Id.* at 29.

[205] *Id.*

[206] *See* Palter et al., *supra* note 202, at 58-59.

[207] *Id.* at 58-60.

[208] *Id.* at 59, 61.

[209] Several third-party market-intelligence firms exist that provide various analytical models and tools to perform this sorting and identification function, and these firms often interface with the corporation's investor relations department. *See, e.g.*, *Deal Making Intelligence*, THOMSON REUTERS, http://dmi.thomsonreuters.com (last visited Jan. 11, 2014); Press Release, Computershare, Computershare Analytics To Provide StreetSight.net Buy-side Intelligence to Track Data's NewsWatch Users (Jun. 18, 2003), https://www-us.computershare.com/Content/download.asp?docId=%7B6E1F40F7-AD89-4D52-9A3C-

D. *Tools for Recruiting and Re-Enforcing Shareholder Stewards (Where the Rubber Hits the Road)*

While identification and sorting primarily involve the firm's investor-relations department, and in many cases one or more third-party shareholder-relation firms, the enlisting and re-enforcing point on the cultivation spectrum is where investor-relation functions, internal corporate governance practices, the realities of today's capital markets, and external law interact; hence, it is where the proverbial rubber hits the road.[210] The cultivation tools that a firm has in its artillery and is able to deploy will depend on firm characteristics and the heterogeneous characteristics of its shareholder base detected in the identification and sorting prong, and such cultivation tools must be designed within governing legal frameworks and against the practical backdrop of modern share ownership.[211]

Enlisting and re-enforcing tools can be loosely classified into three sub-categories, although among the three, there is some slippage and overlap.[212] The first sub-category includes organizational tools, which engage organic documents such as bylaws and articles of incorporation, and organizational frameworks, such as the laws of the state of incorporation or stock exchange listing rules as cultivation tools.[213] The second sub-category consists of capital market tools, which leverage financial securities products and processes to sort, recruit, and cultivate shareholder stewards.[214] Finally, the third sub-category can be loosely defined as rhetorical tools, such as analyst calls and disclosure reports, which utilize communication channels and points of interface not only to speak to the entire shareholder base, but also to recognize the inherent

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37783FC87689%7D&cc=CA&lang=en&bhjs=0&fla=0&theme=cpu; *What We Do*, RIVEL RESEARCH GROUP, http://www.rivel.com/about/1-about/1-what-we-do (last visited Jan. 11, 2014); *About*, RUDER FINN, http://www.ruderfinn.com/#/about/abouthome (last visited Jan. 11, 2014); Press Release, Edelman, Edelman Appoints Stephanie Smirnov New Managing Director, Consumer Marketing in New York (July 11, 2013), http://www.edelman.com/news/edelman-appoints-stephanie-smirnov-new-managing-director-consumer-marketing-in-new-york/; *Strategy Consulting & Research*, FTI CONSULTING, http://www.fticonsulting.com/services/strategic-communications/strategy-consulting-research.aspx (last visited Jan. 11, 2014); *Investor Targeting*, IPREO, http://www.ipreo.com/CorporateServices/Services/Americas/Investor_Targeting.html (last visited Jan. 11, 2014).

[210] *See infra* Parts IV.D.1-3.

[211] *See infra* Parts IV.D.1-3.

[212] *See infra* Parts IV.D.1-3 (explaining three sub-categories of enlisting and re-enforcing tools).

[213] *See infra* Part IV.D.1 (explaining organization tools available to corporations).

[214] *See infra* Part IV.D.2 (examining capital market tools).

heterogeneity in the base, to speak to current and potential shareholder stewards.[215]

1. The Role of State of Incorporation, Stock Exchange Listings, and Organic Documents in Defining Cultivation Zone

The choice of where to incorporate, whether to list on a particular exchange, and the information included in a corporation's bylaws or articles of incorporation, affect the default rules and immutable rules that a company has at its disposal to cultivate shareholders.[216] In turn, the default rules and immutable rules to which a company is subject define the outward bounds of cultivation opportunities and regulate acceptable behavior within the zone of play.[217]

a. *State of Incorporation*

A company's choice of state of incorporation affects the topography of its cultivation zone.[218] Different states provide different legal frameworks, default rules, and a body of jurisprudence that affect the relationship between the corporation and its shareholders.[219] The state of Delaware, for example, adopts an enabling framework that leaves significant discretion to the board to *inter alia*, define the corporation's mission and purpose, provide additional rights to the corporation's shareholders (such as improved proxy access procedures), and determine the rights of shareholders to call special shareholder meetings.[220] In contrast, consider California's corporate law framework, which is generally deemed more shareholder-friendly than Delaware's, and which among other things, has as a default rule that shareholders who are "entitled to cast not less than 10 percent of the votes at the meeting" are entitled to call a special shareholder meeting.[221] Thus, a company's election to incorporate in Delaware or California, or more broadly

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[215] *See infra* Part IV.D.3 (examining rhetorical tools).

[216] *See infra* Part IV.D.1.a-c (discussing how location of incorporation, listing on a particular exchange, and the corporations bylaws and articles of incorporation affect the default rules and immutable rules that a company has at its disposal).

[217] *See supra* Part III.C (examining how default rules and immutable rules define the outward bounds of cultivation opportunities and regulate acceptable behavior within the zone of play).

[218] *See infra* text accompanying notes 220-21.

[219] *See infra* text accompanying notes 220-21.

[220] *See* DEL. CODE ANN. tit. 8, § 141 (2011).

[221] *See* CAL. CORP. CODE § 600(d) (West 2007).

speaking, in one state over another, has practical implications for the way in which power and rights are distributed between shareholders and the board of directors, the limits on board action vis-à-vis shareholders, which in turn impact the types of cultivation techniques that the firm can employ.[222]

Moreover, under the doctrine of internal affairs, which holds that the law of the state of incorporation will govern internal disputes among the directors, officers, and shareholders of the corporation, the choice of state of incorporation has significant doctrinal implications.[223] Thus, the state of incorporation affects the range of Shareholder Cultivation tools that a company has at its disposal,[224] and relatedly it could affect how potential investors view the company and whether they decide to invest in the company's stock.[225] A new wrinkle is that with the advent of new options for corporations to elect to become "social purpose" corporations or "benefit corporations," the choice of state of incorporation is not all that matters.[226] For corporations that opt to incorporate or that are already incorporated in a state that now offers this social-purpose opt-in, the decision on whether to opt into the social purpose/public benefit statutory scheme will further serve a signaling function to potential investors and may also hurt or enhance the corporation's ability to cultivate shareholders.[227]

b. *Choice of Stock Exchange*

Similarly, a corporation's choice of stock exchange listing has implications for the immutable-default rule construct and the types of cultivation tools that it has at its disposal.[228] For example, consider the

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[222]*See supra* text accompanying notes 217-19.

[223]*See, e.g.*, Vantagepoint Venture Partners 1996 v. Examen, Inc., 871 A.2d 1108, 1117-18 (Del. 2005) (explaining that under the internal affairs doctrine a company's state of incorporation governs the choice of law to be applied in certain disputes).

[224]*See supra* text accompanying notes 217-19.

[225]This is particularly true if vigorous competition develops among states for incorporation. *See, e.g.*, Elizabeth Lopatta, *'Virgin' North Dakota Draws Billionaire Icahn in Raider Quest*, BLOOMBERG (Feb. 20, 2009), http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aXgfseyKwJmI ("The state has adopted a law . . . that lets shareholders more easily gain control of any company incorporated there.").

[226]*See, e.g.*, DEL. CODE ANN. tit. 8, §§ 361-368 (2013); N.Y. BUS. CORP. LAW § 1704(b) (McKinney 2003); WASH. REV. CODE ANN. § 23B.25 (West 2012).

[227]*See supra* text accompanying notes 223-26.

[228]*See infra* text accompanying notes 229-31 (showing how the choice of stock exchange listing affects the immutable-default rule construction and types of cultivation tools

case of two companies in the same industry—Hennes & Mauritz AB (also known as "H&M") and Gap, Inc. ("Gap").[229] H&M is a Swedish company (with several hundred stores throughout the U.S.) whose stock is listed on the Swedish stock exchange,[230] but actively trades in the U.S. on the OTC pink sheets.[231] In contrast, Gap is a U.S. company whose stock is listed on the New York Stock Exchange ("NYSE").[232] Even though both are public companies with a presence in the U.S. equity markets, because of differences in stock exchange listing requirements, H&M's shareholders are given a binding vote on executive compensation matters under the newly enacted Swedish stock exchange listing rules,[233] but Gap's shareholders do not have a binding vote on executive compensation matters because neither NYSE listing rules nor U.S. law requires it.[234]

The difference in the treatment of shareholder rights vis-à-vis executive compensation could cut both ways. First, for a company that is open to having a mandatory vote on executive compensation, a listing on the NYSE versus the Swedish stock exchange allows them a chance to distinguish themselves from competitors who are not so inclined and perhaps signal to potential shareholders the importance of their voice and vote on compensation matters.[235] On the other hand, shareholders may self-select and self-identify based on these differences, all things being equal.[236] In a similar vein, one could contrast differences in cultivation

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that a company has at its disposal).

[229]H&M and Gap, Inc. both deal in the apparel industry. *See* H&M, ANNUAL REPORT 2012 (2013) ("The Group's business consists mainly of sales of clothing, accessories, footwear, cosmetics and home textiles to consumers."); The Gap, Inc., Annual Report (Form 10-K) (Mar. 26, 2013) ("Gap is . . . one of the most iconic apparel brands in the marketplace today.").

[230]*See* H&M, ANNUAL REPORT 2012 (2013) ("The company's shares are listed on the Stockholm stock exchange, NASDAQ OMX Stockholm AB.").

[231]*See HMRZF Stock*, OTCMARKETS.COM, http://www.otcmarkets.com/stock/HMRZF/company-info (last visited October 8, 2013) (indicating H&M trades on OTC Pink Sheets).

[232]*See* The Gap, Inc., Annual Report (Form 10-K) (Mar. 26, 2013) (indicating Gap Inc., is traded on the New York Stock Exchange).

[233]*See Articles of Association*, H&M (April 28, 2011), http://about.hm.com/AboutSection/en/About/Corporate-Governance/Other/Articles-of-Association.html#cm-menu (indicating that at the Annual General Meeting shareholders determine the fees payable to the board of directors and the auditors).

[234]*See* The Gap, Inc., Amended and Restated Bylaws of The Gap, Inc. (Form 8-K, Ex. 3(ii)) ("The salary, bonus, and long-term incentive compensation of all executive officers of the Corporation . . . shall be fixed by the Board of Directors or a committee thereof from time to time.").

[235]*See supra* notes 233-34 and accompanying text (noting how the Swedish stock exchange requires a vote on executive compensation whereas the NYSE allows companies to choose and therefore distinguish themselves from other NYSE companies).

[236]*See supra* notes 233-34 and accompanying text.

strategy that arise between corporations listed on the NYSE or Nasdaq and those listed on the London Stock Exchange.[237] As discussed below, those in the former categories would be allowed under the exchange listing requirements to issue up to twenty percent of stock in a private transaction without the need for shareholder approval, while those in the latter category would be allowed to issue no more than ten percent of securities of an existing class.[238] Thus, stock exchange listing requirements potentially change the boundaries and the content of the immutable-default rule construct, which in turn impacts the types of cultivation tools that a firm can employ to attract and curate shareholder stewards.

c. *Organic Documents*

Finally, in terms of organizational tools, a firm's articles of incorporation and its bylaws serve key cultivation functions. Most state corporate statutes provide a limited number of mandated requirements of items that must be included in the corporation's charter or in its bylaws, with wide latitude left to the corporation to tailor its organic documents to its particular purpose and needs.[239] For example, Delaware requires that the certificate of incorporation include the name of the corporation; the address of the registered office and name of the registered agent; the nature and purpose of the business of the corporation; the number of authorized shares; and the names and mailing addresses of the incorporators.[240] Beyond these four requirements, Delaware does not dictate how the corporation may use its certificate of incorporation and instead provides significant discretion to the board in the substance of the provisions that it chooses to include.[241] Similarly, Delaware's corporate code does not specify the substance of what should be included in the bylaws.[242] Instead, the applicable provision of the statute simply states that "[t]he by-laws may contain any provision, not inconsistent with law or with the certificate of incorporation, relating to the business of the corporation, the conduct of its affairs, and its rights or powers or the

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[237] *See infra* Part IV.D.2.b (discussing listing limitations on the amount of shares that can be sold in one private transaction without shareholder approval).

[238] *See infra* Part IV.D.2.b.

[239] *See, e.g.*, DEL. CODE ANN. tit. 8, § 102 (2011) (providing the minimum requirements for the certificate of incorporation).

[240] *See id.* §102(a)(1)-(5).

[241] *See id.*

[242] *See id.* § 109(b).

rights or powers of its stockholders, directors, officers or employees."[243] Thus, as cultivation tools, the organic documents provide for corporations to among other things, define and in some cases, refine their purpose; memorialize the corporation's governance processes and aspirations; and specify the procedures for shareholder engagement.[244] For existing corporations, this is particularly true with respect to the bylaws, which in general can be amended by the board without the consent of the shareholders,[245] as compared to the articles of incorporation, which would require a shareholder vote for amendment.[246]

2. Capital Market Cultivation Tools

For Shareholder Cultivation, capital markets provide a forum for a firm to connect to potential shareholder stewards through the use of targeted financial tools and processes.[247]

a. *IPOs*

From the firm's perspective, going public represents a transition from being surrounded by a core base of founders, initial investors, venture capitalists, and employees who are hopefully supportive of the firm's mission and value proposition, to being surrounded by a new group of shareholders who may or may not support the firm's value proposition.[248] One way to smooth this transition and ensure some cohort

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[243]DEL. CODE ANN. tit. 8, §109(b) (2011). Case law does add some color by specifying that the bylaws should serve a "process creating function" and should not be used for substantive purposes. *See* Auer v. Dressel, 118 N.E.2d 590, 598 (N.Y. 1954).

[244]To avoid implicating the ultra vires doctrine, most corporations declare their mission and purpose in a mission statement rather than in the certificate of incorporation. *See* DAVID A. DREXLER, ET AL., DELAWARE CORPORATION LAW AND PRACTICE § 11.05 (2011) ("Where the general language authorized by Section 102(a)(3) is utilized, the ultra vires doctrine should be totally dead, even with respect to Section 124's three limited exceptions.").

[245]*See, e.g.*, DEL. CODE ANN. tit. 8, § 109 (2011) (granting the board the power to amend the corporation's bylaws without the consent of the shareholders).

[246]*See, e.g.*, *id.* § 242 (providing that a vote of the shareholders is needed to amend a corporations articles of incorporation).

[247]*See infra* Parts III.D.2.a-f.

[248]*See* Bernard S. Black & Ronald J. Gilson, *Venture Capital and the Structure of Capital Markets: Banks Versus Stock Markets*, 47 J. FIN. ECON. 243, 252-53 (1998) (discussing the benefits provided by venture capital providers that would be lost or diminished after the firm goes public); Scott J. Davis, *Would Changes in the Rules for Director Selection and Liability Help Public Companies Gain Some of Private Equity's Advantages?*, 76 U. CHI. L. REV. 83, 87 (2009) ("[O]nce [a] startup becomes a public company . . . . [i]t begins to be assumed that the public investors have different goals than the original backers.").

of shareholders that will invest for the long run is to target shareholders who do just that.[249]

The literature on initial public offerings ("IPO") suggests that in an IPO, underwriters do sell some portion of the allotted shares by allocation rather than by open auction.[250] The idea behind selling shares by allocation is to attract enough shareholders who will hold long-term instead of quickly selling the stock and driving the stock price down.[251] A stylized example of this occurred when Goldman Sachs went public in 1999.[252] According to the *Wall Street Journal*, Goldman placed its shares "with a group of institutional investors and rich individuals who Goldman believed would remain loyal, long-term holders and not 'flip' the stock after its opening."[253]

Goldman's IPO story also highlights that a company's choice to utilize the "traditional" Wall Street allocation route during the IPO process, as opposed to other legally sanctioned methods such as a modified Dutch auction, may affect the company's ability to tailor its shareholder base at the outset.[254] In the case of Goldman, the company was careful to allocate shares in a way that minimized the chances of short-term "flippers" buying its stock.[255] In contrast, when Google Inc. went public in 2004, Google opted to sell its shares through a modified Dutch auction where underwriters gathered bids from investors irrespective of the investor's connection to the underwriters or the size of

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[249]*See* Bharat A. Jain & Omesh Kini, *Venture Capitalist Participation and the Post-Issue Operating Performance of IPO Firms*, 16 MANAGERIAL & DECISION ECON. 593, 593, 600 (1995) ("[V]enture capitalists are typically active investors who try to add value to their portfolio companies through ongoing longer-term involvement with continuing business development[.]" (citation omitted)).

[250]*See* Anita Indira Anand, *Is the Dutch Auction IPO a Good Idea?*, 11 STAN. J.L. BUS. & FIN. 232, 244 (2006) ("While the bookbuilt method can be criticized for giving rise the practices of spinning [the underwriters' practice of allocating coveted IPO shares to existing clients in return for higher commissions or future business.]"); Tim Jenkinson & Howard Jones, *IPO Pricing and Allocation: A Survey of the Views of Institutional Investors*, 22 REV. FIN. STUD. 1477, 1493 (2009) (discussing alternative views of factors that influence allocation in IPO).

[251]*See* Jenkinson & Jones, *supra* note 250, at 1480 (stating that in determining allocation, long-term shareholder status is considered a very important feature of investors).

[252]*See infra* note 253 and accompanying text.

[253]Charles Gasparino, *Goldman IPO Lives Up to Expectations, Posts 33% Gain in First Trading Day*, WALL ST. J., May 5, 1999, http://online.wsj.com/article/SB925832942582883947.html.

[254]*See* Anand, *supra* note 250, at 245 (stating that a firm may choose the traditional bookbuilt process rather than a Dutch auction in order to gain certain long-term benefits not offered by the Dutch auction).

[255]Gasparino, *supra* note 253.

their holding.[256] While a modified Dutch auction approach is viewed as "more fair" than the traditional allocation approach, in terms of a cultivation tool, the allocation approach allows a company to maintain more control over the initial construction of its shareholder base.[257]

b. *The Twenty Percent Rule and Select Private Placements*

The private placement of shares by already-public companies is yet another cultivation tool that corporations can employ to attract and recruit identified co-venturers. Both NYSE and Nasdaq rules allow listed companies to sell up to twenty percent of a given class of securities without shareholder approval and, in terms of SEC regulations, these sales would typically fall under private placement exemptions and would not require registration.[258]

The ability to sell up to twenty percent of a firm's equity without triggering shareholder approval and without SEC registration (assuming such issuance complies with applicable SEC rules and regulations) essentially gives public corporations listed on the NYSE or Nasdaq the leeway to cultivate at least twenty percent of their shareholder base to secure a critical mass of shareholder stewards.[259] When combined with the identification and sorting techniques discussed above, corporations effectively have twenty percent of their equity that they can control and allot to shareholders who they have identified as co-venturers. This twenty percent could be sold to one investor or to multiple investors who exhibit investment behavior and characteristics attractive to the corporation. Stated differently, this twenty percent could serve as a stabilizing shareholder core committed to holding the corporation's shares for some length of time. Such a stabilizing core also signals to the

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[256] *See* Anand, *supra* note 250, at 240.

[257] *See id.* at 247-48.

[258] *NYSE Market Rules: Listed Company Manual*, N.Y. STOCK EXCH. § 3, http://nysemanual.nyse.com/LCMTools/PlatformViewer.asp?selectednode=chp%5F1%5F4%5F10&manual=%2Flcm%2Fsections%2Flcm%2Dsections%2F (last visited Nov. 8, 2013) [hereinafter *NYSE Manual*] (requiring stockholder approval before a listed company can issue twenty percent or more of its outstanding common stock or voting power); *see also Section 5600 Corporate Governance Requirements*, NASDAQ STOCK MKT., http://nasdaq.cchwallstreet.com/NASDAQTools/PlatformViewer.asp?selectednode=chp%5F1%5F1%5F4%5F3&manual=%2Fnasdaq%2Fmain%2Fnasdaq%2Dequityrules%2F (last visited Nov. 8, 2013) (requiring that under certain circumstances, stockholder approval of transactions that may result in the issuance or sale of twenty percent or more of a listed company's outstanding common stock or voting power).

[259] See *infra* Part VI.A.1 for a discussion on critical mass.

market and to other potential shareholders that the corporation has a significant shareholder-supporter base on board who, colloquially speaking, "has its back."

To use the previous, but admittedly somewhat extreme example of Goldman Sachs and Warren Buffett, in 2008, Goldman needed a fresh injection of capital and to steady the ship, so it sought out Buffett (who has a reputation for being a steward).[260] Buffett agreed to invest up to $5 billion, in exchange for perpetual preferred stock.[261] The arrangement was beneficial to both parties because Goldman was able to secure Buffett's support for management's strategy and ward off further attacks, and for his part, Buffett was able to earn a handsome return on his investments.[262]

Similarly, on a less grandiose level than the Goldman-Buffett alliance, private equity funds are often brought in to invest in public companies for similar reasons (referred to as "PIPE" investments or private investment in public equity).[263] Although private equity investors are sometimes criticized for being "asset strippers," private equity can play a tremendous role in the cultivation space.[264] While private equity firms have different investment strategies and focus, they all share the common goal of investing with an eye to enhancing the value of the company in which they have invested.[265] In exchange for injecting capital into a company, the private equity firm receives a stake in ownership, along with one or more seats on the company's board, and

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[260]Ben White, *Deal Seen as Sign of Confidence*, N.Y. TIMES, Sept. 24, 2008, at A1.

[261]*Id.*

[262]*See generally id.*

[263]*See generally* John D. Hogboom, *Private Investment in Public Equity: An Overview*, N.J. L. J., Aug. 16, 2004, *available at* http://www.sec.gov/info/smallbus/gbfor25_2006/hogoboom_invest.pdf (discussing PIPE investments).

[264]*See* Eileen Appelbaum, *How Does Private Equity Really Make Money?*, ROOSEVELT INST., http://rooseveltinstitute.org/how-does-private-equity-really-make-money (last visited Oct. 19, 2013); Davis, *supra* note 248, at 89.

[265]*See* Brian Cheffins & John Armour, *The Eclipse of Private Equity*, 33 DEL. J. CORP. L. 1, 9 (2008) (internal citation omitted) ("[O]ver the past few years [private equity] has become popularly associated with the buying out and taking private of public companies, with the objective being to deliver superior risk-adjusted returns by improving the financial performance and growth profile of the acquired companies."); Davis, *supra* note 248, at 87 (expressing that the primary goal common to venture capitalists is the continuing creation of shareholder value); Trevor M. Gomberg, *After the Storm: Unmasking Publicly-Traded Private Equity Firms to Create Value Through Shareholder Democracy*, 73 ALB. L. REV. 575, 577 (2010) ("The goal of private equity is to create value through investments in unproven or mismanaged companies which likely need help in order to become profitable.").

any rights or benefits included in the relevant acquisition agreement.[266] In addition, the private equity firm has a vested interest in helping company management successfully execute its strategic plan.[267] Thus for cultivation purposes, a private equity investor offers more rooted interest than transient ownership.

c. *Dual-Class Share Structures*

Yet another capital market cultivation tool is the use of dual-class share structures, where targeted shareholders may be given superior voting and dividend rights. The most prevalent form of dual-class share structure is the use of preferred stock.[268] Dual-class shares structures have a long history in corporate law and are explicitly recognized in state corporate codes.[269] To illustrate, the DGCL explicitly sanctions the use of dual-class share structures and provides that a company *may* specify such a structure in its certificate of incorporation.[270] Corporations maintain dual-class share structures for a variety of reasons,[271] but these types of arrangements can also be used as cultivation tools. For example, when Facebook Inc. went public, it did so with a dual-class share structure of Class A and Class B shares.[272] Only the Class A shares were offered in the IPO.[273] The Class B Shares were sold separately to a targeted group of shareholders, which consisted in part of the founder, initial investors, and initial supporters.[274] Facebook's Class A Shares and Class B Shares are identical in all respects, except for voting rights and conversion rights.[275] According to Facebook's prospectus,

> The rights of the holders of Class A common stock and Class B common stock are identical, except with respect to

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[266]Cheffins & Armour, *supra* note 265, at 9.

[267]*See id.*

[268]Douglas C. Ashton, *Revisiting Dual-Class Stock*, 68 ST. JOHN'S L. REV. 863, 865 (1994) ("In most cases, the firm selects a capital structure that is characterized by a combination of debt and equity, the equity portion typically consisting of one class of common stock and one or more classes of preferred stock.").

[269]*See generally id.* at 904-05.

[270]DEL. CODE ANN. tit. 8, § 151(a) (2011).

[271]*See* Ashton, *supra* note 268, at 866.

[272]*See* Facebook, Inc., Registration Statement (Form S-1) (Feb. 1, 2012).

[273]*See Id.*

[274]*See id.*; *see also* Steven M. Davidoff, *A Big Bet on Zuckerberg*, N.Y. TIMES, Feb. 2, 2012, http://dealbook.nytimes.com/2012/02/02/a-big-bet-on-zuckerberg/.

[275]*See* Facebook, Inc., Registration Statement (Form S-1) (Feb. 1, 2012).

> voting and conversion. Each share of Class A common stock is entitled to one vote per share. Each share of Class B common stock is entitled to ten votes per share and is convertible at any time into one share of Class A common stock.[276]

The dual-class share structure is beneficial to Facebook's initial investors because it helps them maintain control over the company's vision and future trajectory after the IPO.[277] Of course, this strategy by Facebook was not without critique, but it is perfectly legal in terms of a cultivation technique, and it does allow the firm to (a) maintain some control over its decisions and strategic choices and (b) signal to the market that the firm has a core group of shareholder stewards.[278] Even for companies who have been public for a long time, the dual-class share structure serves as an enlistment tool to entice and reward targeted shareholders to become owners in the firm.[279]

d. *Time-Weighted Voting*

Another cultivation technique that firms have at their disposal is the use of time-weighted voting, also known as tenured voting or time-phased voting, whereby a shareholder's voting power increases based on the length of time he or she has been a shareholder.[280] Under state law, tenured voting is generally permissible.[281] For example, in *Williams v. Geier*, the Delaware Supreme Court held that the board's decision to

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[276] *Id.*

[277] *See* Davidoff, *supra* note 274 (exploring how Facebook's dual-class share structure and voting agreements with other Class B shareholders enables Zuckerberg to retain control over the company).

[278] *See, e.g.*, Michael J. De La Merced, *I.S.S. Adds to Criticism of Facebook's Governance*, N.Y. TIMES, Feb. 13, 2012, http://dealbook.nytimes.com/2012/02/13/i-s-s-adds-to-criticism-of-facebooks-governance. Facebook's proposed governance plan signals to Class A that its role is primarily financial capital contribution, and the locus of decision-making will rest firmly with the board, the founder, and initial investors. *See id.*

[279] *See* White, *supra* note 260.

[280] *See infra* notes 281-82 and accompanying text.

[281] *See, e.g.*, Hu & Black, *supra* note 60, at 1059 (explaining that under Delaware law, corporations are not explicitly constrained in how they depart from the default one-vote-per-share rule); *see also* DEL. CODE ANN. tit. 8, § 212(a) (2011) ("*[U]nless otherwise provided in the certificate of incorporation*, each stockholder shall be entitled to 1 vote for each share of capital stock.") (emphasis added). *But see* Mercier v. Inter-Tel, Inc., 929 A.2d 786, 815 n.82 (Del. Ch. 2007) ("The concept of time-weighted voting has been around for many years. The DGCL does not embrace it.").