WE('RE) WORKING ON CORPORATE GOVERNANCE: STAKEHOLDER VULNERABILITY IN UNICORN COMPANIES

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ABSTRACT

Large private companies are often characterized by poor corporate governance that harms an array of stakeholders. WeWork provides a recent, high-profile example of such harms. The WeWork vision, and the dominating personality of its co-founder, Adam Neumann, attracted billions of investment dollars. As a private company with a valuation in excess of $1 billion, WeWork was a “unicorn.” In January 2019, WeWork was valued at $47 billion, and SoftBank alone had invested more than $9 billion.

In August 2019, however, a draft of the company’s Form S-1 registration statement was made public. Analysts and the financial press raised serious concerns. The filing revealed an aggressive multi-class voting structure, and an equally bold assessment of profitability reached through very creative accounting. WeWork scrambled to make changes, but the weaknesses proved too much. The IPO was cancelled; valuations were adjusted down to between $8 and $10 billion; SoftBank took control by injecting another $9.5 billion, approximately $1.7 billion of which was to be used to remove Neumann; and a new management team was installed, putatively to turn the company into a model of responsible corporate governance. Thousands of employees were laid off and collateral businesses were sold or shuttered.

Perhaps this story vindicates U.S. financial market regulation: the transparency required by federal securities law ultimately triumphed, and WeWork corrected course. But why did corporate and securities laws enable the WeWork “debacle” in the first place? Why were the substantial costs, both direct and collateral, to the WeWork stakeholders, not least its investors, not avoided?

Unicorns have absorbed hundreds of billions of investment dollars, but unfortunately have also generated massive externalities. When they have succeeded, unicorns have delivered enormous gains for their founders, insiders, and early-stage investors. When they have failed, these entities have imposed substantial hardships on investors and a wide array of stakeholders including employees, customers, suppliers, lenders, the economy, and society itself.

This article explores some of the reasons for the persistently poor governance of unicorns, with emphasis on the homogeneity of company

boards and of decision-makers at the entities funding them. It looks at both securities and corporate law and analyzes how such laws work (or mostly do not, but could, work) to protect investors and other stakeholders.

This article argues that poor governance could be remedied by existing laws. It also proposes specific changes that might be made to rein in unicorns and protect stakeholders.

I. INTRODUCTION

A. A Unicorn Runs Amok

Imagine that you have invested your money in a company. Or imagine that you are a fund manager who has invested the money that other people rely on for their retirement savings. What would you do if you learned that the chief executive officer and chairman of the board of that company:

- used company funds to establish many unrelated collateral businesses (including a "progressive" school for his children, ages 2-8);[1]
- received hundreds of millions of dollars in loans from the company;[2]
- cashed out hundreds of millions of dollars of his[3] shares in the company;[4]
- regularly "hotboxed" the company jet (filled it with marijuana smoke) during business trips to Europe;[5]

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1. Ellen Huet & Gillian Tan, *WeWork Was a Family Affair, Until Things Got Complicated*, BLOOMBERG BUSINESSWEEK (Sept. 28, 2019, 8:00 AM EDT), https://www.bloomberg.com/news/articles/2019-09-28/wework-was-a-family-affair-until-things-got-complicated [https://perma.cc/W7C7-LK8H].

2. Lisa Eadicicco, *WeWork IPO Reveals Company Loaned Millions to CEO Adam Neumann and Other Company Execs,* BUS. INSIDER (Aug. 14, 2019, 12:34 PM), https://www.businessinsider.com/wework-ipo-company-loaned-7-million-ceo-adam-neumann-2019-8 [https://perma.cc/6YJH-X86D].

3. The male-gendered pronoun "his" is used in these examples because they refer to the actions of a particular individual who, like almost all unicorn founders, venture capitalists and fund managers, is male. *See* discussion below in Part II.A.3 (discussing the lack of diversity in unicorn boards).

4. Rebecca Aydin, *The History of WeWork - from Its First Office in a SoHo Building to Pushing Out CEO and Cofounder Adam Neumann*, BUS. INSIDER (Oct. 22, 2019, 1:32 PM), https://www.businessinsider.com/wework-ipo-we-company-history-founder-story-timeline-adam-neumann-2019-8 [https://perma.cc/S2M9-TU7E].

5. Amy Chozick, *Adam Neumann and the Art of Failing Up*, N.Y. TIMES (Nov. 2, 2019), https://www.nytimes.com/2019/11/02/business/adam-neumann-wework-exit-package.html [https://perma.cc/K2PA-3Y5T]. In the employment discrimination suit filed against Neumann and WeWork, former Chief of Staff Medina Bardhi alleged that, when pregnant,

- renamed the company, picking a name to which he had reserved the rights, and charged the company $6 million to use its new name;[6]
- purchased real estate and then leased the real estate to the company;[7]
- hosted notoriously alcohol-fueled parties at many company locations;[8]
- claimed to aspire to being "president of the world";[9]
- described the company as a "state of consciousness";[10]
- embarked on a rapid growth campaign causing massive losses but used a creative accounting method called "community-adjusted EBITDA" or "contribution margin" to recharacterize them as gains;[11]

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she had to stop traveling with Neumann on overseas flights due to Neumann's "hotbox" practice. *See* Class and Collective Administrative Charge of Discrimination, Retaliation, and Gender Pay Disparity, Bardhi v. The We Co., No. [ ] (EEOC filed Oct. 31, 2019), *available at* http://www.wigdorlaw.com/wp-content/uploads/2019/10/Bardhi-v.-WeWork-Filed.pdf [https://perma.cc/5AH4-VD36] (" . . . [Ms. Bardhi] could no longer accompany Mr. Neumann on business travel, particularly due to his penchant for bringing marijuana on chartered flights and smoking it throughout the flight while in the enclosed cabin. Ms. Bardhi obviously could not expose her unborn child to marijuana smoke, much less in such an enclosed space for hours at a time.").

6. *See* Chozick, *supra* note 5 (explaining how Neumann reserved the rights to "We," and renamed the company "We Companies," charging it $5.9 million for the name). The payment was returned after public outcry. *Id.*

7. Eliot Brown, *WeWork's CEO Makes Millions as Landlord to WeWork*, WALL ST. J. (Jan. 16, 2019, 10:01 PM ET), https://www.wsj.com/articles/weworks-ceo-makes-millions-as-landlord-to-wework-11547640000 [https://perma.cc/HCN3-3PCV].

8. Chozick, *supra* note 5.

9. Chozick, *supra* note 5.

10. *See* David Gelles, *The WeWork Manifesto: First, Office Space. Next, the World,* N.Y. TIMES (Feb. 17, 2018), https://www.nytimes.com/2018/02/17/business/the-wework-manifesto-first-office-space-next-the-world.html [https://perma.cc/T2E4-VZTD] (explaining Neumann's ambition to transform the way people work, live, and play).

11. The WeWork August 2019 Form S-1 showed losses of $429 million on $436 million in revenue in 2016, losses of $890 million on $886 million in revenue in 2017, and losses of $1.6 billion on $1.8 billion in revenue in 2018. Troy Wolverton & Shona Ghosh, *WeWork Files for IPO, Revealing Spiraling Losses of $1.6 Billion*, BUS. INSIDER (Aug. 14, 2019, 7:28 AM), https://www.businessinsider.com/wework-s-1-prospectus-ipo-revenue-cash-flow-2019-8 [https://perma.cc/J8SP-M2JH]; *see also* Nori Gerardo Lietz, *WeWork – The IPO That Shouldn't?*, HARV. BUS. SCH. WORKING KNOWLEDGE (Sept. 18, 2019), https://hbswk.hbs.edu/item/wework-the-ipo-that-shouldn-t [https://perma.cc/8LJ5-KTE3] (explaining defects in the "contribution margin" metric); Jamie Powell, *The magic of adjustments: ebitla-dee-da*, FIN. TIMES (Apr. 25, 2018), https://www.ft.com/content/884e7da3-2de7-3c56-bdff-a308152ce086 [https://perma.cc/E9GJ-NM24] (calling Community Adjusted Ebitda "a rather quixotic take on the famous Ebitda metric").

- owned a majority of the stock, including shares in a class that received 20 votes-per-share, ensuring his lifetime control, and control by his family generations into the future;[12]
- hired his spouse and close family members for key leadership positions;[13] and
- set up a system that, in the event of his death, permitted his spouse to name his successor.[14]

Would you try to vote the individual off of the board of directors, or remove him as CEO? Would you try to introduce some counterbalancing influence into the company? Would you sell your stake? Or would you remain invested, and even invest more?

In 2019, as the irregularities at WeWork (renamed "We Company" in January 2019,[15] but "WeWork" for purposes of this article) were revealed, its investors grappled with such questions. The WeWork debacle captured public attention. But the drama had a dark side: jobs were lost, investments disappeared, careers sidetracked, and presumably, more responsible startups found it more difficult to raise capital.[16]

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12. Troy Wolverton, *Adam Neumann Has Locked Up Control of The We Company in a Jaw-Dropping Way, Even by Silicon Valley Standards, by Giving Himself 20 Votes Per Share*, BUS. INSIDER (Aug. 14, 2019, 4:15 PM), https://www.businessinsider.com/wework-ceo-adam-neumann-stock-gives-20-votes-a-share-2019-8 [https://perma.cc/8LXD-NYW2]; *see also* Connie Loizos, *Adam Neumann planned for his children and grandchildren to control WeWork*, TECHCRUNCH (Oct. 18, 2019), https://techcrunch.com/2019/10/18/adam-neumann-planned-for-his-children-and-grandchildren-to-control-wework/ [https://perma.cc/QQ6Q-BC93] (quoting Neumann as saying that WeWork isn't "just controlled, we're generationally controlled" and describing how one of his great-great-granddaughters will still control the company).

13. Huet & Tan, *supra* note 1; *see also* Eric Platt & Andrew Edgecliffe-Johnson, *WeWork: How the Ultimate Unicorn Lost Its Billions*, FIN. TIMES (Feb. 20, 2020), https://www.ft.com/content/7938752a-52a7-11ea-90ad-25e377c0ee1f [https://perma.cc/RTK8-RE5P] (explaining that Rebekah Paltrow Neuman was elevated to co-founder and described as Neumann's "strategic thought partner" in WeWork's August 2019 draft Form S-1).

14. Huet & Tan, *supra* note 1; Platt & Edgecliffe-Johnson, *supra* note 13.

15. Paige Leskin, *WeWork Is Changing Its Name to 'The We Company' as SoftBank Invests $2 Billion*, BUS. INSIDER (Jan. 8, 2019, 9:58 AM), https://www.businessinsider.com/wework-changes-name-to-the-we-company-2019-1 [https://perma.cc/9SU3-5NP9].

16. *See* Kate Rooney, *WeWork's pre-IPO troubles serve as a reality check for start-ups as 'growth at any cost' dies*, CNBC (Sept. 13, 2019) https://www.cnbc.com/2019/09/13/weworks-pre-ipo-troubles-serve-as-reality-check-for-start-ups-as-growth-at-any-cost-dies.html [https://perma.cc/68GS-6SL4] (calling WeWork a cautionary tale for investors); *see also* Charles Duhigg, *How Venture Capitalists Are Deforming Capitalism*, NEW YORKER (Nov. 23, 2020), https://www.newyorker.com/magazine/2020/11/30/how-venture-capitalists-are-deforming-capitalism?irclickid=yEl06X3JExyLTfbwUx0Mo372UkEWC0ydw1X91E0&irgwc=1&source=affiliate_impactpmx_12f6tote_desktop_Bing%20Rebates%20by%20Microsoft&utm_source=impact-affiliate&utm_medium=2003851&utm_campaign=impact&utm_content

Established in 2010 by Adam Neumann and Miguel McKelvey,[17] WeWork acquires office space, redecorates it with modern furniture and features like fizzy water taps and pinball machines,[18] and then leases access to the space on a short-term basis.[19] Buying commercial real estate and then leasing it out is hardly a new idea, but Neumann aspired to reinvent work[20] and to "elevate the world's consciousness."[21] Although fundamentally a real estate development company, in "vision," WeWork resembled the most brash of technology start-ups. It called itself an "SaaS" (space-as-a-service) provider.[22] Neuman pronounced, sententiously, that WeWork is "the world's first physical social network."[23] The company, it was said, would encompass all aspects of human life.[24]

=Logo&utm_brand=tny [https://perma.cc/6FSF-GH4A] (discussing the fundraising difficulties encountered by NextSpace Coworking, a co-working start-up that was earning a modest profit when WeWork began to attract attention from investors).

17. Reeves Wiedeman, *The I in We: How Did WeWork's Adam Neumann Turn Office Space with "Community" into a $47 Billion Company? Not by Sharing*, N.Y. MAG. (June 10, 2019), http://nymag.com/intelligencer/2019/06/wework-adam-neumann.html [https://perma.cc/X86C-9HK7].

18. *See* Andrew Edgecliffe-Johnson, *Pinball, Fizzy Water and Helium Balloons: Why Small Office Perks Loom Large*, FIN. TIMES (Aug. 28, 2019), https://www.ft.com/content/4a5b74cc-c928-11e9-af46-b09e8bfe60c0 [https://perma.cc/GV7N-VRWL] (noting WeWork's shuffleboard tables and "kombucha-stuffed fridges"); *see also* Katherine Rosman, *We Work. We Live. We Work Out. Eventually We Die.*, N.Y. TIMES (Oct. 12, 2017), https://www.nytimes.com/2017/10/12/style/wework-fitness-gyms.html [https://perma.cc/PE37-F3CJ] (calling the WeWork decorating style "foosball-infused bro-deco").

19. *See* George Schultze, *Why WeWork Won't Work: Hello Neumann!* FORBES (Oct. 8, 2019), https://www.forbes.com/sites/georgeschultze/2019/10/08/why-wework-wont-work-hello-neumann/?sh=3552ae624e03 [https://perma.cc/8Q3F-KQNB] (explaining the WeWork business model as "not much more than an office rental company that acts as a middleman between landlords and short-term tenants").

20. *See* We Co., Draft Registration Statement (Form S-1/A) at 5 (Aug. 14, 2019), *available at* https://sec.report/Document/0001628279-19-000233/ [https://perma.cc/29S8-M5FZ] ("We believe that we have laid the foundation to capitalize on our significant market opportunity by continuing to reinvent the future of work."); *see also* Ian Bogost, *The Wildly Appealing, Totally Doomed Future of Work*, THE ATLANTIC (Sept. 26, 2019), https://www.theatlantic.com/technology/archive/2019/09/why-wework-was-destined-fail/598891/ [https://perma.cc/52N4-P6R8] (noting that the company was supposed to reinvent work itself).

21. *See* We Co., *supra* note 20, at 1 ("Our mission is to elevate the world's consciousness.").

22. *See* Kara Swisher, *WeWork: Is There Any There There?*, N.Y. TIMES (Aug. 22, 2019), https://www.nytimes.com/2019/08/22/opinion/wework-ipo.html [https://perma.cc/25WE-WWVD] (describing WeWork's characterization of its workstation rentals as "space-as-a-service," a play on the influential "software-as-a-service sector").

23. Wiedeman, *supra* note 17.

24. *See* Katrina Brooker, *Exclusive: WeWork rebrands to The We Company; CEO Neumann talks about revised Softbank round*, FASTCOMPANY (Jan. 8, 2019), https://www.fastcompany.com/90289512/exclusive-wework-to-rebrand-to-the-we-company-in-wake-of-

The WeWork vision, and Neumann's dominating personality, attracted billions of investment dollars. By August of 2019, SoftBank[25] alone had invested more than $9 billion.[26] As a private company with a valuation in excess of $1 billion, WeWork was a "unicorn."[27] In its January 2019 funding round, WeWork was valued at $47 billion.[28] Investment bankers pitching their initial public offering ("IPO") services to the company in 2018 and 2019 valued WeWork at between $46 and $104 billion.[29]

For years, analysts and the financial press raised questions about the company. Reports were published about Neumann and the incredible losses incurred by his company.[30] But the sheer magnitude of investments made in WeWork, the prestige of the company's attorneys and investment bankers,

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disappointing-funding-news [https://perma.cc/S688-8J3E] (reporting that Neumann planned for the company to encompass all aspects of people's lives, in both physical and digital worlds).

25. SoftBank Group Corp. and its $100 billion Vision Fund, which is backed by the company and two Middle Eastern sovereign-wealth funds, will be referred to together as "SoftBank" in this article.

26. Phred Dvorak & Justin Baer, *SoftBank's WeWork Bailout Draws Investor Concern*, WALL ST. J. (Oct. 26, 2019, 6:34 AM ET), https://www.wsj.com/articles/softbanks-wework-bailout-draws-investor-concern-11572086091 [https://perma.cc/U29M-R28T]*; see also* Maureen Farrell & Eliot Brown, *The Money Men Who Enabled Adam Neumann and the WeWork Debacle*, WALL ST. J. (Dec. 14, 2019, 12:00 AM ET), https://www.wsj.com/articles/the-money-men-who-enabled-adam-neumann-and-the-wework-debacle-11576299616 [https://perma.cc/RN7Z-FW5U] (discussing SoftBank's investment); Megan Hernbroth, *Meet Ron Fisher, the SoftBank Executive on WeWork's Board Leading the Campaign to Oust CEO Adam Neumann*, BUS. INSIDER (Sept. 23, 2019, 10:36 AM), https://www.businessinsider.com/meet-ron-fisher-softbank-vision-fund-behind-wework-valuation-ipo-2019-9 [https://perma.cc/3EGG-VBSY] (same).

27. *See* Aileen Lee, *Welcome to The Unicorn Club: Learning From Billion-Dollar Startups*, TECHCRUNCH (Nov. 2, 2013, 2:00 PM EDT), https://techcrunch.com/2013/11/02/welcome-to-the-unicorn-club/ [https://perma.cc/TR4P-FWMB] (coining the term "unicorn").

28. Sara Salinas & Deirdre Bosa, *WeWork Is Rebranding, and SoftBank Ups Its Investment by $2 Billion*, CNBC (Jan. 8, 2019, 9:13 AM EST), https://www.cnbc.com/2019/01/08/wework-rebranding-as-the-we-company-softbank-invests-2-billion.html [https://perma.cc/R3NE-DKY5].

29. *See* Eric Platt et al*., WeWork Turmoil Puts Spotlight on JPMorgan Chase and Goldman Sachs*, FIN. TIMES (Sept. 24, 2019), https://www.ft.com/content/272d408e-de40-11e9-b112-9624ec9edc59 [https://perma.cc/BV73-J2X3] (identifying the banks as JP Morgan Chase, Goldman Sachs, and Morgan Stanley).

30. *See, e.g.*, Rebecca Aydin, *WeWork isn't even close to being profitable – it loses $219,000 every hour of every day,* BUS. INSIDER (Jul. 3, 2019), https://www.businessinsider.com/wework-not-close-to-profitable-loses-hundreds-thousands-every-hour-2019-7 [https://perma.cc/9BPS-RC6S] (describing the company as "hemorrhaging money"); Michael J. de la Merced, *WeWork's Losses Swell to Nearly $2 Billion as It Seeks Global Expansion*, N.Y. TIMES (Mar. 25, 2019), https://www.nytimes.com/2019/03/25/business/dealbook/wework-loss-billion.html [https://perma.cc/C583-DPYU] (noting that the company's losses had doubled from the prior year).

and Neumann's charismatic personality muted many concerns.[31]

WeWork was expected to be the second largest unicorn to go public in 2019.[32] When a draft of the company's Form S-1 registration statement was made public in August of 2019,[33] however, the skeptics began to outshout the boosters. Criticized as a "masterpiece of obfuscation,"[34] the filing revealed the heavily weighted multi-class voting structure, and the confusing, creative accounting the company used to assess profitability.[35] In

31. *See* Eliot Brown, *How Adam Neuman's Over-the-Top Style Built WeWork. 'This Is Not the Way Everybody Behaves',* WALL ST. J. (Sept. 19, 2019), https://www.wsj.com/articles/this-is-not-the-way-everybody-behaves-how-adam-neumanns-over-the-top-style-built-wework-11568823827 [https://perma.cc/6X2H-NKBR] (describing Neumann's "combination of entrepreneurial vision, personal charisma and brash risk-taking").

32. *See* Drew Singer, *WeWork Analyst Warns IPO Filing a 'Masterpiece of Obfuscation',* BLOOMBERG (Aug. 20, 2019, 8:00 AM EDT), https://www.bloomberg.com/news/articles/2019-08-20/wework-analyst-warns-ipo-filing-a-masterpiece-of-obfuscation [https://perma.cc/DCH7-9A6J] (pointing out that the offering was expected to raise $3.5 billion).

33. We Co., *supra* note 20. Five versions of the Form S-1 had been submitted to the SEC confidentially before the August 14, 2019 version was filed. We Co., Draft Registration Statement Filings (Form DRS & S-1/A) (Dec. 28, 2018; Apr. 25, 2019; May 14, 2019; June 19, 2019; July 18, 2019). Filings can be found through EDGAR System search on sec.gov, *available at* https://www.sec.gov/cgi-bin/browse-edgar?action=getcompany&CIK=0001533523&owner=exclude&count=40&hidefilings=0 [https://perma.cc/M6ZQ-W4PW].

34. Triton Research Inc. CEO Rett Wallace called the prospectus a "masterpiece of obfuscation." Singer, *supra* note 32.

35. We Co., *supra* note 20. Analysts pointed out that using a "contribution margin" metric, WeWork was not recording marketing and sales expenses at its locations once they were open for two years, despite the fact that the expenses were still being paid. *See, e.g.,* Daniel Strauss, *WeWork's IPO Documents Baffled an Analyst Who Specializes in Evaluating Companies Preparing to Go Public*, BUS. INSIDER (Aug. 29, 2019, 2:24 PM), https://markets.businessinsider.com/news/stocks/weworks-ipo-filing-makes-it-impossible-to-model-analyst-says-2019-8-1028460674 [https://perma.cc/9AWB-YBMY] (" . . . the company stops recording marketing and sales expenses at WeWork locations once they've been open for two years even though the expenses don't actually stop."). WeWork's draft Form S-1 revealed a loss of $1.6 billion on $1.8 billion of revenue in 2018. Ellen Florian, *Here's Why WeWork Won't Be in the S&P 500 after Its IPO,* FORTUNE (Aug. 20, 2019, 2:30 PM EDT), https://fortune.com/2019/08/20/wework-ipo-s-and-p-500/ [https://perma.cc/6JS3-MLHF]. The unusual metric, given the costs it excluded, raised questions among analysts and regulators. *See* Amanda Iacone, *SEC Flags Cash-Flow Measure That Made WeWork Look Profitable (1),* BLOOMBERG L. (Dec. 3, 2019, 4:45 AM), https://news.bloombergtax.com/financial-accounting/sec-flags-cash-flow-measure-that-made-wework-look-profitable [https://perma.cc/J2KT-AEJB] (noting that the SEC was reviewing the financial reporting and disclosures); Scott Galloway, *NYU Professor Calls WeWork 'WeWTF' Says Any Wall Street Analyst Who Believes It's Worth Over $10 Billion is 'Lying, Stupid, or Both,'* BUS. INSIDER (Aug. 21, 2019, 9:48 AM) (calling WeWork's "community-based Ebitda" an invented metric that does not account for expenses comprising the bulk of costs required to deliver service).

response, the company revised[36] the "sloppy"[37] Form S-1. WeWork also announced measures to address some of the governance concerns, including the company's ultimately unsuccessful plans to place its first woman, Harvard Business School Professor Frances Frei, on its board of directors.[38]

Despite such belated efforts, the weaknesses of the company's governance proved too much. In the next three months, the IPO was cancelled; some valuations were adjusted down to as low as $8 billion;[39] SoftBank took control[40] by injecting another $9.5 billion, approximately $1.7

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36. WeWork amended the Form S-1 twice more in fall 2019, filing amended versions September 4, 2019 and September 13, 2019. We Co., Draft Registration Statement Filings (Form S-1/A) (Sept. 04, 2019; Sept. 13, 2019). Filings can be found through EDGAR System search on sec.gov, *available at* https://www.sec.gov/cgi-bin/browse-edgar?action=getcompany&CIK=0001533523&owner=exclude&count=40&hidefilings=0 [https://perma.cc/PC8T-W4UH].

37. *See* Jean Eaglesham & Eliot Brown, *WeWork Investors Turned Off by "Sloppy" IPO Filings,* WALL ST. J. (Oct. 7, 2019, 5:31 AM ET), https://www.wsj.com/articles/wework-investors-turned-off-by-sloppy-ipo-filings-11570440674 [https://perma.cc/56AH-BD57] (quoting Nori Gerardo Lietz, a Harvard Business School lecturer who analyzed WeWork).

38. Patrick Clark & Jeff Green, *WeWork Adds Harvard's Frei to All-Mall Board After Criticism,* BLOOMBERG L. (Sept. 4, 2019, 11:13:15), https://www.bloomberglaw.com/document/PXBBM36JIJUO [https://perma.cc/23P4-NC4F] (announcing WeWork's plan to add Frances Frei to its all-male board of directors before becoming a public company). Professor Frei did not end up joining the board. Gillian Tan & Ellen Huet, *WeWork Chairman Says Diversity is Coming to All-Male Board*, BLOOMBERG L. (Oct. 31, 2019, 15:49:34), https://www.bloomberg.com/news/articles/2019-10-31/wework-executive-chairman-claure-promises-more-board-diversity [https://perma.cc/3AT4-W39C] (reporting that Frances Frei was not expected to join WeWork following the withdrawal of the IPO). WeWork's first female board member, SoftBank executive and Facebook veteran Kirthiga Reddy, joined the board in early 2020, after WeWork management was reorganized. *See* David Jeans, *Exclusive: 3 WeWork Board Members Depart, Another to Follow*, THEREALDEAL (Feb. 6, 2020, 10:11 AM), https://therealdeal.com/2020/02/06/exclusive-three-wework-board-members-depart-another-to-follow/ [https://perma.cc/MJA8-GN54] (describing the board shakeup as a "changing of the guard" at WeWork).

39. Sergei Klebnikov, *WeWork's Valuation Plummets to $8 Billion as Softbank Completes Takeover*, FORBES (Oct. 21, 2019, 4:11 PM), https://www.forbes.com/sites/sergeiklebnikov/2019/10/21/weworks-valuation-plummets-to-8-billion-as-softbank-completes-take-over/#4121a094a482 [https://perma.cc/2KSU-DUNL].

40. Mary Meisenzahl, *WeWork's had a terrible 2 months, and now SoftBank is reportedly taking control of the company in a bailout deal*, BUS. INSIDER (Oct. 22, 2019, 9:04 AM), https://www.businessinsider.com/wework-ipo-timeline-delayed-ceo-adam-neumann-scandals-explained-2019-9 [https://perma.cc/KDB3-BT93]. SoftBank's WeWork bailout reportedly left it with 80% of the company, but SoftBank claimed it would not hold a majority of the voting rights – WeWork's board would get voting control of Neumann's shares – and so it did not "control" WeWork. *See* Tom Zanki, *SoftBank Takes 80% WeWork Stake As Ex-CEO Cedes Power*, LAW360 (Oct. 22, 2019), https://www.law360.com/articles/1212170/softbank-takes-80-wework-stake-as-ex-ceo-cedes-power [https://perma.cc/LW4F-FFEK] (describing WeWork as an "associate," not a "subsidiary," of SoftBank). Nevertheless, Softbank

billion of which was to be used to separate Neumann;[41] and a new management team set about turning the company into a model of responsible corporate governance,[42] with an eye toward making a profit.[43] Thousands of

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reportedly sought approval of the package from the Committee on Foreign Investment in the United States (CFIUS), which reviews foreign investments in the United States for national security risks. *See* Sarah McBride & David McLaughlin, *SoftBank to Seek U.S. National Security Review of WeWork Deal*, BLOOMBERG LAW (Oct. 24, 2019), https://www.bloomberg.com/news/articles/2019-10-23/softbank-to-seek-u-s-national-security-review-of-wework-deal [https://perma.cc/3RB3-U9L4] (noting that SoftBank has had trouble with CFIUS in the past).

41. Gerrit de Vynck *et al., WeWork hires corporate turnaround artist with 'plenty of luck' as new CEO*, FORTUNE (Feb. 3, 2020, 8:02 AM), https://fortune.com/2020/02/03/wework-hires-sandeep-mathrani-new-ceo/ [https://perma.cc/9CDF-8KYV]; *see also* Maureen Farrell & Eliot Brown, *SoftBank to Boost Stake in WeWork in Deal That Cuts Most Ties with Neumann*, WALL ST. J. (Oct. 22, 2019, 11:29 PM), https://www.wsj.com/articles/softbank-to-take-control-of-wework-11571746483 [https://perma.cc/6QKK-CFSY] (reporting that the deal involved a $185 million consulting fee to Neumann, Neumann's right to sell SoftBank approximately one-third of his WeWork shares for $970 million, and a SoftBank credit to Neumann of $500 million to enable him to pay off loans made to him by several banks); Eliot Brown, *WeWork Employee Options Underwater as Ex-CEO Reaps,* WALL ST. J. (Oct. 23, 2019, 6:33 PM), https://www.wsj.com/articles/wework-employees-feel-sting-as-ex-ceo-stands-to-reap-11571870011 [https://perma.cc/YK7Y-DR79] (reporting the Neumann would receive up to $1.7 billion as part of the deal with SoftBank). The agreement with Neumann was described as "extraordinary." Joseph E. Bachelder III, *Compensation and Separation Agreement for WeWork CEO,* N.Y.L.J. (Dec. 27, 2019, 12:00 PM), https://www.law.com/newyorklawjournal/2019/12/27/compensation-and-separation-arrangements-for-wework-ceo/?slreturn=20200116183437 [https://perma.cc/2CTP-XQU9]. *But see* Rolfe Winkler, *WeWork Chairman Says Consulting Deal with Adam Neumann No Longer in Place*, WALL, ST. J. (Oct. 19, 2020), https://www.wsj.com/articles/softbank-backs-out-of-consulting-deal-with-wework-co-founder-adam-neumann-11603136659 [https://perma.cc/9TNE-CLLY] (quoting WeWork Executive Chairman Marcelo Claure as saying, "I don't think that consulting agreement is still in place").

42. *See* Matt Levine, *WeSurrender*, BLOOMBERG OPINION (Sept. 27, 2019), https://www.bloomberg.com/opinion/articles/2019-09-27/we-moves-fast-to-unbreak-things [https://perma.cc/FT6T-U4NB] (describing WeWork's efforts to change everything the markets did not like and proceed with the IPO as a "bizarre triumph of corporate governance").

43. WeWork appointed Sandeep Mathrani, a real estate industry veteran, as CEO on February 1, 2020. Under Mathrani, WeWork announced plans to refocus on office rentals and walk away from passion projects. *See* Andrea Navarro & Gillian Tan, *WeWork Adds Maurice Levy, SoftBank Executives in Turnaround Plan*, BLOOMBERG (Nov. 22, 2019), https://www.bloomberg.com/news/articles/2019-11-22/wework-appoints-new-executives-as-part-of-five-year-plan [https://perma.cc/3KF7-23R9] (outlining WeWork's five-year turnaround plan); Gerrit de Vynck *et al., WeWork hires corporate turnaround artist with 'plenty of luck' as new CEO*, FORTUNE (Feb. 3, 2020, 8:02 AM), https://fortune.com/2020/02/03/wework-hires-sandeep-mathrani-new-ceo [https://perma.cc/N4LU-MUWC] (discussing Mathrani's "turnaround expertise.").

employees were laid off,[44] and collateral businesses were sold or shuttered.[45]

Some have argued that this story vindicates U.S. financial market regulation: the transparency required by federal securities law ultimately triumphed, and WeWork corrected course.[46] But why did corporate and securities laws enable the WeWork "debacle"[47] in the first place? Why were the substantial costs, both direct and collateral, to the WeWork stakeholders, not least its investors, not avoided?

B. The Unicorn Governance Problem

WeWork is certainly a dramatic case,[48] and it would be nice to think of it as anomalous. But WeWork is not alone in the "weirdo sparkly unicorn governance" category.[49] Uber, led by its explosive[50] founder Travis Kalanick, was beset with claims of discrimination and sexual harassment of employees;[51] was alleged to have been complicit in the theft of intellectual

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44. Sara Ashley O'Brien, *Inside WeWork's week from hell: How the mass layoffs went down*, CNN BUS. (Nov. 22, 2019, 4:52 PM), https://www.cnn.com/2019/11/22/tech/wework-layoffs-staffers-react/index.html [https://perma.cc/3TRP-3PL9]; Annie Palmer, *WeWork lays off 2,400 employees*, CNBC: TECH (Nov. 21, 2019, 10:48 AM), https://www.cnbc.com/2019/11/21/wework-lays-off-2400-employees.html [https://perma.cc/49RB-A2NK].

45. *See* discussion *infra* Part III.C.3 (discussing how WeWork's poor corporate governance led to the sudden shuttering of WeWork's unrelated collateral ventures).

46. *See* Anne Sraders, *The fall of WeWork was a jolt to venture capital–how that could change VC investing*, FORTUNE (Jan. 22, 2020, 12:00 PM), https://fortune.com/2020/01/22/vc-news-venture-capital-outlook-2020/ [https://perma.cc/K6EQ-JY3N] (asserting that "[i]f the WeWork debacle and the poor public debuts of companies like Uber, Lyft, and SmileDirectClub taught us anything it's that the public markets are going to be tougher on high-flying unicorns.").

47. Farrell & Brown, *supra* note 26.

48. *See* Maureen Farrell et al., *SoftBank Seeking to Take Control of WeWork Through Financing Package*, WALL ST. J. (Oct. 13, 2019, 7:21 PM), https://www.wsj.com/articles/softbank-seeking-to-take-control-of-wework-through-financing-package-11571002488 [https://perma.cc/U8G8-WDNC] (describing WeWork as the "poster child" for startup excesses).

49. Matt Levine, *WeWhoosh*, BLOOMBERG OPINION (Sept. 9, 2019), https://www.bloomberg.com/opinion/articles/2019-09-09/we-might-not-be-working [https://perma.cc/K3QV-26LY] (describing WeWork as the "absolute limit case of unicorn craziness").

50. *See* Mike Isaac, *Inside Uber's Aggressive, Unrestrained Workplace Culture,* N.Y. TIMES (Feb. 22, 2017), https://www.nytimes.com/2017/02/22/technology/uber-workplace-culture.html [https://perma.cc/387F-64B5] (describing Uber's CEO, Travis Kalanick, as creating a "pugnacious" and "aggressive" work culture).

51. Uber settled an EEOC sexual harassment probe in December 2019, for $4.4 million. *See* Press Release, EEOC, Uber to Pay $4.4 Million to Resolve EEOC Sexual Harassment and Retaliation Charges (Dec. 18, 2019), *available at* https://www.eeoc.gov/eeoc/newsroom/release/12-18-19.cfm [https://perma.cc/SGB3-2N3C] (stating that Uber had agreed to strengthen its business culture against sexual harassment and retaliation).

property;[52] and used software to elude detection by local regulators, from whom it lacked operational permission.[53] Theranos, under the control of Elizabeth Holmes, sold clients a blood testing technology that did not really exist.[54] Zenefits, which sold software that enabled companies to manage their human resources, allowed unlicensed employees to sell insurance.[55] Other examples abound.[56]

Unicorns have absorbed hundreds of billions of investment dollars, but unfortunately have also generated massive externalities.[57] When they have

52. Isaac, *supra* note 50; *see also* Paayal Zaveri & Jillian d'Onfro, *Travis Kalanick takes the stand to explain why Uber wanted to poach Google self-driving engineer*, CNBC (Feb. 6, 2018) https://www.cnbc.com/2018/02/06/travis-kalanick-reveals-why-he-wanted-googles-anthony-levandowski.html [https://perma.cc/5RKP-6JH5] (describing Kalanick's involvement in the trade secrets trial between Uber and Waymo).

53. *See* Mike Isaac, *How Uber Deceives the Authorities Worldwide,* N.Y. TIMES (Mar. 3, 2017), https://www.nytimes.com/2017/03/03/technology/uber-greyball-program-evade-authorities.html [https://perma.cc/8FP5-XVR5] (describing Uber's Greyball program, which used data collected form the Uber app and other techniques to evade authorities).

54. Nick Bilton, *Exclusive: How Elizabeth Holmes's House of Cards Came Tumbling Down,* VANITY FAIR HIVE (Sept. 6, 2016), https://www.vanityfair.com/news/2016/09/elizabeth-holmes-theranos-exclusive [https://perma.cc/X35G-V697]; *see also* Charles Duhigg, *supra* note 16 (calling Theranos a "dubious" start-up and noting that it raised seven hundred million dollars from investors before it was revealed as a fraud).

55. Kia Kokalitcheva, *Major CEO Shakeup At Zenefits Over Regulatory Problems,* FORTUNE (Feb. 8, 2016), http://fortune.com/2016/02/08/zenefits-parker-conrad-resigns/ [https://perma.cc/7KXZ-XB3U]. After Zenefits co-founder Parker Conrad was forced out as CEO in 2016, he co-founded employee-management software company Rippling, which was valued at $270 million in 2019. Josh Constine, *Rippling raises $45 million at $270 million to be the biz app identity layer,* TECHCRUNCH (Apr. 3, 2019, 9:18 AM), https://techcrunch.com/2019/04/03/rippling-45-million/ [https://perma.cc/8G2P-K32A].

56. In 2019, food delivery service Postmates postponed its IPO. Among other things, the company had endured a messy fight with its employees after restructuring pay rates. Carolyn Said, *'No rich people working for Postmates': Couriers protest pay change*, S.F. CHRON. (May 21, 2019), https://www.sfchronicle.com/business/article/There-are-no-rich-people-working-for-13867172.php [https://perma.cc/8APY-XAG7]. Online trading app Robinhood also postponed its IPO in 2019 after a number of controversies, including bad publicity and an SEC fine over revelations that it was selling customer orders to high-frequency traders. Dave Michaels, *Robinhood Settles Claims It Didn't Ensure Best Prices for Customer Trades*, WALL ST. J. (Dec. 19, 2019, 12:22 PM), https://www.wsj.com/articles/robinhood-settles-claims-it-didnt-ensure-best-prices-for-customer-trades-11576776167 [https://perma.cc/VVB6-PP3S]. The stock trading app, however, went on to raise over $500 million the following year. *See* Jeff John Roberts, *Robinhood raises $200M as IPO speculation swirls*, FORTUNE (Aug. 17, 2020, 11:00 AM), https://fortune.com/2020/08/17/robinhood-ipo-speculation-funding-round-series-g-predictions/ [https://perma.cc/4ZB8-55FH] (noting that the company claimed a valuation of $11.2 billion).

57. *See* Renee M. Jones, *The Unicorn Governance Trap*, 166 U. PA. L. REV. ONLINE 165, 167 (2017) (discussing several unicorn stumbles); *see also* Donald C. Langevoort & Robert B. Thompson, *"Publicness" in Contemporary Securities Regulation After the JOBS Act*, 101

succeeded, unicorns have delivered enormous gains for their founders, insiders, and early-stage investors.[58] When they have failed, these entities have imposed substantial hardships on investors and a wide array of stakeholders, including employees,[59] customers, suppliers, lenders, the economy,[60] and society itself.[61]

When privately held highly valued companies were first given the moniker "unicorns" in 2013, the name was intended to convey the rarity of

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GEO. L.J. 337, 340 (2013) (exploring the public-private divide after the JOBS Act was enacted). For example, when financing negotiations between the robotic pizza company Zume and Softbank broke down in 2019, hundreds of employees were laid off. Sraders, *supra* note 46.

58. *See* Kate Vinton, *Meet The 14 Unicorn Startups That Have Created 25 Billionaires*, FORBES (Mar. 6, 2016, 7:00 PM), https://www.forbes.com/sites/katevinton/2016/03/06/meet-the-14-unicorn-startups-that-have-created-25-billionaires/#18408fb5485b [https://perma.cc/A5K7-UEBM] (finding among other things that Uber and Airbnb produced three billionaires each, while Snapchat and Pinterest produced two each).

59. For example, when London-based augmented reality unicorn Blippar went under in 2018, all employees were let go. Paul Sawers, *The rise and fall of augmented reality 'unicorn' Blippar,* VENTUREBEAT, (Dec. 18, 2018, 11:23 AM), https://venturebeat.com/2018/12/18/the-rise-and-fall-of-augmented-reality-unicorn-blippar/ [https://perma.cc/KZ57-524W].

60. *See, e.g.,* Jason Zweig, *How We Should Bust an Investing Myth*, WALL ST. J. (Sept. 24, 2019, 1:51 PM), https://www.wsj.com/articles/how-we-should-bust-an-investing-myth-11568991786 [https://perma.cc/7ZN8-DJU4] (noting that the private markets are more prone to error than the public markets because they are both shallow and narrow and prone to over-optimistic valuations); *see also* Farrell & Brown, *supra* note 26 (claiming that WeWork investors' "extraordinarily optimistic" perspectives "supercharged WeWork's visions of grandeur").

61. *See, e.g.,* Abbey Stemler, *The Myth of the Sharing Economy and Its Implications for Regulating Innovation*, 67 EMORY L.J. 197 (2017) (providing a critical perspective on unicorns that deploy rhetoric and persuasion to subvert regulation and harm consumers and communities). Consider Arrivo Corporation, a California-based unicorn founded by engineer Brogan BamBrogan, after he was "dramatically ousted" from Hyperloop One in 2016. Andrew J. Hawkins, *Ousted Hyperloop One founder Brogan BamBrogan just atarted a new company,* THE VERGE (Feb. 9, 2017, 12:00 PM), https://www.theverge.com/2017/2/9/14559974/hyperloop-brogan-bambrogan-arrivo-los-angeles-lawsuit [perma.cc/75WQ-ATC9]. Arrivo successfully pitched a magnetic levitation rail system to the Colorado Department of Transporation (CDOT) and then shut down, inflicting costs on its investors as well as the state of Colorado. Aaron Gordon, *How Arrivo Got Colorado to Back a Wild-Eyed Highway Scheme*, WIRED (Mar. 2, 2019, 7:00 AM), https://www.wired.com/story/arrivo-colorado-brogan-bambrogan-hyperloop-concept [https://perma.cc/2LTN-3LF2]; Marshall Zelinger, *The Colorado Department of Transportation is rethinking the money it spends on technology*, 9NEWS (Nov. 19, 2019, 7:42 PM), https://www.9news.com/article/news/local/next/the-colorado-department-of-transportation-is-rethinking-the-money-it-spends-on-technology/73-4f986ed2-c676-4060-a083-105cb10ee860 [https://perma.cc/Q2RB-KRCY].

such companies.[62] They are not that rare anymore.[63] Thanks to plentiful venture capital and private equity funding, sustained low interest rates, the (at least perceived) burden of becoming a reporting company under the U.S. federal securities laws, and changes in those laws that enable some companies to stay private longer,[64] the number of unicorns has been steadily rising. As of November 2020, there were approximately 500 unicorns, with a cumulative valuation of over $1.58 trillion.[65]

Despite being the size of many public companies, many unicorns lack the basic corporate governance one would expect, given the number of zeroes on their (non-GAAP[66]) financial statements.[67] Unicorns are often characterized by few restraints on founder discretion and lack many of the standard checks on corporate decision-making. Their upper echelons are largely homogenous in terms of gender, i.e., are overwhelmingly male.[68] Unicorns also appear to be vulnerable to strategic error, because their

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62. *See* Lee, *supra* note 27 (comparing the rarity of developing a unicorn company to catching an MLB foul ball or being struck by lightning). Of course, family-held companies have been around forever, and may be valued at over $1 billion. Unicorns, however, achieve these valuations in the feverish venture capital markets, not by dint of being a long-standing dynasty. As discussed below, the valuations of unicorns may in some cases be inflated, or at least optimistic. *See* Robert P. Bartlett III, *A Founder's Guide to Unicorn Creation: How Liquidation Preferences in M&A Transactions Affect Start-up Valuation, in* RESEARCH HANDBOOK ON MERGERS AND ACQUISITIONS *1,* 1–3 (Claire A. Hill & Steven Davidoff Solomon, eds., 2016) (arguing that unicorn valuations are unreliable measures of firm value).

63. *See* Jennifer S. Fan, *Regulating Unicorns: Disclosure and the New Private Economy,* 57 B.C. L. REV. 583, 587 (2016) (calling unicorns "ubiquitous").

64. *See* Carlos Berdejo, *Going Public after the JOBS Act*, 76 OHIO ST. L. J. 1, 14–17 (2015) (walking through some of the costs of being public); *see also infra* Part II.B.2 (discussing companies' decisions to stay private longer).

65. *The Complete List of Unicorn Companies*, CB INSIGHTS, https://www.cbinsights.com/research-unicorn-companies [https://perma.cc/5EP7-HSL3] (last visited Nov. 21, 2020). Other sources put the number even higher. *See, e.g.,* Gené Teare, *Private Unicorn Board Now Above 600 Companies Valued At $2T*, CRUNCHBASE NEWS, (June 29, 2020), https://news.crunchbase.com/news/private-unicorn-board-now-above-600-companies-valued-at-2t/ [https://perma.cc/9SV2-5ZD2] (putting the number of unicorns at 601 with a total valuation just under $2 trillion).

66. GAAP refers to "generally accepted accounting principles" in the United States. 17 CFR § 244.101(b). The SEC requires reporting companies that are disclosing information either to use GAAP or to provide information that reconciles their calculations with GAAP. 17 C.F.R. §244.100(a).

67. *See* Nori Gerardo Lietz, *WeWork–The IPO That Shouldn't?*, HARVARD BUS. SCH. WORKING KNOWLEDGE (Sept. 18, 2019), https://hbswk.hbs.edu/item/wework-the-ipo-that-shouldn-t [https://perma.cc/T6P9-YGB5] (discussing the misleading financial disclosure in the WeWork August 2019 draft Form S-1).

68. *See* Jennifer S. Fan, *Innovating Inclusion: The Impact of Women on Private Company Boards*, 46 FLA. ST. U. L. REV. 345, 350 (2019) (noting that men control over 90% of unicorn board seats).

funding sources often provide only positive feedback.[69] Many such companies have been, and still are, led by founders who maintain control over the company, sometimes even after the company goes public.[70] As WeWork exemplifies, many of these companies are run with a messianic style[71] and a lack of restraint reminiscent of the robber barons.[72]

One reason there are so many enormous private companies is that successful start-ups are staying private longer. The average time between first venture-capital financing and going public has increased from approximately four years in the 1990s to seven years today.[73] In 1980, the average age of a company when it went public was six years; in 2019, it was ten.[74] Startups are not only able to stay independent and privately held long after they first raise capital, late-stage startups have seen an increase in the amount of capital they are able to raise, and therefore levels of employment they are able to maintain.[75] Without the near-term prospect of an IPO, unicorns may lack incentives to impose the systems of corporate governance that we expect from large corporations.[76]

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69. *See* Jesse M. Fried & Jeffrey N. Gordon, *The Valuation and Governance Bubbles of Silicon Valley,* THE CLS BLUE SKY BLOG (Oct. 10, 2019, 11:29 PM), https://clsbluesky.law.columbia.edu/2019/10/10/the-valuation-and-governance-bubbles-of-silicon-valley/ [https://perma.cc/JN56-8MH2] (noting that there is no way for investors to "short" an overvalued startup).

70. *See* Amy Deen Westbrook & David A. Westbrook, *Snapchat's Gift: Equity Culture in High-Tech Firms*, 46 FLA. ST. U. L. REV. 861, 865 (2019) (highlighting founder control); *see also* Dileep Rao, *Is the Cult Of The "Unicorn-Founder" Dead?,* FORBES (Jan. 21, 2020, 11:12 PM), https://www.forbes.com/sites/dileeprao/2020/01/21/is-the-cult-of-the-unicorn-founder-dead/?sh=40db65405c70 [https://perma.cc/94RR-6HMP] (arguing that venture capital investors frequently cede, and will continue to cede, control to unicorn founders).

71. Neumann is quoted as saying, "We are here in order to change the world . . . Nothing less than that interests me." Platt & Edgecliffe-Johnson, *supra* note 13.

72. *See* Amy Deen Westbrook & David A. Westbrook, *Unicorns, Guardians, and the Concentration of the U.S. Equity Markets*, 96 NEB. L. REV. 688, 693–95 (2018) (discussing robber barons in the context of contemporary equity markets).

73. Michael Ewens & Joan Farre-Mensa, *The Deregulation of the Private Equity Markets and the Decline in IPOs,* REV. FIN. STUD., 3 (forthcoming Feb. 7, 2020), *available at* https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3017610 [https://perma.cc/J5XX-4U06V].

74. *See* Jay R. Ritter, *Initial Public Offerings: Updated Statistics,* UNIV. FLA. https://site.warrington.ufl.edu/ritter/files/IPO-Statistics.pdf?te=1&nl=debatable&emc=edit_db_20210202 [https://perma.cc/8W96-U8A4] (last visited Nov. 21, 2020) (providing data about the median age and fraction of IPOs with VC and buyout backing between 1980 and 2019).

75. *See* Michael Ewens & Joan Farre-Mensa, *The Deregulation of the Private Equity Markets and the Decline in IPOs*, 3 (May 9, 2020) (unpublished manuscript) (on file with The Review of Financial Studies), *available at* https://doi.org/10.1093/rfs/hhaa053 [https://perma.cc/G596-9URE] (noting that previously, these levels were only consistently achieved by public companies).

76. *See* Paresh Dave & James Rufus Koren, *Have Investors Allowed Tech Founders Like*

During their years in the "enchanted forest," there is little internal need for unicorn companies to establish governance mechanisms.[77] Unicorns are often led by a single or small number of male founders operating informally, *i.e.*, with few checks.[78] Unicorns may often suffer from a lack of internal discipline.[79] While the idealized appeal is obvious – a small group of brilliant friends founding a company – the lack of responsible governance in such super-sized startups can harm a broad spectrum of stakeholders.

C. Poorly Governed Unicorns Threaten a Variety of Stakeholders

Although bad governance may be ignored by the legal regime and the financial markets when companies are small, problems are not so easily dismissed when billions of dollars and large numbers of people are involved. One may be concerned with investors who provide their money (or, in startups, often labor) to the firm in exchange for equity interests or debt. State corporation laws and federal securities laws may apply in different ways to protect those shareholders and other investors. Various laws may also apply to additional persons interested in the firm, such as employees, members of the community, suppliers, and consumers (collectively referred to as "stakeholders").

This article argues that many of the hundreds of unicorns impacting the financial markets have unsatisfactory corporate governance, and it proposes

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Uber's Travis Kalanick to Grow too Powerful?, L.A. TIMES (June 14, 2017, 3:00 AM), http://www.latimes.com/business/technology/la-fi-tn-uber-investors-20170613-story.html [https://perma.cc/TPM9-LBVV] (discussing Uber). *But see* Crystal Tse, *Tech Unicorns Rushing to Go Public Defy Sleepy Summer Season (1)*, BLOOMBERG LAW (Aug. 25, 2020, 8:53 AM), https://www.bloomberg.com/news/articles/2020-08-25/tech-unicorns-rushing-to-go-public-defy-sleepy-summer-season [https://perma.cc/HK2H-P7S8] (reporting that the lull in the first months of the Covid-19 outbreak had ended, and 2020 turned out to be the 'busiest summer' investment bankers could remember).

77. This is a common refrain. *See, e.g.*, Matt Levine, *Mutual Funds in the Enchanted Forest*, BLOOMBERG LAW (Oct. 11, 2019), https://www.bloomberglaw.com/product/blaw/document/PZ7WT66JTSEE?criteria_id=16fe85f88a3594201bf564f9306875a5 [https://perma.cc/MZ2Z-WZN4] (noting that people are worried about unicorns).

78. According to a 2018 deal between Neumann and SoftBank, Softbank could remove Neumann as CEO "only if he committed a violent crime and was jailed in a common law jurisdiction." *See* Platt & Edgecliffe-Johnson, *supra* note 13 (identifying this as an "extreme" example of trust placed in founders).

79. *See* David Benoit et al., *WeWork is a Mess for JP Morgan. Jamie Dimon is Cleaning it up*, WALL ST. J. (Sept. 24, 2019, 2:33 PM), https://www.wsj.com/articles/wework-is-a-mess-for-jpmorgan-jamie-dimon-is-cleaning-it-up-11569349994 [https://perma.cc/8DNZ-54XL] ("The governance reflects there are no adults in the room. The underwriters are as guilty as the board for instituting a preposterous governance."); *see also* Jones, *supra* note 57, at 167 (citing the "unique governance challenges" posed by unicorns).

ways to address the problem. Part II walks through the ways corporation and securities laws are failing to protect unicorn investors. Part III argues that poor unicorn governance has even broader impacts and looks at the ways other stakeholders are being harmed. Part IV considers and rejects the argument that bad governance is a fair price to pay for the innovation offered by some unicorns. Part V then turns to practical suggestions and walks through a number of ways to rein in unicorns and protect stakeholders. Part VI concludes, however, with the observation that real reform in unicorn governance is not imminent.

II. INVESTORS ARE HARMED

As this section shows, the law of corporate investment hardly ensures that unicorns are well governed. As a result, people who have material interests in the success of a unicorn are vulnerable. Specifically, this section considers unicorn investors, first as shareholders who are not effectively protected by state corporation law, and second, as investors who are not effectively protected by federal securities law. The next section considers stakeholders more broadly, who are also, generally, not legally protected from the consequences of bad firm governance.

Big investments – especially big losing investments – get attention. As of May 2020, SoftBank had invested $19.9 billion in WeWork, which nonetheless was valued at only $8 billion.[80] But not only venture capitalists and institutional investors lose money when a unicorn implodes. Ordinary shareholders, many of them employees, lose too. In fact, because start-ups often compensate employees with equity, employee shareholders may lose almost all remuneration for their work when the entity fails.

A. Corporation Law Does Not Protect Unicorn Shareholders

1. Corporation Law Theory and Practice

One might think that shareholders at WeWork, or any other unicorn,

80. Paige Leskin et al., *SoftBank-Backed Startups are Bleeding, as Investors Tighten up Scrutiny over Loss-Making Business Models*, BUS. INSIDER (Jan. 31, 2020, 3:50 PM), https://www.businessinsider.com/running-list-softbank-investments-2017-7 [https://perma.cc/NLW9-GL75] (providing a list of SoftBank technology investments); *see* Bryan Pietsch, *WeWork's Valuation has Fallen from $47 Billion Last Year to $2.9 Billion*, BUS. INSIDER (May 18, 2020, 11:38 AM), https://www.businessinsider.com/wework-valuation-falls-47-billion-to-less-than-3-billion-2020-5 [https://perma.cc/L5UK-E5AK] (noting that the valuation was due in part to the Covid-19 pandemic).

would be protected by the basic structure of the corporation and the dictates of corporation law. After all, the corporation concentrates shareholders' capital in the hands of professional management, the separation of ownership and control that Berle and Means identified as the defining characteristic of the modern corporation.[81]

In the simplest and most idealized terms, shareholders vote for the board of directors. In turn, the board runs the corporation's business and affairs, largely by installing and delegating authority to the executive officers. The officers are responsible for the day-to-day operations of the company.[82] Thus, in the corporate structure, the "owners" of the corporation appoint agents who "control" it. This system works because the directors and officers, and in fact all employees (agents) of the corporation, have fiduciary duties to act in the best interests of the corporation.[83] Failure to fulfill such duties is in principle actionable by either the corporation or its shareholders.[84]

This, one might be excused for thinking, ought to be enough to protect shareholders, and more generally, to foster sound corporate governance, regardless of whether the company is private or public.

In practice, however, shareholders have few ways to hold corporate managers accountable for the majority of their decisions. This section explores some of these problems in the context of unicorns.

2. Fiduciary Duties Are Hard to Enforce

a. Derivative Suits

Corporation law relies on the idea of fiduciary duties, but fiduciary duties can be vague.[85] In practice, shareholders' abilities to vindicate their rights to fiduciary behavior by the agents running the corporation are

81. ADOLPHE A. BERLE & GARDINER C. MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY xi (Transaction Publishers 1991) (1932).

82. DEL. CODE ANN. tit. 8, § 141(a) (2011).

83. *See* Stone v. Ritter, 911 A.2d 362, 369 (Del. 2006) (considering a shareholder derivative suit for directors' fiduciary duty failure). A full explanation of what is meant by the "best interests of the corporation," is beyond the scope or goals of this article.

84. *See* Maldonado v. Flynn, 413 A.2d 1251, 1255 (Del. Ch. 1980) (exploring directors' business judgment in the context of derivative suits).

85. *See* Mark J. Loewenstein, *The Diverging Meaning of Good Faith*, 34 DEL. J. CORP. L. 433, 433 (2009) (noting that defining the fiduciary duties of those who control corporations and unincorporated business entities has tested the flexibility and resourcefulness of the Delaware courts).

limited.[86] Firms do not always succeed; business involves risk. Many losses, including the loss of the firm itself, do not occur because some individual breached a fiduciary duty. Courts, therefore, are not inclined to see all business losses as some sort of tort, for which the victim (the investor) is owed a remedy.[87]

Suppose, however, a person behaves in a way that harms the corporation, through a breach of fiduciary duty or otherwise. In the first instance, it is the responsibility of the board and the executives to address that harm and (if appropriate) have the corporation seek redress.[88] But what if the board declines to prosecute persons that harm the corporation? What if it is the board itself, in violation of fiduciary duty, harming the corporation? In that case, the shareholders have a limited right to sue on behalf of the corporation in a derivative suit.[89] Courts in Delaware and elsewhere are hostile to such suits, which tend to upend a cardinal precept of corporation law: the power of the board to run the corporation's business.[90]

b. The Business Judgment Rule

If a derivative suit relates to a business decision made by the board,[91] then the "business judgment rule" protects that decision.[92] The business

86. *See* Julian Velasco, *Taking Shareholder Rights Seriously*, 41 U.C. DAVIS L. REV. 605 (2007) (discussing shareholder rights and how they have been affected by statutory provision and are no longer meaningful); Julian Velasco, *The Fundamental Rights of the Shareholder*, 40 U.C. DAVIS L. REV. 407, 407 (2006) (discussing the decrease in shareholder rights and the need to establish fundamental rights for shareholders); Stephen M. Bainbridge, *Response to Increasing Shareholder Power: Director Primacy and Shareholder Disempowerment*, 119 HARV. L. REV. 1735, 1736 (2006) (arguing the majority view of shareholder rights should be preserved).

87. *See In re* Citigroup Inc. S'holder Derivative Litig., 964 A.2d 109, 125–26 (Del. Ch. 2009) (noting that the business judgment rule discourages courts from hindsight evaluation of director decisions).

88. *See* Rales v. Blasband, 634 A.2d 927, 932–33 (Del. 1993) (discussing the role of the board).

89. *See* Aronson v. Lewis, 473 A.2d 805, 811 (Del. 1984) (raising the bar for pre-suit demand excusal in shareholder derivative suits).

90. *Id.* Ironically, during litigation over SoftBank's decision not to complete its 2019 agreement to purchase $3 billion of WeWork shares from Neumann and several other shareholders, the Delaware Court of Chancery took that opportunity to reaffirm the WeWork board's supremacy over matters relating to the corporation. *In re* WeWork Litig., No. CV 2020-0258-AGB, 2020 WL 4917593, at *1 (Del. Ch. Aug. 21, 2020).

91. There has been significant scholarly debate regarding the extent to which the business judgment rule protects corporate officers and executives. *See, e.g.*, Lyman P.Q. Johnson, *Corporate Officers and the Business Judgment Rule*, 60 BUS. LAW. 439, 440 (2005) (arguing that the rule should not be applied in suits against officers and executives).

92. *Lyman Johnson, The Modest Business Judgment Rule,* 55 BUS. LAW. 625, 625 (2000)

judgment rule is a judicial presumption that board decisions are informed, disinterested, and in the best interests of the corporation.[93] Courts therefore will not overturn, or punish management for, such decisions. The business judgment rule's presumptions in favor of the board can be rebutted, for example, by showing an uninformed decision, but rebuttal is difficult.[94] Suits challenging the business judgment of corporate directors or executives fail most of the time.[95] Generally, even questionable corporate decisions, such as buying a coding bootcamp operator,[96] are likely to be protected by the courts.

c. Duty of Loyalty: Oversight and Conflicts of Interest

If the suit relates to the board's oversight of the corporation, corporation law requires the shareholders to show that the director or executive acted in bad faith and violated a duty of loyalty to the corporation.[97] To extract compensation on behalf of the corporation, the shareholders must show grievous lack of supervision by the board.[98] Shareholder derivative complaints based on oversight failures have been called the most difficult to bring in corporation law,[99] and these suits seldom survive an initial motion to dismiss.[100]

A fiduciary duty of loyalty violation is slightly easier to establish in

(explaining that the business judgment rule can be understood as a policy of judicial non-review of board decisions).

93. Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984).

94. Cede & Co. v. Technicolor, Inc., 634 A.2d 345, 361 (Del. 1993) (noting that there is a powerful presumption in favor of the decisions that a board of director makes).

95. Itai Fiegenbaum, *The Controlling Shareholder Enforcement Gap*, 56 AM. BUS. L.J. 583, 601–02 (2019) (observing that in most cases, allegations of director negligence will be dismissed because they fail to overcome the presumptions of the business judgment rule).

96. *See* Becky Peterson & Meghan Morris, *WeWork's Coding Boot Camp Flatiron School Has Laid off Dozens of Employees*, BUS. INSIDER (Nov. 7, 2019, 12:40 PM), https://www.businessinsider.com/weworks-flatiron-school-lays-off-dozens-of-people-2019-11 [https://perma.cc/LX9U-W2QG] (reporting layoffs at the school).

97. *See* Stone v. Ritter, 911 A.2d. 362, 370 (Del. 2006) (refusing to excuse pre-suit demand in a shareholder derivative suit relating to board oversight).

98. *See* Reiter v. Fairbank, C.A. No. 11693-CB, 2016 WL 6081823, (Del. Ch. Oct. 18, 2016) (holding that the plaintiffs failed to plead facts that show the directors acted in bad faith).

99. *See In re* Caremark Int'l Inc. Derivative Litig., 698 A.2d 959, 967 (Del. Ch. 1996) (refusing to excuse pre-suit demand in a shareholder derivative suit relating to board oversight).

100. *See* Anne Tucker Nees, *Who's the Boss – Unmasking Oversight Liability within the Corporate Power Puzzle*, 35 DEL. J. CORP. L. 199, 205 (2010) ("Such claims have been quickly dismissed for engaging in second-guessing of business decisions.").

cases of management conflict of interest. For example, what if a CEO buys buildings and then rents them back to the corporation?[101] Fiduciary duty would seem to prohibit such self-dealing.[102]

Given the regularity with which conflicts of interest arise, however, corporation law has developed ways that a corporation may "cleanse" such transactions. Such "safe harbors" require the informed approval of a majority of the disinterested directors, informed approval by a majority of the shareholders, or a judicial finding that the transaction was fair to the corporation.[103] If the corporation jumps through one of these hoops, shareholder ability to challenge the transaction is limited. Thus, conflicts of interest like the self-dealing[104] and nepotism that attracted attention at WeWork[105] are subject to more exacting corporation law requirements, but such requirements may not be stringent enough to deter the action.

d. Procedural Barriers

It is not just the substantive law that makes shareholder derivative suits difficult to pursue. There are significant procedural barriers as well. The pre-suit demand requirement in derivative litigation requires shareholders to "allege with particularity the efforts, if any, made by the plaintiff to obtain

101. Brown, *supra* note 7. Conflicts have arisen in other current and former unicorns. *See, e.g.*, Jeff Montgomery, *Six Tesla Directors Settle SolarCity Merger Suit in Del. for $60M*, LAW360 (Jan. 30, 2020, 4:51 PM) (discussing partial settlement of suit against Tesla founder Elon Musk and his fellow Tesla directors arising from Tesla's purchase of SolarCity, a company founded by Musk and two cousins, and in which Musk and five of the Tesla directors owned substantial stock).

102. *See* Weinberger v. Uop, Inc., 457 A.2d 701, 710 (Del. 1983) (rejecting a merger for failing to satisfy the reasonable concept of fair dealing because of conflicts of interest among the directors). In the case of WeWork, many of the outside directors had conflicts of interest themselves. Farrell & Brown, *supra* note 26.

103. *See* Benihana of Tokyo, Inc. v. Benihana, Inc., 906 A.2d 114, 120 (Del. 2006) (stating that interested director transactions approved pursuant to the Delaware Corporations Law §144 safe harbor are reviewed under the business judgment rule).

104. Eliot Brown, *WeWork's Long List of Potential Conflicts Adds to Questions Ahead of IPO*, WALL ST. J. (Sept. 6, 2019, 6:26 PM), https://www.wsj.com/articles/weworks-long-list-of-potential-conflicts-adds-to-questions-ahead-of-ipo-11567808023 [https://perma.cc/UF7T-2WG7] (noting a corporate culture rife with conflicts of interest and a lack of accountability).

105. Neumann is reported to have toasted "to nepotism" at a WeWork retreat. *See* Farrell & Brown, *supra* note 26 (reporting that children of board members were hired by WeWork); *see also* Eliot Brown et al., *WeWork Cleans House, Looks to Trim Staff Close to Ex-CEO, Sell Private Jet*, WALL ST. J. (Sept. 27, 2019, 3:13 AM), https://www.wsj.com/articles/wework-cleans-house-looks-to-trim-staff-close-to-ex-ceo-sell-private-jet-11569531640 [https://perma.cc/N5LR-VJ3H] (noting that, in the wake of Neumann's stepping down as CEO, the new leaders had plans to fire nearly twenty friends and family members of Neumann and his wife).

the action the plaintiff desires from the directors or comparable authority and, if necessary, from the shareholders or members, and the reasons for the plaintiff's failure to obtain the action or for not making the effort."[106] In a pleading (pre-discovery) context, this is difficult.[107] Because a request to the board to file suit (against its own members or its appointed executives) is likely to produce a negative answer, which is then protected by the business judgement rule, shareholders tend to seek excusal of the pre-suit demand requirement.[108] In order to be excused from making a demand upon the board, however, shareholders must show that demand would have been futile,[109] which is another high hurdle.[110] And finally, even if directors are shown to have violated their fiduciary duties, many corporations have exculpation,[111] indemnification, and/or insurance[112] measures that protect directors, further weakening the deterrent effect of corporation law penalties.

Thus, despite corporation law provisions requiring executives and directors to act in the unicorn's best interests, shareholders are far from protected by the law and have a limited ability to obtain a remedy even if they are able to show bad behavior.

Nevertheless, on November 4, 2019, a WeWork minority shareholder and former employee filed a class action and derivative complaint against Neumann, WeWork directors, and SoftBank.[113] The complaint alleges that

106. Del. Ch. Ct. R. 23.1(a).

107. *See* Kamen v. Kemper Fin. Servs., Inc., 500 U.S. 90, 96 (1991) (holding that the demand requirement in Rule 23.1 "speaks only to the adequacy of the shareholder representative's pleadings").

108. *See* Collins J. Seitz, Jr.& S. Michael Sirkin, *The Demand Review Committee: How It Works, and How It Could Work Better*, 73 BUS. LAW. 305, 317 (2018) (arguing for a conditional demand in order to ameliorate the "harsh consequences" of a stockholder making a demand).

109. Rales v. Blasband, 634 A.2d 927, 932–33 (Del. 1993). The Model Business Corporations Act, which reflects practices in a number of other (non-Delaware) states, requires the pre-suit demand. MODEL BUS. CORP. ACT §7.42 (2016).

110. Aronson v. Lewis, 473 A.2d 805, 811 (Del. 1984).

111. *See* Julian Velasco, *The Diminishing Duty of Loyalty,* 75 WASH. & LEE L. REV. 1035, 1090–91 (2018) (calling exculpation provisions "ubiquitous").

112. *See* 4 JAMES D. COX & THOMAS LEE HAZEN, TREATISE ON THE LAW OF CORPORATIONS §15:21 (3d ed. 2019) (delineating a basic overview of director indemnification and insurance).

113. *See* First Amended Shareholder Class Action and Derivative Complaint, Carter v. Neumann (No. CGC-19-580474) (Cal. Sup. Ct. Jan. 10, 2020) (arguing that Adam Neumann, the We Company board, and SoftBank are working in concert with one another to the benefit of themselves and the detriment of We Company's minority shareholders); *see also* Theron Mohamed, *A Former WeWork Employee Is Suing Over Adam Neumann's $1.7 Billion Golden Parachute*, Bus. Insider (Nov. 9, 2019), https://markets.businessinsider.com/news/stocks/we work-ex-employee-sues-adam-neumann-2-billion-leaving-deal-2019-11-1028675038 [https: //perma.cc/S76A-2MF3] (detailing the original complaint filed by Natalie Sojka, which was later combined with others and amended).

Neumann, Softbank, and the WeWork board members (whom the complaint described as "supine")[114] breached their fiduciary duties. The complaint alleges that the board approved self-dealing transactions like WeWork leasing space in buildings that Neumann owned and purchasing the "We Company" name from Neumann[115] and provided "massive" loans on commercially unreasonable terms to Neumann.[116] The derivative suit also emphasizes the fact that, because WeWork is a private company which failed to hold annual meetings for several years, minority shareholders had only limited information about the company.[117] The suit emphasizes the adverse financial impact on the minority shareholders, whose stock and options have lost most or all of their value.[118]

3. Problems with Board Independence and Diversity

a. Founder Dominance and Multi-Class Share Structures

Unicorn shareholders might seek judicial enforcement of fiduciary duties because they cannot get satisfaction through corporate governance, *i.e.,* electing a board that will look out for their interests.[119] In many cases, corporation law does not ensure adequate unicorn governance because the founder(s) dominate such start-ups, often serving as chief executive and a board member (perhaps chair).[120] It is also common for all of the board members to be friendly with the founder, who is likely to hold the majority

114. First Amended Shareholder Class Action and Derivative Complaint, Carter v. Neumann, *supra* note 113, para. 58.

115. First Amended Shareholder Class Action and Derivative Complaint, Carter v. Neumann, *supra* note 113, para. 48–9.

116. First Amended Shareholder Class Action and Derivative Complaint, Carter v. Neumann, *supra* note 113, para. 78.

117. First Amended Shareholder Class Action and Derivative Complaint, Carter v. Neumann, *supra* note 113, para. 13–14.

118. First Amended Shareholder Class Action and Derivative Complaint, Carter v. Neumann, *supra* note 113, para. 68.

119. Much has been written about the fact that shareholder voting may be ineffective in a large corporation. LISA M. FAIRFAX, SHAREHOLDER DEMOCRACY: A PRIMER ON SHAREHOLDER ACTIVISM AND PARTICIPATION 4 (Carolina Academic Press, 2011).

120. *In re* Cysive, Inc. S'holders Litig., 836 A.2d 531, 553 (Del. Ch. 2003) (involving a shareholder challenge to a management buy-out in which the chief proponent was the founder, CEO, and board chair who controlled approximately 40% of the company's voting equity); N.J. Carpenters Pension Fund v. infoGROUP, Inc., No. Civ.A. 5334-VCN, 2011 WL 4825888, at *4, *11 (Del. Ch. Oct. 6, 2011) (determining that a board lacked independence in connection with a merger transaction based on allegations that the company's founder, former CEO, and director owned approximately 37% of the company's stock and pressured the board to sell the company under sub-optimal circumstances due to a personal liquidity concern).

of the voting shares.[121] Board members may be founder family members,[122] or representatives of early investors such as venture capital firms,[123] who are bullish on the entity and its management.[124] Some WeWork directors reportedly saw themselves more as advisers than as persons with oversight and decision-making responsibility.[125]

The rise of these founder-dominated unicorns, especially in the technology sector, has been accompanied by a resurgence of multi-class share systems.[126] This problem is not entirely new, nor restricted to privately

121. *See* Elizabeth Pollman, *Startup Governance*, 168 U. PA. L. REV. 155, 200–09 (2019) (discussing board monitoring failures in the startup context).

122. For example, Elon Musk's brother, Kimbal Musk, has long served on the board of the former unicorn, Tesla. Tom Hals, *Tesla Directors Settle, Isolating Musk as SolarCity Trial Looms*, REUTERS (Jan. 30, 2020), https://www.reuters.com/article/us-tesla-solarcity-lawsuit/tesla-directors-settle-isolating-musk-as-solarcity-trial-looms-idUSKBN1ZT2HF [https://perma.cc/S3PX-7CBG].

123. Until the SoftBank shakeup following the cancelled IPO, the WeWork board included Neumann, as well as Softbank executive Ron Fisher; Rhone Capital CEO Steven Langman; former Goldman Sachs executive Mark Schwartz; Lew Frankfort, former CEO of handbag maker Coach; Bruce Dunlevie, the CEO of Benchmark Capital, and John Zhao, CEO of Hony Capital. David Jeans, *Three WeWork Board Members to Depart, Another to Follow*, THEREALDEAL (Feb. 6, 2020), https://therealdeal.com/national/2020/02/06/exclusive-three-wework-board-members-depart-another-to-follow/amp/ [https://perma.cc/9PBK-8C7D].

124. *See* Charles Duhigg, *supra* note 16 (discussing how Bruce Dunlevie joined the WeWork board and admitted to a partner that he was taken with Neumann but did not know how WeWork would ever make a profit). This "bullish" attitude is most clearly demonstrated by unicorn valuations. Brett Ryder, *WeWork Shows Why Some Venture Capitalists are in a World of Make-Believe*, ECONOMIST (Sept. 28, 2019) www.economist.com/business/2019/09/28/wework-shows-why-some-venture-capitalists-are-in-a-world-of-make-believe [https://perma.cc/SX6Y-97N7] ("It is the venture-capital industry that helps spin the invisible yarn that creates the legends. Some of its biggest names, such as SoftBank, have been peddling valuations of companies like WeWork that border on the absurd"). Pavel Alpeyev *et al.*, *SoftBank Unveils $9.5 Billion WeWork Rescue, Gets 80% Stake*, BLOOMBERG (Oct. 23, 2019) (suggesting that people are suspicious of actual valuations of unicorn companies).

125. Farrell & Brown, *supra* note 26. Bill Gurley, a partner at WeWork venture capital investor Benchmark Capital, has described the struggles of venture firms to balance their duties as board members with their need to foster close relationships with founders: "Silicon Valley has become so competitive in the venture capital market that the level of discipline invoked from the board is just not there." Winkler, *supra* note 41. There were a number of internal problems at WeWork that should have concerned the WeWork board members, and some of the company's collateral ventures seemed "outlandish," but the board approved nearly all of Neumann's proposals. Duhigg, *supra* note 16.

126. Lucian A. Bebchuk & Kobi Kastiel, *The Untenable Case for Perpetual Dual-Class Stock,* 103 VA. L. REV. 585, 594 (2017) (arguing that there has been an upward trend in the adoption of dual-class stock since Google went public with a dual-class structure in 2004, followed by well-known tech companies, such as Facebook, Groupon, LinkedIn, Snap, Trip Advisor, and Zynga).

held companies. Henry Ford used dual-class shares.[127] But the use of dual-class shares to ensure founder domination has reached a new prominence.[128] In 2019, over 38% of technology IPOs and over 22% of all IPOs had dual-class share structures.[129]

By holding super-voting shares (shares that get three or five or 10 or even 20 votes-per-share),[130] unicorn founders and their friends ensure complete control of the company: the right to appoint all of the directors[131] and to green-light even fundamental transactions that normally would require broad-based shareholder approval. In many cases such as Facebook and Alphabet, founder voting control persists even once the firms have moved into the public markets.[132] This control, vested in a small cadre of

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127. *See* Joel Seligman, *Equal Protection in Shareholder Voting Rights: The One Common Share, One Vote Controversy*, 54 GEO. WASH. L. REV. 687, 700 (1985) (discussing Ford's use of dual-class shares). Ironically, Neumann has been compared to Henry Ford in his effort to transform the workplace. Sam Walker, *WeWork's Adam Neumann Was Right About One Thing: Someone Needs to Reinvent Work*, WALL ST. J. (Sept. 21, 2019), https://www.wsj.com/articles/weworks-adam-neumann-was-right-about-one-thing-someone-needs-to-reinvent-work-11569038406 [https://perma.cc/9D4C-TPEM].

128. *See, e.g.*, Maureen Farrell, *In Snap IPO, New Investors to Get Zero Votes, While Founders Keep Control*, WALL ST. J. (Jan. 16, 2017), https://www.wsj.com/articles/in-snap-ipo-new-investors-to-get-zero-votes-while-founders-keep-control-1484568034 [https://perma.cc/2QSU-SGBA] ("Between 2012 and 2016, roughly 19% of U.S. tech firms that went public did so with dual-class structures—more than double the share over the prior five-year period.").

129. Ritter, *supra* note 74.

130. Facebook's multi-class shares include Class B shares, controlled by founder Mark Zuckerberg and a small group of insiders, totaling about 18% of the shares, but with 10 votes-per-share. Bob Pisani, *Shareholders Won't Force Zuckerberg's Hand in Facebook Management,* CNBC (Mar. 20, 2018), https://www.cnbc.com/2018/03/20/shareholders-wont-force-zuckerbergs-hand-in-facebook-management.html [https://perma.cc/M245-2QKT]. Alphabet (Google) has three classes of stock, but it is the B Shares, controlled by insiders Larry Page, Sergey Brin and Eric Schmidt, that control over 60 percent of the voting shares with 10 votes-per-share. The publicly traded Class A shares have only one vote-per-share (GOOGL) and the other publicly traded shares, Class C (GOOG), have no voting rights. *Id.*

131. *See* Matt Levine, *We Wants a New Boss*, BLOOMBERG OPINION (Sept. 23, 2019), https://www.bloomberg.com/opinion/articles/2019-09-23/we-wants-a-new-boss [https://perma.cc/LDE2-NMDW] (explaining that thanks to the supervoting shares, Neumann controlled all the votes and so had the power to fire the entire board, though SoftBank's investment provided considerable influence).

132. *See, e.g.*, Deepa Seetharaman & Emily Glazer, *Mark Zuckerberg Asserts Control of Facebook, Pushing Aside Dissenters*, WALL ST. J. (Apr. 28, 2020), https://www.wsj.com/articles/mark-zuckerberg-asserts-control-of-facebook-pushing-aside-dissenters-11588106984 [https://perma.cc/G66W-B642] (noting Zuckerberg's control over eight years after the company's IPO); *see also* Troy Wolverton, *Facebook's Mark Zuckerberg isn't accountable to anyone so it's time Congress took away the source of his power,* BUS. INSIDER (Nov. 17, 2018), https://www.businessinsider.com/congress-should-ban-facebooks-dual-class-stock-structure-2018-11?op=1 [https://perma.cc/4LG3-DGTG] (comparing Zuckerberg to an

managers, has arguably prevented the normal functioning of the corporate form and has enabled some of the excesses of recent years.[133]

In the case of WeWork, when the first draft of its Form S-1 was made public on August 14, 2019, the markets learned that Neumann was holding super-voting Class B and Class C shares with 20 votes each.[134] The proposed capital structure ensured Neuman's control of the company not only for his lifetime, but beyond the grave. At one meeting with the company employees, Neumann described the company as not, "just controlled – we're generationally controlled," and claimed that "one day, maybe in 100 years, maybe in 300 years, a great-great-granddaughter of mine will walk into that room and say, 'Hey you don't know me; I actually control the place.'"[135] Part of the SoftBank bailout deal in October 2019 was the requirement that all WeWork shares carry one vote apiece.[136]

There have been several regulatory initiatives to restrain the use of multi-class share structures. In 1988, the SEC promulgated Rule 19c-4, which prohibited exchanges from listing stock of companies that issued dual-

"absolute monarch" who lacks accountability because of the Facebook share structure); Pollman, *supra* note 121, at 181–82 (explaining how founder control is established in the pre-IPO stages of startups).

133. For a more detailed discussion of these issues, *see generally* Westbrook & Westbrook, *supra* note 72 (arguing that control by unicorns' founders and insiders in the private markets, combined with the dominance of a small number of institutional investors in the public markets, has produced a concentration of power that may threaten corporate governance).

134. We Co., *supra* note 20. The media focused on the August 2019 draft Form S-1 revelation that Neumann controlled the majority of voting rights through the company's Class B and Class C shares, with both classes carrying 20 votes-per-share compared with Class A shares, which have one vote-per-share. Annie Palmer, *WeWork's Valuation Could Fall to Below $15 billion in IPO, Down From $47 billion Private Valuation*, CNBC (Sep. 13, 2019), https://www.cnbc.com/2019/09/13/wework-makes-sweeping-corporate-governance-changes-ahead-of-ipo.html [https://perma.cc/Q4ZK-ZKPC]. In an amended Form S-1 filed September 13, 2019, WeWork claimed it was changing its super-voting stock from 20 votes-per-share to 10 votes-per-share, curtailing Neumann's voting power. We Co., Amendment No. 2 to Form S-1 Registration Statement (Sept. 13, 2019).

135. Loizos, *supra* note 12; Meghan Morris, *Leaked Video Reveals Adam Neumann Told Staff Earlier This Year That His Family Had 100% Control of WeWork and That Even in 300 Years His Descendants Would Be in Control*, BUS. INSIDER (Oct. 18, 2019), https://www.businessinsider.com/wework-adam-neumann-said-family-control-company-300-years-january-2019-10 [https://perma.cc/ZMV9-TXTT]; *see also* Platt & Edgecliffe-Johnson, *supra* note 13 (reporting Neumann hoped to keep the company in his family's control for generations). As mentioned, this control is not necessarily curbed by a public offering. Google, LinkedIn, Groupon, Zyna, Facebook, Wayfair, Match and Snap, to name just a few, went public with dual-class shares preserving founder voting control. *See* Westbrook & Westbrook, *supra* note 70, at 871–80.

136. *See* Farrell & Brown, *supra* note 26 (detailing the SoftBank bailout).

class shares.[137] That rule was removed after the Business Roundtable, a non-profit association of chief executives of major U.S. companies,[138] successfully challenged it as beyond the SEC's power.[139] In response to recent scandals and objections, stoked by the Snap (non-voting shares) IPO,[140] several indexes have restricted new listings by companies with dual-class share structures.[141] This may indicate a shift in market tolerance for such arrangements,[142] but they remain commonly used by unicorns.[143]

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137. Voting Rights Listing Standards; Disenfranchisement Rule, 53 Fed. Reg, 26,376, 26,394 (1988), codified at 17 CFR §240.19c-4 (1990).

138. *About Us,* BUSINESS ROUNDTABLE, https://www.businessroundtable.org/about-us [https://perma.cc/G8MV-MH3D] (last visited Feb. 23, 2020).

139. *See* Business Roundtable v. SEC, 905 F.2d 406 (D.C. Cir. 1990) (holding that the SEC lacked statutory authority to prohibit exchanges from listing stock of corporations which nullify, impair, or disparately reduce per share voting rights of common shareholders). For a full discussion of the rule and the Business Roundtable's case, *see generally* Stephen M. Bainbridge, *The Short Life and Resurrection of SEC Rule 19c-4*, 69 WASH. U. L. Q. 565 (1991) (explaining the motivation for the promulgation of the rule).

140. *See generally* Westbrook & Westbrook, *supra* note 70 (walking through the Snap IPO, other IPOs by companies with dual-class share structures, and both regulatory and market reactions to those structures). Following its IPO, Snap was involved in a protracted legal fight with investors over allegedly faulty growth metrics ahead of the offering. That litigation was settled for $187.5 million in February 2020. Tyler Sonnemaker, *Snap Says It Agreed to a $187.5 Million Settlement in a Lawsuit Where Investors Said That the Company Understated Snapchat's Threat from Instagram,* BUS. INSIDER (Feb. 4, 2020), https://www.businessinsider.com/snap-budgets-100-million-preliminary-settlement-ipo-class-action-lawsuit-2020-2 [https://perma.cc/7JJ5-3D4E] (noting that the DOJ and SEC dropped their investigation over the matter in 2019).

141. "Tracking stocks and companies with multiple share class structures are NOT eligible for the S&P Composite 1500 and its component indices." S&P DOW JONES INDICES, S&P U.S. INDICES: METHODOLOGY 6 (2019), https://us.spindices.com/documents/methodologies/methodology-sp-us-indices.pdf [https://perma.cc/4LLN-2GF6]; *see also* Joanna Ossinger, *Goldman Gives New Reason IPOs May Suffer: Multi-Class Shares,* BLOOMBERG (Sept. 30, 2019), https://www.bloomberg.com/news/articles/2019-09-30/goldman-gives-another-reason-ipos-may-suffer-multi-class-shares [https://perma.cc/MTX5-P9K8] (noting that firms restricted for joining major indices will miss out on flows from passive investment managers tracking those benchmarks).

142. The August 2019 draft Form S-1 also claimed Neumann's super-voting shares would be reduced to 10 votes-per-share if he did not donate a least $1 billion to charity within 10 years of the planned IPO. *See* Andrea Vittorio, *WeWork Links Co-Founder's Voting Rights to Charity Giving Goal*, BLOOMBERG LAW (Aug. 16, 2019), https://www.bloomberglaw.com/document/XBR82N50000000?bna_news_filter=corporate-law&jcsearch=BNA%25200000016c96dddeaea97ff6df24490001#jcite [https://perma.cc/TRW5-YGYC] (reporting that investors opposed to founder-favoring dual-class share structures have been pushing companies like Lyft and Pinterest to add sunset provisions to their arrangements).

143. For a defense of dual-class share structures, *see* Bernard S. Sharfman, *A Private Ordering Defense of a Company's Right to Use Dual-Class Share Structures in IPOs*, 63 VILL. L. REV. 1, 26–31 (2018) (discussing the regulatory history of class share structures and arguing that they provide an optimal corporate governance scheme). For a more innovative

b. *Lack of Diversity in Unicorn Boards (and Financing)*

The technology sector, where most unicorns are found, long has been criticized for its "boys' club" mentality, with regard to both investment and operations.[144] Founder dominance often exacerbates and is exacerbated by the lack of gender diversity on unicorn boards. Most unicorns lack even a single woman director. Fewer than 10% of unicorn board seats are held by women.[145] Consonantly, in 2019, only about 14% of venture-capital deals funded companies with at least one woman founder, and less than 3% of the deals were with all-female-founded firms.[146] A management structure dominated by a small number of similar persons may be expected to foster groupthink.[147] Lacking the variety of strengths and capabilities of a diverse group of directors, unicorn boards may circumscribe their decision-making capacity.[148]

This problem is in part enabled by the fact that several of a unicorn's directors are usually appointed by venture capitalists, who are

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approach, *see also* Lawrence Cunningham, *Quality Shareholder Voting*, THE CLS BLUE SKY BLOG (Nov. 21, 2019), https://clsbluesky.law.columbia.edu/2019/11/21/quality-shareholder-voting/ [https://perma.cc/J36L-KDFJ] (proposing a "Quality Shareholder Voting" approach that would increase the voting power of long-term shareholders by adding votes to shares based on holding periods and high concentrations).

144. Olufunmilayo B. Arewa, *Investment Funds, Inequality, and Scarcity of Opportunity*, 99 B.U. L. REV. 1023, 1043–44 (2019) (noting that 75% of venture capital firms have never had a senior woman investor). This is contrasted with the fact almost all Fortune 500 company boards have at least one female director. *See* Claire Zillman & Emma Hinchliffe, *WeWork Rent the Runway, Heidi Cruz, Cyan Banister: Broadsheet October 19*, FORTUNE (Oct. 19, 2018), http://fortune.com/2018/10/19/wework-rent-the-runway-heidi-cruz-cyan-banister-broadsheet-october-19/ [https://perma.cc/3VXZ-FYLY] (noting the conflicting feelings that many majority board members have regarding the push toward board diversification). *But see* Allyson Kapin, *Women-Led Startups Are Tearing Down the Boys' Club,* FORBES (Mar. 31, 2019), https://www.forbes.com/sites/allysonkapin/2019/03/31/women-led-startups-are-tearing-down-the-boys-club/#a2924147b6e3 [https://perma.cc/R5ZD-4JY9] (noting that Rent the Runway and Glossier had just achieved unicorn status).

145. According to Boardlist, as of June 30, 2017, only 8.75% of unicorn board seats were held by women. *Women on Unicorn Boards*, BOARDLIST, https://theboardlist.com/research [https://perma.cc/D26H-CLCB] (last visited Feb. 28, 2020).

146. *See* PITCHBOOK & NAT'L VENTURE CAPITAL ASS'N, VENTURE MONITOR 4Q 2019, 24 https://files.pitchbook.com/website/files/pdf/Q4_2019_PitchBook_NVCA_Venture_Monitor.pdf [https://perma.cc/FA5V-63AZ] (last visited Feb. 13, 2020) (pointing out that these low numbers represented an increase from 2018 levels).

147. *See* IRVING LESTER JANIS, VICTIMS OF GROUPTHINK: A PSYCHOLOGICAL STUDY OF FOREIGN-POLICY DECISIONS AND FIASCOES 2–3 (1972) (analyzing the decisions that are made when there is a close-knit body seeking consensus under strong leadership).

148. *See* Deborah L. Rhode & Amanda K. Packel*, Diversity on Corporate Boards: How Much Difference Does Difference Make?* 39 DEL. J. CORP. L. 377, 394–401 (2014) (evaluating arguments for and studies relating to racial, ethnic, and gender diversity on corporate boards).

overwhelmingly male.[149] A 2018 report noted that nearly 75% of venture capital firms had no women partners.[150] In fact, homogeneity in venture capital firms is not confined to gender. According to another report, in 2018, 82% of venture capital investors were male, 70% were white, and 40% of them went to either Harvard or Stanford.[151] Drawn from a small pool, many of the powerful[152] financing sources for unicorns present "one-sided sentiment."[153] This risks positive feedback for even the most erratic unicorn management.

In August 2019, the WeWork board included Neumann and six other men affiliated with WeWork investors.[154] The other board members have been described as "mesmerized" by Neumann, and they did not impose much restraint: "[l]ittle of WeWork's trajectory would have been possible were it not for the collection of veteran executives and financiers from the upper echelons of Wall Street and Silicon Valley who enabled Mr. Neumann."[155] The board shakeup following the failed IPO resulted in the appointment of an array of new investor representatives, including a female Softbank executive.[156]

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149. Silicon Valley has been described as a "boys' club" with limited opportunities for women. *See* EMILY CHANG, BROTOPIA: BREAKING UP THE BOYS' CLUB OF SILICON VALLEY 40 (2018) (suggesting that the lack of diversity negatively impacts decision-making); s*ee also* Pollman, *supra* note 121, at 173 (discussing the rights of venture capital investors).

150. *See* Cromwell Schubarth, *More VC Forms Have Women Partners But Nearly 75% Have None,* SILICON VALLEY BUS. J. (Jan. 2, 2019), https://www.bizjournals.com/bizwomen/news/latest-news/2019/01/more-vc-firms-have-women-partners-but-most-have.html [https://perma.cc/6CBN-BQCV] (noting that the "overwhelming majority" of venture money is going to startups that have no women on the founding team).

151. Richard Kerby, *Where Did You Go to School?* NOTEWORTHY – THE JOURNAL BLOG (July 30, 2018), https://blog.usejournal.com/where-did-you-go-to-school-bde54d846188 [https://perma.cc/S7PP-HCTJ].

152. *See* Ilya A. Strebulaev & Will Gornall, *How Much Does Venture Capital Drive the U.S. Economy?*, INSIGHTS BY STAN. BUS. (Oct. 21, 2015), https://www.gsb.stanford.edu/insights/how-much-does-venture-capital-drive-us-economy [https://perma.cc/Y8UU-FJ5A] (noting that a fifth of current public U.S. companies received venture capital financing).

153. Fried & Gordon, *supra* note 69.

154. *See supra* note 123 (listing 2019 board members).

155. Farrell & Brown, *supra* note 26.

156. In 2020, Softbank executive Ron Fisher, Rhone Capital CEO Steven Langman, former Goldman Sachs executive Mark Schwartz, and Lew Frankfort, former CEO of handbag maker Coach, left or were expected to leave the board. Their places were taken by WeWork's newly appointed CEO Sandeep Mathrani, SoftBank executives Kirthiga Reddy and Marcelo Claure (as chairman), and Jeff Sine, a partner of the Raine Group. Jeans, *supra* note 123. However, in part due to the ongoing litigation relating to SoftBank's decision not to pursue the tender offer reported in fall 2019, new directors have been added to the board, but several of the original directors remained. *See* Konrad Putzier, *WeWork Directors Sue SoftBank Over Terminated $3 Billion Share Offer*, WALL ST. J. (Apr. 7, 2020), https://www.

B. Securities Law Does Not Protect Unicorn Investors

1. Securities Law Theory and Practice

a. Historical Background

Classically, startups raise money (and compensate employees) by issuing equity, shares of stock. Those shareholders are participants in corporate governance, and their rights and privileges are governed by state corporation laws, discussed in the preceding section. But shares are also securities, and investors in securities (stocks, bonds, and many other instruments) are protected by the securities laws, most of which are federal.[157]

Most large companies—which, in the course of their history, raise capital by issuing securities to the public—are disciplined by securities laws.[158] Those laws were designed during the Great Depression and in direct response to the stock market crash of 1929.[159] They are based on the understanding that ordinary people, including the most uninformed and vulnerable investors ("widows and orphans")[160] might be persuaded, often fraudulently, to buy stock in companies without appreciating the risks.[161]

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wsj.com/articles/wework-directors-sue-softbank-over-terminated-3-billion-share-offer-11586271317#:~:text=Konrad%20Putzier,-Biography&text=Two%20WeWork%20directors%20filed%20a,%243%20billion%20in%20WeWork's%20shares.&text=The%20board%20is%20made%20up,Dunlevie%20and%20former%20Coach%20Inc [https://perma.cc/WLX3-9KR8] (explaining Lew Frankfort and Bruce Dunlevie's roles in the litigation); *see also* Jef Feeley, *WeWork Board Factions Head for Clash Over New Directors*, BLOOMBERG NEWS (May 28, 2020, 8:14 AM), https://news.bloomberglaw.com/corporate-governance/wework-board-factions-head-for-clash-over-new-directors?context=search&index=1 [https://perma.cc/XSJ9-LDR7] (outlining plans to appoint the new directors, and the litigation). It is unclear whether minority shareholders will benefit from the new management.

157. *See* 4 JAMES D. COX & THOMAS LEE HAZEN, TREATISE ON THE LAW OF CORPORATIONS § 27:3 (3d ed. 2019) (outlining the role of state "blue sky" laws).

158. *See* Westbrook & Westbrook, supra note 72, at 704–12 (describing the emergence of securities law and the resulting effects on the conduct of business).

159. *See* Steve Thel, *The Original Conception of Section 10(b) of the Securities Exchange Act,* 42 STAN. L. REV. 385, 408 (1990) (noting that the public blamed the Stock Market Crash for the Great Depression, which made substantial legislation to regulate stock exchanges inevitable).

160. *See* Adam C. Pritchard, *The SEC at 70: Time for Retirement?* 80 NOTRE DAME L. REV. 1073, 1085 (2005) (noting the SEC's focus on protecting vulnerable and uninformed investors).

161. *What We Do,* U.S. SEC. & EXCH. COMM'N, https://www.sec.gov/Article/whatwedo.html#create [https://perma.cc/X88V-R5BN] (last updated Oct. 15, 2020) (overview of the SEC functions and responsibilities).

Consequently, Congress imposed an anti-fraud and mandatory disclosure regime. By requiring companies to provide information material to investment decisions and punishing their failure to do so as securities fraud, Congress hoped both to protect investors and to ensure the soundness of securities markets, which in turn would foster the formation of investment capital.[162] In broad outline, the federal securities law seem to have worked pretty well.[163]

Under this regime, in order to raise money in the public markets (by, for example, offering stock to the public) companies must register with the SEC, detailing the investment in a registration statement, which is made available to the public. After the IPO, the company is required to file periodic reports, which are also made available to the public.[164] Going public has traditionally been understood to offer numerous advantages to a company: a relatively cheap way to raise large amounts of capital; liquidity for founders; a currency with which the company could pursue acquisitions; and a signal to the market that the company was mature.[165] In exchange, a company accepts the costs of the transition, including the discipline of mandatory public accounting, enforced by antifraud remedies.[166]

b. The Public-Private Distinction

Securities law generally distinguishes between public transactions, which are subject to extensive regulation, and non-public, or "private,"

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162. *See* Thel, *supra* note 159 (explaining the background of the federal securities laws and the drive to prevent and punish misleading information provided to investors, which could foster sound, long-term investment).

163. *See e.g.*, Merritt B. Fox, *Retaining Mandatory Securities Disclosure: Why Issuer Choice Is Not Investor Empowerment*, 85 VA. L. REV. 1335, 1416 (1999) (finding disclosure on the whole beneficial). *But see* Roberta Romano, *Empowering Investors: A Market Approach to Securities Regulation*, 107 YALE L.J. 2359, 2376 (1998) (finding that mandatory disclosure is not effective).

164. What we commonly refer to as a "public" company is required to file periodic reports under the Securities Exchange Act of 1934 (the Exchange Act). Reporting company status may be triggered by listing securities on a national exchange (Exchange Act § 12(a)), exceeding the 2000 shareholder cap along with having over $10 million in assets (Exchange Act § 12(g)), or engaging in a registered public offering – often of debt securities (Exchange Act § 15(d)). *See* STEPHEN J. CHOI & A.C. PRITCHARD, SECURITIES REGULATION: CASES AND MATERIALS 205 (5th ed. 2019) (summarizing the three categories of public companies under the Exchange Act).

165. *See* Jones, *supra* note 57, at 170 (outlining the advantages typically associated with going public).

166. *See* Westbrook & Westbrook, *supra* note 72 at 711–12 (describing the legal obligations that accompany growth via public offerings).

transactions, which are much less heavily regulated.[167] This distinction often corresponds to a company's size. To understand why, consider the easy case of a small company that distributes shares to its investors. A traditional assumption has been that there is little risk of a small company harming its unknowing investors or the economy as a whole.[168] Its investors, perhaps friends or family, are in a position to know the managers personally, and therefore may be informed enough about the risks and opportunities presented by the investment to fend for themselves.[169] Wealthy or very sophisticated investors tend to be similarly knowledgeable, albeit for different reasons. They generally are in a position to bargain for information, may employ their own lawyers, accountants and other experts, and therefore have little need for information required in compliance with the mandatory disclosure regime of the securities laws.[170]

From an investor protection standpoint, until a company begins to affect a wider constituency of investors ("widows and orphans"), who may be swindled out of their savings, it is inefficient, if not inappropriate, to expend government resources enforcing most of the securities law disclosure and trading rules.[171] And, from the perspective of the company itself, compliance with the securities laws would impose a great cost. Therefore, generally speaking, transactions in the securities of small companies, or securities offered to sophisticated investors, are deemed "transaction[s] not involving any public offering" and are exempted from the reporting and registration requirements imposed on large corporations and their securities.[172] These are so-called private offerings. In contrast, the federal securities laws are primarily concerned with securities offered by large corporations to the

167. Section 5(c) of the Securities Act of 1933 (the Securities Act) generally prohibits the offer of securities without registration with the SEC. 15 U.S.C. § 77e(c) (2020). Section 4(a)(2) of the Securities Act exempts "transactions by an issuer not involving any public offering" from the registration requirements of Section 5. 15 U.S.C. § 77d(a)(2).

168. *See* H.R. REP. NO. 73–85, at 5–7 (1933) (supporting the distinction of public transactions since the inception of U.S. securities law, stemming from the concept that private transactions do not affect the national economy because they are limited in scope and effect).

169. SEC v. Ralston Purina Co., 346 U.S. 119, 125 (1953) (discussing whether investors can "fend for themselves" in the context of determining whether an offer is public).

170. *See infra* Section II.B.2.a (discussing the definition of Accredited Investors).

171. *See* Pritchard, *supra* note 160, at 1085 (noting that many investors may be able to protect themselves, but that the SEC usually focuses on the stereotypical "widows and orphans" in designing and enforcing protections). As discussed below in Part V.B.1, the basic antifraud rules are an exception to this and apply to purchases and sales of any securities (public or private).

172. *SEC v. Ralston Purina Co.,* 346 U.S. 119, 125–26 (1953) (establishing the criteria for the private offering exemption under Securities Act Section 4(a)(1)).

broader public and traded by members of the public.[173]

Unicorns are, by definition, privately held. It is possible to argue that unicorn investors are privately approached and almost always able to get the information that they need, and so they can fend for themselves.[174] No registration is necessary, but governance may be expected to be informal. Then, when the companies finally access the deeper capital of the public markets, when the risks of their operations begin to impact the public at large, federal securities regulation steps in to require disclosure and other formalities like GAAP financials. A public offering makes companies play by the book. This, the comforting narrative goes, is what happened with WeWork.[175] While it remained private, all sorts of irregularities took place. When it tried to go public, WeWork encountered the "buzz saw" of the equity markets and was forced to reorganize.[176]

Although this story has a certain traditional force, it does not adequately capture what happened at WeWork or, more generally, the reality of the financial markets today. Given their scale and their potential for harm, unicorns clearly need stricter corporate governance. All of the counterarguments rely on the longstanding distinction between public and private companies, and the tacit but no longer valid assumption that private companies are relatively small.[177] As discussed above, the term "unicorn" is

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173. *See* Elisabeth de Fontenay, *The Deregulation of Private Capital and the Decline of the Public Company*, 68 HASTINGS L.J. 445, 453 (2017) (observing that most federal securities regulation targets publicly traded equities and their corporate issuers).

174. The definition is "intended to encompass those persons whose financial sophistication and ability to sustain the risk of loss of investment or ability to fend for themselves render the protections of the Securities Act's registration process unnecessary." Regulation D Revisions; Exemption for Certain Employee Benefit Plans, Securities Act Release No.33-6683, 52 Fed. Reg. 3015, 3017 (Jan. 16, 1987).

175. *See, e.g.,* Fred Wilson, *The Great Public Market Reckoning,* AVC (Sept. 29, 2019) https://avc.com/2019/09/the-great-public-market-reckoning/ [https://perma.cc/3H3K-RX2W] (summarizing the bottom line as "[t]he public markets are a lot different than the private markets"). *But see* Esha Dey *et al.*, *Unprofitable Companies Are Raising the Most IPO Cash Since the Dot-Com Era*, BLOOMBERG (Sept. 27, 2019, 7:00 AM), https://www.bloomberg.com/graphics/2019-unprofitable-ipo-record-uber-wework-peloton/ [https://perma.cc/6Z2H-JEGW] (noting the amount of cash raised in IPOs by unicorns such as Uber, Lyft, and Peloton in 2019).

176. Erin Griffith, *Silicon Valley Is Trying Out a New Mantra: Make a Profit*, N.Y. TIMES (Oct. 8, 2019), https://www.nytimes.com/2019/10/08/technology/silicon-valley-startup-profit.html [https://perma.cc/H22T-M8NN] (identifying the "buzz saw" of Wall Street); *see also* Justin Lahart, *Public Markets Expose the Myth of the Unicorn,* WALL ST. J (May 23, 2019, 12:12 PM), https://www.wsj.com/articles/public-markets-expose-the-myth-of-the-unicorn-11558627761 [https://perma.cc/9AZB-SBS8] (noting problems encountered by Uber, Pinterest, Lyft and WeWork).

177. *See* de Fontenay, *supra* note 173, at 463 (noting an increase in the threshold size at which public company status becomes desirable).

less than a decade old.[178] Today, however, with the advent of enormous private companies, the line between public and private companies is blurry. To make matters worse, relatively recent regulatory and technology changes have substantially weakened the application of the securities laws and, consequently, their ability to ensure responsible corporate governance in unicorns.[179]

2. The Private Placement Exception Has Swallowed the Registration Rule [180]

a. *Reg D/Rule 506/Accredited Investors*

The question of what constitutes "a public offering" requiring registration is central to securities regulation. In order to reduce ambiguity, the SEC has created safe harbor measures that companies can rely on to ensure they do not trigger reporting company obligations with particular offerings. In the unicorn context, the critical safe harbor is Regulation D's Rule 506.[181] Regulation D private placements are popular for good reason. As long as a unicorn abides by its safe harbor rules, the offering will not be deemed public and thereby trigger expensive registration and reporting requirements.[182]

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178. *See* Lee, *supra* note 27 (popularly credited with coining the term).

179. *See* Jones, *supra* note 57, at 170 (describing a class of unaccountable unicorns emerging from the JOBS Act and similar reforms).

180. *See* de Fontenay, *supra* note 173, at 467 (calling the Accredited Investor designation "the exception that swallows the rule").

181. Regulation D was promulgated in 1982. Revision of Certain Exemptions from Registration for Transactions Involving Limited Orders and Sales, Securities Act Release No. 33-6389, 47 Fed. Reg. 11, 251 (Mar. 8, 1982) (to be codified at 17 C.F.R. § 230, 239). It currently includes Rules 504 and 506. Exemptions to Facilitate Intrastate and Regional Securities Offerings, Securities Act Release No. 33-10238, 81 Fed. Reg. 83494 (Nov. 21, 2016) (repealing Rule 505). Rule 504 is of limited utility to unicorns because of the $5 million cap on the amount of securities that can be sold to investors. 17 C.F.R § 230.504 (2019).

182. Companies relying on an exemption from registration of securities under Rule 506 must file a Form D with the SEC within 15 calendar days of the date of the first sale for each new offering of securities. *Form D. Notice of Exempt Offering of Securities*, U.S. SEC. & EXCH. COMM'N, https://www.sec.gov/about/forms/formd.pdf [https://perma.cc/2SGB-YVDU]. However, that document includes only a fraction of the information required of public companies. *See Investor Bulletin: Private Placements under Regulation D,* U.S. SEC. & EXCH. COMM'N, (Sept. 24, 2014) https://www.sec.gov/oiea/investor-alerts-bulletins/ib_privateplacements.html [https://perma.cc/JS32-R9B4] (warning that private placements are not subject to some of the laws and regulations that are designed to protect investors, such as the comprehensive disclosure requirements that apply to registered offerings).

Companies are increasingly doing just that and staying private longer.[183] Start-ups are accessing a historically deep and broad pool of capital with little regulatory scrutiny.[184] Approximately 99.9% of reported private market capital raised since 2009 has relied on Rule 506.[185] WeWork had raised capital eleven times using Rule 506 before it withdrew its registration request in September 2019.[186] Arguably, the lack of accountability imposed by the private financings enabled WeWork to present its financials in a way which one scholar said, "in aggregate, could be considered misleading."[187]

Rule 506 allows a unicorn to raise an unlimited amount of money from an unlimited number of "Accredited Investors"[188] and up to thirty-five other purchasers.[189] As already suggested, the idea behind the Accredited Investor exception is that a person (legal or natural) with the funds and sophistication to assess the risk of an investment, and even sustain the loss if it proves worthless, does not need the full protection of the securities laws.[190] Many

183. *See* discussion in Part I.B (discussing the increasing average time between venture-capital financing and a start-up's decision to go public).

184. *See* Westbrook & Westbrook, *supra* note 72, at 704–17 (discussing the oversight resulting from public company status and the increasing access to capital by non-public companies).

185. SCOTT BAUGUESS ET AL., SEC DIVISION OF ECONOMIC AND RISK ANALYSIS, CAPITAL RAISING IN THE US: AN ANALYSIS OF THE MARKET FOR UNREGISTERED SECURITIES OFFERINGS, 2009-2017, 13 (Aug. 2018), https://www.sec.gov/dera/staff-papers/white-papers/dera_white_paper_regulation_d_082018 [https://perma.cc/52TM-YT8C].

186. We Co., *supra* note 36.

187. *See* Nori Gerardo Lietz, *WeWork – The IPO That Shouldn't?*, HARV. BUS. SCH. WORKING KNOWLEDGE (Sept. 18, 2019) https://hbswk.hbs.edu/item/wework-the-ipo-that-shouldn-t [https://perma.cc/5NZ6-DR49] (noting that WeWork presented the most favorable outcomes, without providing counterbalancing offsets).

188. 17 C.F.R. § 230.501(a) (2019) (as amended, effective October 25, 2020).

189. 17 C.F.R. § 230.506 (2019). Each purchaser who is not an accredited investor must have "such knowledge and experience in financial and business matters that he is capable of evaluating . . . the merits and risks of the prospective investment." 17 C.F.R. § 230.501(i)(iii)(2). In addition, with the passage of the National Securities Markets Improvement Act of 1996 (NSMIA), firms selling unregistered securities under Rule 506 are also exempted from complying with state securities laws. Pub. L. No. 104-290, 110 Stat. 3416 (1996) (codified as amended at 15 U.S.C. § 77r (2020)). *See* Ewens & Joan Farre-Mensa, *The Deregulation of the Private Equity Markets and the Decline in IPOs, supra* note 73, at 2 (showing that after the passage of NSMIA "late-stage startups are more likely to raise capital from out-of-state investors than early-stage startups"); *see also* Linda Gorman, *Regulatory Changes, Private Equity Markets, and the Decline of IPOs*, NAT'L BUR. ECON. RES. DIG., https://www.nber.org/digest/jan20/w26317.shtml [https://perma.cc/4DSA-XTK9] (Jan., 2020) (noting that startups companies' access to capital increased following the passage of NSMIA).

190. *See* William K. Sjostrom, Jr., *Rebalancing Private Placement Regulation,* 36 SEATTLE U. L. REV. 1143, 1158 (2013) (noting the increased proportion of investors that qualify as accredited investors). Restricting these investment opportunities to relatively

entities, including banks, registered broker-dealers, insurance companies, and registered investment companies qualify as Accredited Investors based on their legal status, and other entities may qualify based on their status and their assets.[191] So, Accredited Investors are often institutions such as banks and investment companies, and natural persons with fairly high net worth.[192] Unicorn investors are, in most cases, all Accredited Investors.[193]

b. *Traditional Unicorn Investors: Venture Capital and Hedge Funds*

Some funds (often venture capital funds) that have large, early stakes in unicorns, are made up of relatively few, very wealthy, investors.[194] Following the National Securities Markets Improvement Act (NSMIA) in 1996, which raised the threshold for the number of investors that trigger registration under the Investment Company Act,[195] it became easier for private funds to raise large amounts of money for investment in start-ups.[196] At the end of 2017, global private equity assets under management were estimated at $3.06 trillion.[197] In 2018, hedge fund assets were estimated to

affluent investors may be a poor idea as a policy matter. Arguably, the Accredited Investor limitation contributes to increasing income inequality. *See* Westbrook & Westbrook, *supra* note 72, at 712–15 (discussing securities law's success at opening equity markets beyond the wealthy).

191. Amending the "Accredited Investor" Definition, Proposed Rule, Securities Act Release No. 33-10738, 85 Fed. Reg. 2332 (proposed Jan. 15, 2020). The rule was amended in August 2020. Amending the "Accredited Investor" Definition, Final Rule, Sec. Act Rel. No. 33-10824; 34-89669 Fed. Reg. 2332 (Aug. 26, 2020).

192. 17 C.F.R. § 230.501(a). If an issuer does not satisfy the Regulation D requirements, an exemption from registration may still be available under Section 4(a)(2) (a transaction not involving a public offering), but the uncertainty of that exemption may discourage the issuer.

193. *See* Tara Siegel Bernard, *Opening the Door to Unicorns Invites Risk for Average Investors*, N.Y. TIMES (Jan. 4, 2020), https://www.nytimes.com/2020/01/04/your-money/investing-private-market-startups.html [https://perma.cc/66GJ-4VR4] (noting that the SEC's proposal to expand the Accredited Investor definition would enable more persons to invest in unicorns).

194. *See Unicorn Hunters: These Investors Have Backed the Most Billion-Dollar Companies*, CB INSIGHTS (May 7, 2019), https://www.cbinsights.com/research/best-venture-capital-unicorn-spotters-2/ [https://perma.cc/NYR4-NSL4] (cataloging the unicorn investments of exclusive hedge funds and venture capital funds such as Tiger Global Management and Sequoia Capital).

195. Investment Company Act 15 U.S.C. § 80a-3(c)(7).

196. NSMIA removed the 100-investor cap in private placement funds, which triggered the creation of mega private equity funds. *See* Ewens & Joan Farre-Mensa, *supra* note 73, at 2 (showing that, after NSMIA, "late-stage startups' ability to raise large funding rounds increases more than that of their early-stage counterparts").

197. *See* James Comtois, *Preqin: Private Equity AUM Grows 20% in 2017 to Record*

be at $3.22 trillion.[198] These funds have a great deal of money to invest. In 2018, venture capital deal value reached a record $140.2 billion (invested in 10,542 deals), and 2019 was not far behind with $136.5 billion invested in 10,777 deals.[199]

Such private funds fairly embody the animating conception of the Accredited Investor, an actor with the sophistication and clout to get good information, negotiate reasonable deals, and weather the occasional loss, even if substantial. Such funds are run by sophisticated managers and have the capacity to negotiate and impact the behavior of the unicorn companies.[200] They may hold preferred shares and negotiate for seats on the board of directors.[201] For example, it was SoftBank that ultimately pushed out Adam Neumann.[202] Venture capital investor Benchmark Capital helped remove Travis Kalanick from Uber in 2017.[203] Even for such funds, however, better corporate governance would help. Direct investor involvement in the corporate governance of companies often comes after heavy losses.[204]

$3.06 Trillion, PENSIONS & INV. (July 24, 2018, 1:33 PM), https://www.pionline.com/article/20180724/ONLINE/180729930/preqin-private-equity-aum-grows-20-in-2017-to-record-306-trillion [https://perma.cc/8AM5-JCXK] (pointing out that the record high was also the result of the highest annual growth rate recorded by the financial data company Preqin).

198. *See* Amanda Cantrell, *Hedge Fund Assets Hit Record High*, INSTITUTIONAL INV. (Apr. 19, 2018), https://www.institutionalinvestor.com/article/b17v773lkvph3y/hedge-fund-assets-hit-record-high [https://perma.cc/QCB3-CN4U] (noting the growth despite recent challenges for hedge funds).

199. NAT. VENTURE CAP. ASS'N, *supra* note 146.

200. Funds may also be subject to moral hazard because of "IPO ratchet" provisions, which entitle them to additional shares if the IPO prices below the valuation reflected in the final private-equity round. Using such provisions, even relatively passive mutual fund investors are protected from down rounds, at the expense of other (then-diluted) shareholders. *See* John C. Coffee, Jr., *Toxic Unicorns: What Has Been Missed About WeWork's Fiasco*, THE CLS BLUE SKY BLOG (Nov. 6, 2019) (noting that the WeWork prospectus buried disclosure of an IPO ratchet).

201. The National Venture Capital Association's Model Investors' Rights Agreement, for example, requires companies to provide their "major investors" with regular financial statements, budgets, and business plans. NAT. VENTURE CAP. ASS'N, *Investor Rights Agreements*, MODEL LEGAL DOCUMENTS, 5–8, n.7, http://nvca.org/resources/model-legal-documents/ [https://perma.cc/Y7Q7-A3Q3] (last updated Sept., 2020).

202. Farrell & Brown, *supra* note 26.

203. Greg Bensinger & Maureen Farrell, *How Uber Backers Orchestrated Kalanick's Ouster as CEO*, WALL ST. J. (June 21, 2017) https://www.wsj.com/articles/how-uber-backers-orchestrated-kalanicks-ouster-as-ceo-1498090688?mod=article_inline&mod=article_inline [https://perma.cc/J6HG-T2MB].

204. *See supra* Part II (discussing SoftBank losses in WeWork). Unicorn founders often prefer venture capital investors who promise not to interfere or question their decisions. *See* Duhigg, *supra* note 16 (discussing venture capital firms that claim to be "founder friendly" and relatively hands-off).

c. More Unicorn Investors: Direct and Indirect

In the current market, unicorn investors include more than just the venture capital funds often found in the technology sector. There are also less active investors,[205] such as corporate venture capital funds,[206] sovereign wealth funds, and mutual funds.[207]

Given the current levels[208] of participation in the financial markets, much of which is through institutional arrangements and retirement plans,[209] the idea that public investors are not impacted by unicorn irregularities and losses may no longer be accurate. Institutional investors, which aggregate the investments of many smaller investors, accounted for 8% of equity ownership in 1950, and as much as 80% in 2017.[210] Studies estimate that household equity holdings as a share of disposable income in 2019 were three times larger than they were in the 1980s.[211]

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205. *See* Jones, *supra* note 57, at 173 (noting angel investors are another source of less active capital). It is also worth noting that the array of investors includes some individual angel investors, but they are outnumbered by the institutional investors. *Id*; *see also*, Ryan Feit, *Searching for the Unicorn Investor*, INC. (May 5, 2015) https://www.inc.com/ryan-feit/searching-for-the-unicorn-investor.html [https://perma.cc/U2FP-Z4ER] (stating that one of the main reasons companies raise capital online is to combine value-add angel investors with larger, institutional investors such as venture funds).

206. For a fuller discussion of corporate venture capital, *see* Jennifer S. Fan, *Catching Disruption: Regulating Corporate Venture Capital*, 2018 COLUM. BUS. L. REV. 341 (2018) (noting that corporate venture capital has become a powerful force in the field of venture capital).

207. For a discussion of the problems posed by mutual fund investment in startups, *see* Jeff Schwartz, *Should Mutual Funds Invest in Startups? A Case Study of Fidelity Magellan Fund's Investments in Unicorns (and Other Startups) and the Regulatory Implications*, 95 N.C. L. REV. 1341 (2017) (noting in particular the lack of awareness of and information for mutual fund investors, and valuation issues).

208. *See generally* WILLIAM A. BIRDTHISTLE, EMPIRE OF THE FUND: THE WAY WE SAVE NOW (2016) (describing the rise of investment management).

209. *See* Michael Sheetz, *More Americans Than Ever Own Stocks, Potentially Giving the Market a Bigger Wealth Effect,* CNBC (Jan. 16, 2019), https://www.cnbc.com/2019/01/16/more-americans-than-ever-own-stocks-potentially-giving-the-market-a-bigger-wealth-effect.html [https://perma.cc/R4NS-VR4U] (noting, however, that the wealthiest 1% still own half of all total household equities).

210. *See* Olufunmilayo B. Arewa, *Investment Funds, Inequality, and Scarcity of Opportunity*, 99 B.U. L. REV. 1001, 1014 (2019) (describing institutional investors as a powerful force in global financial markets).

211. *See* Quentin Fottrell, *One Reason Why the Stock Market's Wild Fluctuations Don't Faze Most Americans,* MARKETWATCH (Feb. 12, 2019), https://www.marketwatch.com/story/americas-super-wealthy-own-more-stocks-leaving-average-people-in-the-dust-2019-01-28 [https://perma.cc/25KY-Y5KF] (noting that more wealthy Americans own stocks than four decades ago, though millions have no stake in the markets); *see also* Sheetz, *supra* note 209 (citing a study by a Goldman Sachs senior economist).

The funds in which many ordinary Americans have interests through their retirement accounts or college savings accounts are the Accredited Investors that may purchase stakes in unicorns.[212] Non-Accredited Investors can purchase shares in a mutual fund formed to invest in private companies.[213] In fact, all of the major fund groups have funds focused on private companies.[214] "Widows and orphans" *are* invested in nominally private markets, they are just invested indirectly.[215]

This indirect investment may be particularly risky. As mentioned above, the funds may not be active investors. The defining characteristic of the largest investment funds, so-called "index funds," is that they spend few resources on monitoring and interfering in the corporate governance of their investment.[216] They are structured to be big, diversified, and above all, passive.[217] Their lack of personnel and active management keeps overhead and fees low, which is good for investors.[218] As a matter of corporate governance, however, these funds are generally along for the ride. Thus, index funds and their investors are both enablers and victims of bad corporate

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212. *See* Andrew Ross Sorkin, *Main Street Portfolios Are Investing in Unicorns*, N.Y. TIMES (May 11, 2015), https://www.nytimes.com/2015/05/12/business/dealbook/main-street-portfolios-are-investing-in-unicorns.html [https://perma.cc/Z8L9-9ZVN].

213. de Fontenay, *supra* note 173, at 471.

214. *See* Dawn Lim, *Vanguard Broadens Reach with Entry into Private Equity,* WALL ST. J. (Feb. 5, 2020) (announcing Vanguard's launch of a private equity fund, which will be offered at first only to endowments, foundations, and other institutions). Another example is the SharesPost 100 Fund, which invests in a variety of late-stage private growth companies unicorns. *See* SHARESPOST 100 FUND, ANNUAL REPORT (2018), *available at* https://sharespost.com/downloads/SharesPost_100_Fund_2018_Annual_Report.pdf [https://perma.cc/296G-4M6C] (last visited Nov. 21, 2020).

215. *See* Troy Wolverton, *WeWork's meltdown was supposed to leave everyday investors unharmed. It didn't, and you probably don't even realize if your 401(k) took a WeWork hit*, BUS. INSIDER (Dec. 11, 2019) https://www.businessinsider.com/mutual-fund-investments-in-startups-wework-pose-risks-average-investors-2019-12?IR=T [https://perma.cc/U95Y-8X4L] (discussing the opportunities and dangers for retail investors who are economically exposed unicorns like WeWork through mutual fund investments).

216. *See* David McLaughlin and Annie Massa, *Index Fund Takeover Makes 'Big Three' into Corporate Overlords,* BLOOMBERG L. (Jan. 9, 2020, 1:40 PM), https://www.bloomberglaw.com/document/XCBDC45S000000?bna_news_filter=banking-law&jcsearch=BNA%25200000016f8a8cd182a77fdfdf045d0000#jcite [https://perma.cc/8W2G-7W74] (noting that on average, Blackrock, Vanguard, and State Street own 22% of the typical S&P 500 company).

217. Jones, *supra* note 57, at 173–74 (noting overall passivity of all unicorn investors, including not just mutual funds but angel investors, sovereign wealth funds, corporate venture capital arms, and even, given the competition to fund start-ups, traditional venture capitalists).

218. *See* Michael Regan, *Q&A with Jack Bogle: "We're in the Middle of a Revolution,"* BLOOMBERG MKTS (Nov. 23, 2016), https://www.bloomberg.com/features/2016-jack-bogle-interview [https://perma.cc/4R5Y-HEYV] (discussing the merits of passive investing).

governance.

In addition to the Softbank Vision Fund, WeWork investors included venture capital firms (Benchmark, DAG Ventures), private equity funds (Hony Capital), investment funds (T. Rowe Price), and prominent investment banks (JP Morgan Chase, Goldman Sachs), as well as wealthy individuals (Mortimer Zuckerman).[219] The idea that "public" investors are not impacted by investments in "private" companies is simply inaccurate.

d. Even More Unicorn Investors: More Accredited Investors

Although the bulk of investment in unicorns is by funds, there are also individuals. These include so-called angel investors and other high net-worth individuals. WeWork investors included, for example, billionaire Mortimer Zuckerman,[220] former chairman of Boston Properties and owner of the *New York Daily News*.[221]

In addition, individual Accredited Investors are now much more common, although hardly democratically representative. In 2019, 13% of U.S. households qualified as Accredited Investors, up from approximately 2% in 1983.[222] In August, 2020, the SEC expanded the Accredited Investor pool to include more individuals with demonstrated financial sophistication.[223] The changes are intended to expand "investment opportunities while maintaining appropriate investor protections and

219. *See* Farrell & Brown, *supra* note 26 (listing a number of We Co. investors); Alex Konrad, *Inside the Phenomenal Rise of WeWork,* FORBES (Nov. 24, 2014), https://www.forbes.com/sites/alexkonrad/2014/11/05/the-rise-of-wework/#493d1b456f8b [https://perma.cc/M8JU-EGP4] (reviewing the history of WeWork).

220. Konrad, *supra* note 219.

221. *#327 Mortimer Zuckerman*, FORBES, https://www.forbes.com/profile/mortimer-zuckerman/#22c4e7c2445b [https://perma.cc/8UXB-PC27] (assigning him a real-time net worth of $2.68 billion as of November 21, 2020) (last visited Nov. 21, 2020).

222. Amending the "Accredited Investor" Definition, 85 Fed. Reg. 2574 (proposed Jan. 15, 2020) (proposing to add new categories of natural persons that may qualify as Accredited Investors based on their professional knowledge, experience, or certifications, and expanding the list of entities that may qualify by allowing any entity that meets an investments test to qualify).

223. *Id.*; Amending the "Accredited Investor" Definition, *supra* note 191; *see also* Concept Release on Harmonization of Securities Offering Exemptions, 84 Fed. Reg. 30460 (proposed June 26, 2019) (soliciting comments on exemptions from registration under the Securities Act of 1933 that enable capital raising). *But see* Securities and Exchange Commission, Statement on the Proposed Expansion of the Accredited Investor Definition (Dec. 18, 2019), https://www.sec.gov/news/public-statement/statement-lee-2019-12-18-accredited-investor#_ftn18 [https://perma.cc/8ZTF-Y3DJ] (objecting to certain aspects of the expansion).

promoting capital formation."[224]

e. Unicorns May Market Shares Using General Advertising

The 2012 Jumpstart Our Business Startups Act (the JOBS Act) was passed to encourage IPOs,[225] but may simultaneously have made it easier for some companies to avoid going public.[226] For one thing, the JOBS Act loosened the general solicitation and advertising rules that had prevented non-public companies from using the internet to seek purchasers for their securities when pursuing an exempt offering under Rule 506.[227] Under the JOBS Act, the SEC adopted Rule 506(c),[228] which allows issuers under Rule 506 to engage in general solicitation as long as the securities are sold only to Accredited Investors.[229] This change has created a wider audience for capital formation efforts by start-ups.[230] The idea makes sense when thinking about small start-ups, but it also enables large private companies to continue raising funds without submitting to the financial disclosure and governance requirements that the public markets would impose.[231]

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224. Press Release, Sec. & Exch. Comm'n, SEC Modernizes the Accredited Investor Definition (Aug. 26, 2020) https://www.sec.gov/news/press-release/2020-191 [https://perma.cc/9PZC-PBLT].

225. Jumpstart Our Business Startups Act, Pub. L. No. 112-106, 126 Stat. 306 (2012) ("An Act [t]o increase American job creation and economic growth by improving access to the public capital markets for emerging growth companies").

226. *See* de Fontenay, *supra* note 173, at 456 (claiming that "the JOBS Act simultaneously liberalized private capital raising . . . rendered nugatory the Act's efforts to encourage IPOs").

227. 17 C.F.R. § 230.506 (2013). As Regulation D existed before 2013, a sale of securities that sought the Rule 506 exemption from registration could not use general solicitation or general advertising to find potential investors. 7 C.F.R. § 230.502(c) (2013). The revisions to Rule 506(c), however, eliminated that restriction for Rule 506 offerings. Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings 78 Fed. Reg. 44771 (July 24, 2013).

228. *See* JAMES D. COX ET AL., SECURITIES REGULATION: CASES AND MATERIALS 277–79 (8th ed. 2017) (noting that the SEC was reluctant to make the change but was required to do so by Congress).

229. 17 C.F.R. § 230.502(c)(1) (2017). The company is simply required to take reasonable steps to verify that purchasers are accredited investors. *Id.* The revised rule also provided four non-exclusive ways an issuer can meet the "reasonable steps to verify" requirement. *See* Michael L. Hermsen, *SEC Eliminates General Solicitation and General Advertising Prohibitions from Certain Private Offerings*, MAYER BROWN (July 17, 2013), https://www.mayerbrown.com/en/perspectives-events/publications/2013/07/sec-eliminates-general-solicitation-and-general-ad [https://perma.cc/3EAN-8SP5] (discussing the adoption of rule 506).

230. Darian M. Ibrahim, *Equity Crowdfunding: A Market for Lemons*?, 100 MINN. L. REV. 561, 585–86 (2015) (explaining the benefits of Title II such as reduction of transaction costs and addition of passive investors).

231. WeWork's submission of a confidential Form S-1 on December 31, 2018 relied on

The JOBS Act also expanded Regulation A to create a crowdfunding exemption known as "Reg A+," pursuant to which a private company can sell up to $20 million (Tier 1) or $50 million (Tier 2) of equity securities to the general public in a 12-month period with much less burdensome disclosure requirements and fees (a kind of "mini-IPO").[232] A Tier 2 Regulation A offering imposes more obligations on the issuer, including the provision of audited financial statements and reporting requirements,[233] and the investors who do not qualify as Accredited Investors are limited to investing no more than 10% of their annual income or net worth.[234] Nevertheless, the expanded exemption provides another opportunity for companies to raise substantial amounts of capital without going public.

f. Unicorn Securities May Be Freely Resold after a Year

Traditionally, one of the major reasons to go public has been to create a liquid secondary market. Securities law restricts resales of private company securities for which public information is not available. In the 1970s, the SEC created a safe harbor provision that allows secondary market sales of securities of private companies after a certain holding period under Rule 144.[235] In 2007, however, the SEC reduced that holding period,[236] and

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its status as an emerging growth company under the JOBS Act (as amended by the FAST Act) because in the prior fiscal year (2017), its revenues were still less than $1.7 billion. To take advantage of those reduced disclosure requirements, WeWork submitted the confidential Form S-1, but that started the clock ticking on a one-year period during which the company had to consummate the IPO. Many commentators feel that the deadline contributed to WeWork's anxiety to get the offering done in 2019. *See, e.g.,* Elie Finegold, *WeWork IPO Part II: Here to Represent the EGC*, LINKEDIN (Sept. 6, 2019), https://www.linkedin.com/pulse/wework-ipo-part-ii-here-represent-egc-elie-finegold [https://perma.cc/GQ7L-9RCJ] (explaining the requirements for emerging growth companies under the JOBS Act); Lauren Silva Laughlin, *Adam Neumann's Ouster Won't Change WeWork Equation*, WALL ST. J. (Sept. 24, 2019, 2:20 PM), https://www.wsj.com/articles/adam-neumanns-ouster-wouldnt-change-wework-equation-11569342629 [https://perma.cc/YA5L-KFNW] (explaining that the company had to list before the end of 2019 or it would lose its status as an emerging growth company).

232. 17 C.F.R. §§ 230.251-230.263 (2019).

233. 17 C.F.R. § 230.257 (2019).

234. 17 C.F.R. § 230.251(d)(2)(C) (2019).

235. *See* Definition of the Terms "Underwriter" and "Brokers' Transactions," Securities Act Release No. 33-5223, 37 Fed. Reg. 591 (Jan. 14, 1972) (describing the newly adopted Rule 144 and how it relates to the application of registration provisions to the resale of securities).

236. *See* Revisions to Rules 144 and 145, Securities Act Release No. 33-8869, 72 Fed. Reg. 71,546 (Dec. 17, 2007) (codified at 17 C.F.R. § 230.144, Persons Deemed Not to Be Engaged in a Distribution and Therefore Not Underwriters (2018)). For public (reporting) companies, the holding period is only six months, with conditions on resale during the period

currently an investor holding stock in a private company can resell that stock with minimal conditions after twelve months.[237] And finding a secondary market buyer for one's private company securities is easier than ever.[238] For Rule 144 resales, investors can look to online platforms like SharesPost,[239] NASDAQ Private Market,[240] Forge Capital,[241] and EquityZen.[242]

In addition to Rule 144, Rule 144A allows immediate resales of certain restricted (private company) securities to Qualified Institutional Buyers (QIBs).[243] QIBs tend to be large firms, often insurance companies, investment companies, or banks, that in the aggregate own and invest on a discretionary basis at least $100 million in securities of issuers that are not affiliated with the entity.[244] Rule 144A, which was amended by the JOBS Act to remove restrictions on general solicitation and advertising,[245] also

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between six months to one year from acquisition. For non-reporting companies, the holding period is one year and, if the resale is effected by a person who is not an affiliate of the issuer, there are no information requirements after the expiration of the year. *See* CHOI & PRITCHARD, *supra* note 164, at 797 (showing resale requirements in a tabular format).

237. *See* CHOI & PRITCHARD, *supra* note 164, at 797 (showing resale requirements in a tabular format).

238. With multiple platform options, over $4 billion in transaction volume was executed in 2017. *See* David F. Larker et al., *Cashing It In: Private-Company Exchanges and Employee Stock Sales Prior to IPO*, HARV. L. SCH. F. CORP. GOVERNANCE (Oct. 9, 2018), https://corpgov.law.harvard.edu/2018/10/09/cashing-it-in-private-company-exchanges-and-employee-stock-sales-prior-to-ipo/ [https://perma.cc/AYY7-GYF7] (analyzing transactions on SharesPost, Equidate (now Forge Capital), EquityZen, and Nasdaq Private Market).

239. *See* SHARESPOST, https://sharespost.com [https://perma.cc/3YUX-K7H8] (last visited Nov. 21, 2020) (advertising services for institutional investors, individual investors, selling shareholders and companies).

240. *See Streamline your Liquidity Management with Nasdaq Private Market*, NASDAQ, https://www.nasdaq.com/solutions/nasdaq-private-market [https://perma.cc/F997-VSZV] (last visited Nov. 16, 2020) (advertising company provided solutions for private companies and funds). The platform announced a new transaction record in the first half of 2019, completing 36 private company-led transactions at a $2.3 billion transaction value. *Nasdaq Private Market Sets New Transaction Record in the First Half of 2019*, GLOBENEWSWIRE (July 23, 2019, 10:05 ET), https://www.globenewswire.com/news-release/2019/07/23/1886533/0/en/Nasdaq-Private-Market-Sets-New-Transaction-Record-in-the-First-Half-of-2019.html [https://perma.cc/B5PW-E6CV].

241. *See* FORGE, https://forgeglobal.com [https://perma.cc/F8UQ-Z342] (last visited Nov. 16, 2020) (claiming $3.2 billion in recorded transaction volume since inception).

242. *See* EQUITYZEN, https://equityzen.com [https://perma.cc/D9TR-PW4Y] (last visited Nov. 16, 2020) (calling itself the "marketplace for pre-IPO equity").

243. *See* 17 C.F.R. § 230.144A (2013). Note that the JOBS Act changes also included removal of the restrictions on general solicitation and advertising in the context of Rule 144A resales.

244. *See* 17 C.F.R. § 230.144A(a)(1) (2013) (describing qualified institutional buyers).

245. *See* Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings, Securities Act Release No. 9415, 78 Fed. Reg. 44,771 (July 24, 2013) (allowing securities to be offered to persons other than qualified institutional

makes the markets for privately placed securities more liquid.[246] Overall, Accredited Investors, including QIBs, can purchase and resell unicorn and other private company securities more easily than ever.[247] Under these rules, for many participants, private markets offer liquidity that once required public offerings.

g. *Unicorns May Have Up to 2000 Shareholders*

Even for private companies with many shareholders, the need to go public due to dispersed ownership of the companies' securities has been reduced.[248] The JOBS Act also amended Section 12(g) of the Exchange Act to increase the number of shareholders that triggers registration: private companies can have up to 2000 shareholders, including up to 500 non-Accredited Investors.[249] The previous (500 total shareholder) threshold[250] is reportedly what drove former unicorns Google and Facebook to make IPOs.[251] That threshold is reached much later now, if at all. Some estimated

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buyers).

246. *See* Dan Caplinger, *How Rule 144A Created a Shadow Financial Market*, NASDAQ (July 3, 2015, 12:00 PM), https://www.nasdaq.com/articles/how-rule-144a-created-shadow-financial-market-2015-07-03 [https://perma.cc/Z34D-AMQ2] ("Rule 144A has made the markets for privately placed restricted securities more liquid than they would otherwise be" by allowing shorter-term investment in securities.). Resales of Rule 144A securities are eligible for Depository Trust Company clearance and settlement, with issuers and participants responsible for determining that the securities laws are observed. *See* Order Approving a Proposed Rule Change Relating to Eliminating the SRO Requirement as a Condition of DTC-Eligibility for Securities that are Eligible for Resale Under Rule 144A Under the Securities Act of 1933, Exchange Act Release No. 59384, 74 Fed. Reg. 7941 (Feb. 20, 2009).

247. *But see* Publication or Submission of Quotations Without Specified Information, Exchange Act Release No. 87115, 84 Fed. Reg. 58206 (proposed Oct. 30, 2019) (proposing an increase in the requirements for information provided to investors).

248. *See* Michael J. Zeidel, *The JOBS Act: Did It Accomplish Its Goals?* HARV. L. SCH. F. CORP. GOVERNANCE (Jul. 18, 2016), https://corpgov.law.harvard.edu/2016/07/18/the-jobs-act-did-it-accomplish-its-goals/ [https://perma.cc/68UR-Q3HC] (characterizing this as "providing [private] companies with more flexibility in timing their IPOs" as a result of the number of shareholders).

249. 17 C.F.R. § 240.12g-1 (2016).

250. *See* Elizabeth Pollman, *Information Issues on Wall Street 2.0*, 161 U. PA. L. REV. 179, 192 (2012).

251. Dan Primack, *Killing the 500-Shareholder Rule*, FORTUNE (Nov. 8, 2011), https://fortune.com/2011/11/08/killing-the-500-shareholder-rule/ [https://perma.cc/3UZM-Z4MJ] (discussing introduction of legislation to raise the limit); Letter from Darrell Issa, Chairman, House Comm. on Oversight & Gov't Reform, to the Hon. Mary L. Schapiro, Chairman, U.S. Sec. & Exch. Comm'n (Mar. 22, 2011), *available at* http://www.knowledgemosaic.com/resourcecenter/Issa.041211.pdf [https://perma.cc/2D4P-SK64] (arguing for the raised threshold). The JOBS Act was passed soon after Facebook's IPO, and many scholars feel that Mark Zuckerberg's complaints contributed directly to the raised threshold. de Fontenay, *supra* note

that when the JOBS Act was passed, more than two-thirds of *public* companies were beneath the 2000 shareholder cap.[252]

h. Cumulative Result

The cumulative result of these regulatory and market developments is a dramatic increase in more passive investment in large private startups. Deregulatory measures have relieved pressure on unicorns to pursue an IPO.[253] Consequently, long-term and often large-scale private companies have no need to establish the governance mechanisms or provide the investor protection through information that securities law requires of public companies.[254] Companies can remain in "stealth mode"[255] long after they achieve a size and scope that may pose a threat to an increasingly large number of investors.

III. MANY STAKEHOLDERS ARE HARMED

A. Corporations Serve the Interests of Stakeholders Other Than Shareholders

It is not only investors who may be harmed by unicorns with poor corporate governance. All corporations, including unicorns, serve the interests of a variety of stakeholders. Given their size and, therefore, their potential impact, unicorns need accountable corporate governance to protect the array of persons, both legal and natural, connected to them. They are big enough to generate substantial negative externalities in the event of a meltdown and are operating in largely unregulated spaces that enable them to bypass most of our legal mechanisms to ensure good governance.

173, at 460.

252. John Coates & Robert Pozen, *Bill to Help Businesses Raise Capital Goes Too Far*, WASH. POST (Mar. 14, 2012), https://www.washingtonpost.com/opinions/bill-to-help-businesses-raise-capital-goes-too-far/2012/03/13/gIQAVWgFCS_story.html [https://perma.cc/DUT8-P5JZ] (arguing against the change).

253. Sjostrom, Jr., *supra* note 190, at 1153 (discussing ways in which the JOBS Act would enable companies to remain private).

254. *See* Jones, *supra* note 57, at 179–182 (noting that unicorn investors may not receive the kind of information they would get from a public company, and that "[b]ecause unicorns are free from public disclosure requirements, they can engage in questionable activities with less fear of exposure").

255. Matt Villano, *Why Startups Launch in 'Stealth Mode' and Others Don't*, ENTREPRENEUR (Oct. 17, 2013), http://www.entrepreneur.com/article/229461 [https://perma.cc/29X9-WCTD] (explaining the pros and cons of the practice).

Unicorns provide extreme examples of the need for stakeholder (not just shareholder or investor) protection.

For many decades, depending on whether one measures from the 1919 *Dodge v. Ford* decision requiring Henry Ford pay a special dividend to the company shareholders,[256] or from economist Milton Friedman's writing in the 1960s and 70s,[257] shareholder primacy has been a dominant way to understand corporate decision-making and governance. In this view, the corporation is to be run primarily for the benefit of the stockholders – the owners of the business.[258] As Friedman expressed it: "there is one and only one social responsibility of business – to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game . . . ."[259] Other incidental benefits are permissible,[260] but the fundamental objective and basis for corporate decision-making is clear. As the Business Roundtable put it in its 1997 statement on corporate governance: "[t]he paramount duty of management and of boards of directors is to the corporation's stockholders; the interests of other stakeholders are relevant as a derivative of the duty to stockholders."[261] This understanding was dominant for so long, in fact, that in 2000, Professors Reiner Kraakman and Henry Hansmann argued for the "end of history" for corporate law.[262] Kraakman and Hansmann asserted that "[t]here is no longer any serious competitor to the view that corporate law should principally strive to increase long-term shareholder value."[263]

There have always been other views. Corporations began as instrumentalities of the state[264] and require state government action to come

256. Dodge v. Ford Motor Co. 204 Mich. 459, 507 (1919) (holding that a "business corporation is organized and carried on primarily for the profit of the stockholders").

257. MILTON FRIEDMAN, CAPITALISM AND FREEDOM (1962); Milton Friedman, *The Social Responsibility of Business Is to Increase Its Profits,* N.Y. TIMES MAG. (Sept. 13, 1970), *available at* http://umich.edu/~thecore/doc/Friedman.pdf [https://perma.cc/L2SV-X9ET].

258. *See* John H. Matheson & Vilena Nicolet, *Shareholder Democracy and Special Interest Governance*, 103 MINN. L. REV. 1649, 1653 (2019) (noting that the "traditional shareholder primacy model of a corporation derives from the concept that the shareholders are the owners of the corporation").

259. FRIEDMAN, *supra* note 257, at 112.

260. Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc. 506 A. 2d 173, 182 (Del. 1986) (holding that the board can consider the interests of other constituencies only if there are rationally related benefits accruing to the shareholders).

261. THE BUSINESS ROUNDTABLE, STATEMENT ON CORPORATE GOVERNANCE 3 (Sept. 1997), *available at* http://www.ralphgomory.com/wp-content/uploads/2018/05/Business-Roundtable-1997.pdf [https://perma.cc/XN2K-NLS9].

262. Henry Hansmann & Reiner Kraakman, *The End of History for Corporate Law*, 89 GEO. L.J. 439 (2000).

263. *Id.*

264. Trs. of Dartmouth Coll. v. Woodward, 17 U.S. 518, 636 (1819) (holding that the

into existence.[265] Moreover, corporations are important actors in society, fulfilling a multitude of social roles. In the 1930s, two prominent corporate law experts, Adolph Berle and Merrick Dodd debated corporate purpose in the *Harvard Law Review*. Professor Berle took the side of shareholder primacy,[266] and Professor Dodd argued that a corporation's purpose is broader and includes benefits for employees, consumers, and society itself.[267]

At present, such broader views of the corporation's responsibility are gaining strength. And these broader views are particularly persuasive in the unicorn context.

B. Contemporary Debate Regarding Stakeholders

1. Emphasis on Stakeholders

An exclusive focus on the well-being of shareholders hardly captures the impact that our largest companies, regardless of whether their capital structure is public or private, have on the world. Profits (and executive salaries) are skyrocketing, along with income and wealth inequality.[268] Environmental and social concerns of various types are mounting, and the varied obligations of business corporations are increasingly recognized.[269] In

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Contract Clause prohibits states from violating contracts with private or public corporations).

265. To form a corporation, the incorporations file articles of incorporation (also known as a certificate of incorporation) with the secretary of state in the state of incorporation. Those documents must be accepted by the state, and the corporation must remain in compliance with state statutes and regulations in order to continue in existence. *See* David M. Steingold, *Steps in Articles of Incorporation*, NOLO, https://www.nolo.com/legal-encyclopedia/articles-incorporation.html [https://perma.cc/4J56-5VM8] (last visited Nov. 21, 2020) (discussing the general requirements of articles of incorporation).

266. Adolf A. Berle, *Corporate Powers as Powers in Trust*, 44 HARV. L. REV. 1049, 1049 (1931) (arguing management powers should be exercised for the "ratable benefit of all the shareholders.").

267. E. Merrick Dodd Jr., *For Whom Are Our Corporate Managers Trustees*, 45 HARV. L. REV. 1145, 1148 (1932) (arguing that corporations should have "a social service as well as a profit-making function . . .").

268. *See* Michael Batty *et al*., *Introducing the Distributional Financial Accounts of the United States, Finance and Economics Discussion Series,* U.S. FEDERAL RESERVE BOARD OF GOVERNORS, 26 (2019), *available at* https://www.federalreserve.gov/econres/feds/files/2019017pap.pdf [https://perma.cc/W3WE-DPFF] (pointing out that persons in the top 10% of the wealth distribution in the United States hold a large and growing share of U.S. wealth, while the bottom half hold substantially less).

269. *See, e.g.,* LYNN STOUT, THE SHAREHOLDER VALUE MYTH (2012); *see also* Todd H. Baker, *Shareholder Primacy Isn't the Best of All Possible Worlds*, CLS BLUE SKY BLOG (Oct. 23, 2019), *available at* https://clsbluesky.law.columbia.edu/2019/10/23/shareholder-primacy-isnt-the-best-of-all-possible-worlds/ [https://perma.cc/BY2Y-2CFR] (suggesting that shareholder primacy contributed to the rapid growth of income and wealth inequality in the

2019, as the WeWork IPO unraveled and the Uber and Lyft IPOs disappointed,[270] significant players in the corporate world were talking, once again, about the appropriate roles of the business firm.

In his 2018 letter to the chief executives of major corporations, Larry Fink, CEO of Blackrock, stated, "Society is demanding that companies, both public and private, serve a social purpose."[271] Martin Lipton, one of the founders of a preeminent New York corporate law firm, described a "New Paradigm."[272] Lipton argued that shareholder profit is a byproduct of a well-functioning corporate governance regime, not its sole objective, and that governments charter corporations to promote the economy and increase opportunity for society at large, not just to make money for shareholders.[273]

In August 2019, the Business Roundtable revised its 1997 statement of the purpose of the corporation.[274] The new statement did not mention shareholders until over 80% of the way through,[275] and then only in the context of "long-term"[276] value and a commitment to transparency and effective engagement. The statement, signed by 181 CEOs, focused on

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United States); Andrew Ross Sorkin, *How Shareholder Democracy Failed the People,* N.Y. TIMES DEALBOOK, (Aug. 20, 2019) https://www.nytimes.com/2019/08/20/business/dealbook/business-roundtable-corporate-responsibility.html [https://perma.cc/PXH4-9RGR] (arguing that the adoption of Friedman's shareholder primacy argument brought with it increased layoffs, decreased research and development budgets, and the substitution of 401(k)s for pension programs).

270. Maureen Farrell, *2019: The Year of IPO Disappointment*, WALL ST. J. (Dec. 29, 2019), https://www.wsj.com/articles/2019-the-year-of-ipo-disappointment-11577615400 [https://perma.cc/4RXG-J597] (noting investor "wariness" of the Uber and Lyft IPOs).

271. Larry Fink, *Larry Fink's 2018 Letter to CEOS A Sense of Purpose*, BLACKROCK (2018), https://www.blackrock.com/corporate/investor-relations/2018-larry-fink-ceo-letter [https://perma.cc/6ZCJ-YLGU].

272. Martin Lipton, *It's Time to Adopt the New Paradigm*, HARV. L. SCH. F. CORP. GOVERNANCE (Feb. 11, 2019), https://corpgov.law.harvard.edu/2019/02/11/its-time-to-adopt-the-new-paradigm/ (based on his 2017 memorandum, *Corporate Governance: The New Paradigm,* available through the University of Pennsylvania Delaware Corporation Law Research Center, *available at* https://www.law.upenn.edu/live/files/7876-culled-martin-lipton-publicationspdf [https://perma.cc/94D9-P5EG] (last visited Nov. 21, 2020).

273. *Id.*

274. *See* BUSINESS ROUNDTABLE, STATEMENT ON THE PURPOSE OF A CORPORATION (August 2019) https://www.businessroundtable.org/business-roundtable-redefines-the-purpose-of-a-corporation-to-promote-an-economy-that-serves-all-americans [https://perma.cc/J4ZZ-DNEV].

275. Alan Murray, *America's CEOs Seek a New Purpose for the Corporation*, FORTUNE (Aug. 19, 2019), https://fortune.com/longform/business-roundtable-ceos-corporations-purpose/ [https://perma.cc/9NVE-U2AR] (describing the organization's change from its previous statement of corporate purpose)

276. BUSINESS ROUNDTABLE, *supra* note 274.

customers, employees, suppliers, and communities.[277]

In October 2019, then-Delaware Supreme Court Chief Justice Leo Strine released *Towards a Fair and Sustainable Capitalism*.[278] In it, Justice Strine argued that "[t]he incentive system for the governance of American corporations has failed in recent decades to adequately encourage long-term investment, sustainable business practices, and most importantly, fair gainsharing between shareholders and workers."[279] Justice Strine suggested ways to reform corporate governance in order to make corporations give more thoughtful consideration to their employees and social responsibility.[280]

Some unicorns have embraced this perspective. Airbnb announced in January 2020 that it would tie bonuses to the firm's performance on social goals.[281] Airbnb also announced a stakeholder committee on its board of directors and promised to hold a "stakeholder day" to report on its progress.[282] Others promote things like employee experience and bettering the global community.[283]

2. Objections to Stakeholder Emphasis

Unsurprisingly, insistence on the importance of stakeholders to corporate decision making has met with substantial skepticism and influential objections. Warren Buffett argued, "This is the shareholders' money," and corporate managers should not make company decisions based on their social beliefs.[284] Professor Jesse Fried predicted that the Business

277. BUSINESS ROUNDTABLE, *supra* note 274.

278. Leo E. Strine, Jr, *Toward Fair and Sustainable Capitalism* (U. Penn. Inst. for Law & Econ. Research Paper No. 19-39, 2019), *available at* https://www.law.nyu.edu/sites/default/files/Fair%20and%20Sustainable%20Capitalism%20Proposal%20-%20White%20Paper_09.26.19%20FINAL.pdf [https://perma.cc/3TUV-G53D].

279. *Id.* at 1.

280. *Id.* at 3–22.

281. John D. Stoll, *Airbnb's New Compensation Plan Asks Shareholders to Share with Other Stakeholders*, WALL ST. J. (Jan. 18, 2020), https://www.wsj.com/articles/airbnbs-new-compensation-plan-asks-shareholders-to-share-with-other-stakeholders-11579358335 (describing the debate as having reached "peak handwringing" with the Business Roundtable letter).

282. *See Id.* (noting recent challenges faced by Airbnb with respect to policing its platform).

283. For example, now-defunct Better Place, Inc. sought to reduce global dependency on petroleum. *Better Place, Inc.* BLOOMBERG, https://www.bloomberg.com/profile/company/3279529Z:US [https://perma.cc/RVN5-DSTS] (last visited Nov. 23, 2020).

284. Robert Armstrong, *Warren Buffett on Why Companies Cannot Be Moral Arbiters,* FIN. TIMES (Dec. 29, 2019), https://www.ft.com/content/ebbc9b46-1754-11ea-9ee4-11f260415385 [https://perma.cc/QRP2-GDEU] (reporting Buffett's opinion that the government should promote select projects, not companies).

Roundtable pledge will not affect how the signers run their companies and described that as a "[g]ood thing," because shareholder primacy keeps corporate managers accountable and enables efficient capital flows in the economy.[285] The media was quick to point out that, less than a month after Jeff Bezos signed the Business Roundtable letter, Amazon subsidiary Whole Foods cut medical benefits for hundreds of part-time workers.[286] Commentators have suggested that the choices that need to be made among various stakeholder groups result in even more power for the board.[287]

Still, the debate itself may indicate a wider appreciation of the persons affected by corporate operations, regardless of whether they are public or private.

C. *Poor Unicorn Governance Endangers a Large Number of Stakeholders*

Corporate governance failure directly impacts more than founders and their large investors. Corporate governance failure in a large company, regardless of its reporting status, creates broad harms.[288] And when the entity is a private company, the harm is particularly unforeseeable for the stakeholders who have little information and limited remedies.[289]

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285. Jesse Fried, *Shareholders Always Come First and That's a Good Thing,* FIN. TIMES (Oct. 7, 2019), https://www.ft.com/content/fff170a0-e5e0-11e9-b8e0-026e07cbe5b4 [https://perma.cc/QM9V-6K3H] (arguing that payouts from public companies to shareholders are then invested in new companies, for example by private equity and venture capital outfits).

286. *See* Matt Levine, *We Is Sorry About the Weirdness*, BLOOMBERG OPINION (Sept. 13, 2019), https://www.bloomberg.com/opinion/articles/2019-09-13/we-is-sorry-about-the-weirdness [https://perma.cc/XP4T-AVYP] (discussing "stakeholder capitalism"); Hayley Peterson, *Whole Foods Is Cutting Medical Benefits for Hundreds of Part-time Workers,* BUS. INSIDER (Sept. 12, 2019), https://www.businessinsider.com/whole-foods-cuts-medical-benefits-for-part-time-workers-2019-9 [https://perma.cc/2JYL-TWKR] (noting that the change impacted less than 2% of the company's workforce, some of whom had worked there for many years).

287. *See* Matt Levine, *Tidjane Thiam Gets Some Time to Garden*, BLOOMBERG OPINION (Feb. 7, 2020), https://www.bloomberg.com/opinion/articles/2020-02-07/tidjane-thiam-gets-some-time-to-garden [https://perma.cc/5QE6-N9YR] (discussing stakeholder capitalism and using the contentious ouster of Credit Suisse Group AG CEO Tidjane Thiam as an example); *see also* Matthew Levine, *Bank Isn't Happy with Its Owner,* BLOOMBERG OPINION (Jan. 21, 2020), https://www.bloomberg.com/opinion/articles/2020-01-21/bank-isn-t-happy-with-its-owner [https://perma.cc/3NS4-MCJM] (discussing who controls a company and observing that "[s]takeholders have *more* ways to disagree than shareholders do").

288. Steven L. Schwarcz, *Keynote Reflections: The Public Governance Duty*, 50 GA. L. REV. 1, 5 (2015) (pointing out that corporate risk-taking can impact the public as well as investors, particularly in large, "systemically important" firms).

289. *See supra* Part II.B (discussing the lack of public disclosure regarding unicorns).

A troubled company at a unicorn scale may subject employees to substandard working conditions, or sudden unemployment. When a unicorn stumbles, it may jeopardize the viability of related companies and rattle markets. And, in some sectors, a poorly governed unicorn may even put individuals' health at risk.

1. Employees

Unicorns employ thousands of people. In February 2020, Airbnb reported approximately 7,500 employees,[290] Doordash approximately 7500,[291] and SpaceX over 6000.[292] A poorly governed unicorn may subject those employees to discrimination, harassment, and an overall "toxic corporate culture" in the workplace.[293] In a 2017 survey, almost half of women working in startups reported being sexually harassed, and almost three-quarters reported experiencing gender-based discrimination.[294] In 2017, Susan Fowler publicized the sexist culture and harassment at Uber, discussing specific instances in a now-famous blog post.[295] The eventual result was the firing of twenty employees[296] and the ouster of Travis Kalanick as CEO.[297] WeWork is currently defending a pregnancy discrimination

290. *Airbnb's Competitors, Revenue, Number of Employees, Funding and Acquisitions,* OWLER https://www.owler.com/company/airbnb [https://perma.cc/RN3G-C926] (last visited Nov. 21, 2020).

291. *Doordash's Competitors, Revenue, Number of Employees, Funding and Acquisitions,* OWLER, https://www.owler.com/company/doordash [https://perma.cc/85MX-79ZA] (last visited Nov. 21, 2020).

292. *About*, SPACEX, https://www.spacex.com/about [https://perma.cc/N3SD-9GND] (last visited Nov. 21, 2020).

293. Press Release, U.S. Equal Emp. Opportunity Comm'n, Uber to Pay $4.4 Million to Resolve EEOC Sexual Harassment and Retaliation Charge (Dec. 18, 2019), https://www.eeoc.gov/eeoc/newsroom/release/12-18-19.cfm [https://perma.cc/4HPJ-T7G7]; *see also* Jones, *supra* note 57, at 180 (noting the toxic corporate cultures of both Uber and Theranos).

294. Megan Rose Dickey, *Boardlist Founder Says Sexual Discrimination Is More Prevalent than People Think,* TECHCRUNCH (Jan, 28, 2017, 1:49 PM) https://techcrunch.com/2017/01/28/boardlist-founder-says-sexual-discrimination-is-more-prevalent-than-people-think/ [https://perma.cc/T95C-W8KL].

295. Susan Fowler, *Reflecting on One Very, Very Strange Year at Uber*, SUSAN FOWLER (Feb. 19, 2017), https://www.susanjfowler.com/blog/2017/2/19/reflecting-on-one-very-strange-year-at-uber [https://perma.cc/RH92-T5WM].

296. Sarah Buhr, *Uber Has Fired More than 20 People over Harassment Probe,* TECHCRUNCH (June 6, 2017, 1:51 PM) https://techcrunch.com/2017/06/06/uber-may-have-fired-more-than-20-people-over-sexual-harrasment-probe/ [https://perma.cc/NQ7E-9VKN].

297. *See* Zoe Kleinman, *Uber: The scandals that drove Travis Kalanick out,* BBC (Jun. 21, 2017), https://www.bbc.com/news/technology-40352868 [https://perma.cc/4NTB-MBZQ] (chronicling scandals relating to sexual harassment, macho culture, and the departure of senior executives that led to Kalanick's resignation).

lawsuit filed by Neumann's former chief of staff on behalf of herself and other women at that company.[298]

In addition, many start-up employees are compensated partially in the form of company stock options. Private company stock options are illiquid[299] and function as a *de facto* noncompete until the company goes public.[300] Unicorn employees compensated with stock options tend to be both unprotected and uninformed regarding, for example, senior rights of managers and other investors.[301]

This was even more pronounced in the case of WeWork, because Softbank's October 2019 bailout was originally supposed to include not just $6.5 billion to the company, but also a $3 billion tender offer.[302] Those funds were supposed to extract Neumann, as well as certain institutional investors, who would receive at least some return on their investment and flee.[303] When SoftBank backed out of the share purchase arrangement,[304] litigation ensued.[305]

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298. Class and Collective Administrative Charge of Discrimination, Retaliation, and Gender Pay Disparity, Bardhi v. The We Co., *supra* note 5.

299. *See* Anat Alon-Beck, *Unicorn Stock Options – Golden Goose or Trojan Horse?*, 2019 COLUM. BUS. L. REV. 107, 108 (2019) (noting that the extended private status of unicorns delays liquidity for employees paid in options).

300. *See* Seth Oranburg, *Democratizing Startups*, 68 RUTGERS L. REV. 1013, 1015 (2016) (noting problems with the JOBS Act and proposing a new rule to permit transparent, web-based venture exchanges).

301. *See* Abraham J.B. Cable, *Fool's Gold? Equity Compensation & the Mature Startup*, 11 VA. L. & BUS. REV. 613, 614–16 (2017) (arguing that although startup employees may be relatively capable investors in a company's early stages, they are poorly equipped to navigate the risks of a unicorn).

302. Taylor Telford, *WeWork Snags $9.5 Billion Bailout from SoftBank, Staving Off Bankruptcy*, WASH. POST (Oct. 23, 2019, 8:27 AM), https://www.washingtonpost.com/business/2019/10/23/wework-snags-billion-bailout-softbank-staving-off-bankruptcy/ [https://perma.cc/6MFA-AXVP] (noting that WeWork would have run out of money within weeks without the cash infusion).

303. Theron Mohamed, *SoftBank's $9.5 Billion Bailout of WeWork Hits a Hurdle as Japanese Banks Are Worried about Funding It*, MARKETS INSIDER (Dec. 23, 2019, 6:09 AM), https://markets.businessinsider.com/news/stocks/softbank-wework-rescue-deal-hits-hurdle-japanese-bank-talks-stall-2019-12-1028781774 [https://perma.cc/F6PM-EFNA].

304. Noah Kirsch, *Softbank's Latest Lifeline to WeWork Is a Fresh Snub of Adam Neumann, But What Happens Next?*, FORBES (Aug. 15, 2020, 8:00 AM), https://www.forbes.com/sites/noahkirsch/2020/08/15/softbanks-latest-lifeline-to-wework-is-a-fresh-snub-of-adam-neumann-but-what-happens-next/#8f85a7820038 [https://perma.cc/8CAR-NXSA] (explaining Softbank's new investment in the company, and Softbank's decision to back out of the purchase agreement based on WeWork's failure to meet the required conditions).

305. Neumann v. SoftBank Group Corp, No. 2020-0329, (Del. Ch. filed May 4, 2020) (seeking damages for SoftBank's decision not to proceed with the share purchase); The We Company v. SoftBank Group Corp, No. 2020-0258, (Del. Ch. filed Apr. 7, 2020) (seeking specific performance of the $3 billion share purchase agreement). This litigation is ongoing,

Most employees, however, would have been unable to take advantage of the tender offer anyway. Over 90% of employees holding options were underwater, meaning that the SoftBank share price being offered was below the grant price for the employees' awards or options.[306] For such employees, those options, a large part of their compensation, are not and may never be worth anything.[307]

In some cases, the lack of corporate governance can lead to sudden contraction or even closure of the unicorn. Theranos closed its operations.[308] When WeWork lost 85% of its valuation[309] and refocused and reorganized its operations, the company fired 2,400 employees, and transferred another 1,000 to an outside vendor.[310] WeWork's losses and layoffs continued as the Covid-19 pandemic struck.[311] Airbnb laid off 25% of its workforce in

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and in August 2020, the Delaware Chancery Court released a preliminary opinion regarding different directors' rights to review information and control decisions relating to the lawsuits. In re WeWork Litig., 2020 BL 319261, 2020 Del. Ch. Lexis 270, (Del. Ch. Aug. 21, 2020) (holding that members of a special board committee that was established before the SoftBank decision not to proceed with the tender offer are still entitled to discovery of company attorney communications related to the dispute). In October 2020, the Court rejected some breach of fiduciary duty claims made by Neumann against SoftBank and an affiliated venture fund. In re WeWork Litig., No. 2020-0258-AGB, 2020 WL 6375438, Mem. Op. at 3 (Del. Ch. Oct. 30, 2020) (holding that those claims duplicated other contractual claims that are being made in the consolidated action).

306. Eliot Brown, *WeWork Employee Options Underwater as Ex-CEO Reaps,* WALL ST. J. (Oct. 23, 2019, 6:33 PM), https://www.wsj.com/articles/wework-employees-feel-sting-as-ex-ceo-stands-to-reap-11571870011 [https://perma.cc/YK7Y-DR79] (describing company employees as not doing as well as Neumann).

307. Sarah E. Needleman & Eliot Brown, *WeWork to Cut Around 17% of Workforce,* WALL ST. J. (Nov. 21, 2019, 2:17 PM), https://www.wsj.com/articles/wework-to-cut-around-17-of-workforce-11574355656 [https://perma.cc/K2WV-NDJQ].

308. Reed Abelson, *Theranos Is Shutting Down*, N.Y. TIMES (Sept. 5, 2018), https://www.nytimes.com/2018/09/05/health/theranos-shutting-down.html [https://perma.cc/454G-ZEHP] (reporting that the company would shutter its operations). Any equity investments in the company became worthless. John Carreyrou, *Blood-Testing Firm Theranos to Dissolve*, WALL ST. J. (Sept. 5, 2018, 12:10 AM), https://www.wsj.com/articles/blood-testing-firm-theranos-to-dissolve-1536115130 [https://perma.cc/VZX6-Y27E].

309. Maureen Farrell et al., *The Fall of WeWork: How a Startup Darling Came Unglued,* WALL ST. J. (Oct. 24, 2019 4:40 PM), https://www.wsj.com/articles/the-fall-of-wework-how-a-startup-darling-came-unglued-11571946003 [https://perma.cc/F622-6W2R] (explaining that the WeWork valuation went from $47 billion in January 2019 to less than $8 billion in October 2019).

310. Gillian Tan, *WeWork Says It's Cutting 2,400 Jobs Globally*, BLOOMBERG (Nov. 21, 2019 3:40 PM), https://www.bloomberg.com/news/articles/2019-11-21/wework-says-it-s-cutting-2-400-jobs-globally-to-reach-efficiency [https://perma.cc/BKT8-FKA7]; Needleman & Brown, *supra* note 307.

311. Samantha Sharf, *WeWork Unraveling Continues with New Layoff Round*, FORBES (Apr. 30, 2020, 7:02 PM), https://www.forbes.com/sites/samanthasharf/2020/04/30/wework-unraveling-continues-with-new-layoff-round/#4ee1ac363581 [https://perma.cc/3PGJ-RD9T]

May 2020, as its pandemic-related losses began to be felt.[312]

2. Customers or Clients (or Patients)

A poorly governed unicorn may lack the compliance structures needed to ensure that it is licensed to operate[313]—or is medically safe.[314] The risk seems particularly acute given the "growth-at-any-cost"[315] mindset of many startups.[316] This risk is illustrated in the case of Theranos. Thanks to over-generous capitalization and underwhelming governance, Theranos achieved a peak valuation of $9 billion and raised over $700 million[317] while refusing to disclose the details of its blood-testing technology, which did not perform as claimed.[318] Dominated by its charismatic founder, Elizabeth Holmes, the "blood unicorn" barreled forward with falsified results despite employee complaints and physician concerns.[319] Eventually, the company had to void tens of thousands of test results that had been issued to patients and physicians.[320]

Better Place Inc., a California-based unicorn that sold electric cars and built charging station networks under founder Shai Aggasi's hubristic

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(quoting a company spokesperson who called it "realigning").

312. PYMTS, *Airbnb Suffers Record Losses in Q2, IPO Still Planned,* PYMTS.COM (Aug. 13, 2020), https://www.pymnts.com/earnings/2020/airbnb-suffers-record-losses-in-q2-ipo-still-planned/ [https://perma.cc/46N2-LRM8] (reporting that 25% of Airbnb's 1900-person workforce were being laid off).

313. This was a problem at Uber. *See* Elizabeth Pollman & Jordan M. Barry, *Regulatory Entrepreneurship,* 90 S. CAL. L. REV. 383, 385–87 (2017) ("Uber and many other businesses are built around and based upon a plan to change the law—and, in some instances, to simply break the law in the meantime.").

314. As discussed above, Theranos marketed a non-functioning blood testing service.

315. Jeremy G. Philips, *The Rise and Fall of the Unicorn*, N.Y. TIMES (Feb. 12, 2016), https://www.nytimes.com/2016/02/13/business/dealbook/the-rise-and-fall-of-the-unicorn.html [https://perma.cc/Y3TK-GSX4].

316. *How Unicorns Grow*, HARV. BUS. REV., Jan.-Feb. 2016, at 28, 28-30 (discussing the rapid growth of unicorn companies and how it is happening).

317. Matt Levine, *The Blood Unicorn Theranos Was Just a Fairy Tale*, BLOOMBERG OPINION (Mar. 14, 2018, 3:18 PM), https://www.bloomberg.com/opinion/articles/2018-03-14/theranos-misled-investors-and-consumers-who-used-its-blood-test [https://perma.cc/E28S-M8UN].

318. John Carreyrou, *Hot Startup Theranos Has Struggled with Its Blood-Testing Technology*, WALL ST. J. (Oct. 16, 2015, 3:20 PM), https://www.wsj.com/articles/theranos-has-struggled-with-blood-tests-1444881901 [https://perma.cc/J97Z-D727] (detailing Theranos falsifications and complaints against it).

319. *Id.*

320. John Carreyrou, *Theranos Voids Two Years of Edison Blood-Test Results*, WALL ST. J. (May 18, 2016, 8:16 PM), https://www.wsj.com/articles/theranos-voids-two-years-of-edison-blood-test-results-1463616976 [https://perma.cc/647Z-4AUC].

leadership, left all of its Israeli car owners without the necessary charging and battery swap infrastructure when the company went bankrupt in 2013.[321] Stories of gross exaggeration, if not lies, about the company's technology, runaway expenses, cronyism, so-called "Shai math,"[322] and lack of board oversight abounded.[323]

3. Collateral Businesses

Many unicorns operate related businesses, which may also go under due to governance issues at the unicorn itself. In fall 2019, WeWork sought to cut costs and unload assets quickly. The sudden shuttering of WeWork's unrelated collateral ventures imposed substantial hardships on a variety of stakeholders.[324] Over 100 children were impacted by WeWork's abrupt decision to close its WeGrow school.[325] Meetup, an event-facilitating company that WeWork bought for $200 million in 2017, laid off as much as

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321. Max Chafkin, *A Broken Place: The Spectacular Failure Of The Startup That Was Going To Change The World,* FAST COMPANY (Apr. 7, 2014), https://www.fastcompany.com/3028159/a-broken-place-better-place [https://perma.cc/6FFC-5PRV].

322. *Id.*

323. *Id*; *see also* BRIAN BLUM, TOTALED: THE BILLION-DOLLAR CRASH OF THE STARTUP THAT TOOK ON BIG AUTO, BIG OIL AND THE WORLD 177–233 (2017) (chronicling mismanagement, overpromising, and lack of trust in the company in chapters such as "Bait and Switch," "How to Lose Everything without Really Trying," and "Who Trusts Shai?").

324. Needleman & Brown, *supra* note 307 (noting the 1,000 employees of companies WeWork had acquired and was trying to sell).

325. Meghan Morris & Becky Peterson, *WeWork's school is closing at the end of the academic year as the company ditches passion projects to stem its huge losses,* BUS. INSIDER (Oct. 11, 2019, 11:46 AM), https://www.businessinsider.com/wework-closes-wegrow-rebekah-neumanns-school-effort-2019-10 [https://perma.cc/5A2B-XATW]; *see also* Blake Montgomery, *WeWork's Ritzy Private School Has 'Stranded' Parents as CEO Walks Away With Nearly $2 Billion*, DAILY BEAST (Oct. 23, 2019, 5:14 AM), https://www.thedailybeast.com/weworks-private-school-wegrow-has-stranded-parents-as-adam-neumann-cashes-out [https://perma.cc/M69P-7ZAA] (quoting an educational consultant as saying, "[t]he kids will be the collateral damage when the school closes"). WeGrow closed in late 2019. However, Rebekah Neumann bought back the curriculum and some furnishings of the WeGrow school and is attempting to reopen the program. David Jeans, *Rebekah Neumann Buys Back WeGrow, WeWork's Defunct $42,000-A-Year School, With Plans To Relaunch*, FORBES (Jun. 30, 2020, 3:49 PM) https://www.forbes.com/sites/davidjeans/2020/06/30/rebekah-neumann-buys-back-wegrow-weworks/#312f42b92376 [https://perma.cc/82JZ-MNZY]. Ironically, following the fall 2019 WeGrow program closure, WeWork CEO Sandeep Mathrani coordinated with New York City schools to use WeWork locations in response to Covid-19 to hold in-person classes while reducing the density among students. Kevin Stankiewicz, *WeWork is talking to NYC private schools about holding classes in offices this fall, CEO says,* CNBC REAL ESTATE (Jun. 16, 2020, 10:14 AM), https://www.cnbc.com/2020/06/16/wework-talking-to-nyc-private-schools-about-holding-classes-in-offices.html [https://perma.cc/Q4QV-VJM9].

25% of its workforce in the wake of WeWork's cancellation of its IPO.[326] WeWork's woes led to layoffs of thousands of staff members at Managed by Q, an office management platform purchased by WeWork for $220 million in April 2019[327] (and which it sold in January 2020 for less than a quarter of the price).[328] In December 2019, WeWork shut down Spacious, a restaurant coworking start-up that WeWork had acquired four months earlier, laying off its entire fifty-person staff and disrupting the company's customers' businesses.[329]

4. Economy and Markets

Economic ripples from unicorn stumbles may also be widespread. By 2019, WeWork was the largest commercial tenant in New York City, and only the British government controlled more space in London.[330] While still private, Uber had a significant impact on the transportation behavior of below-median-income consumers who may have lower rates of automobile ownership.[331] In 2017, Airbnb represented a significant percentage of the hotel room supply in several major cities[332] and had a significant effect on

326. Kate Clark, *WeWork-owned Meetup confirms restructuring, layoffs*, TECHCRUNCH (Nov. 4, 2019, 6:18 PM), https://techcrunch.com/2019/11/04/wework-owned-meetup-confirms-restructuring-layoffs/ [https://perma.cc/TLM5-8V7M].

327. TRD Staff, *WeWork plans to sell Managed by Q at a major loss*, THEREALDEAL (Dec. 19, 2019, 11:15 AM), https://therealdeal.com/2019/12/19/wework-plans-to-sell-managed-by-q-at-major-loss/ [https://perma.cc/U8UP-Z4TP].

328. Daria Rud, *WeWork Sells Managed by Q Unit at an Incredibly Low Price*, COINSPEAKER (Jan. 23, 2020, 1:09 PM), https://www.coinspeaker.com/wework-sells-managed-by-q-unit/ [https://perma.cc/5ZVT-VF8D].

329. Shirin Ghaffary, *WeWork is Shutting Down a Restaurant Coworking Startup Acquired Only 4 Months Ago*, VOX (Dec. 12, 2019), https://www.vox.com/recode/2019/12/12/21012723/wework-spacious-shutting-down-adam-neumann-coworking [https://perma.cc/JJW6-BE7W].

330. *See* Jack Sidders & Natalie Wong, *WeWork Landlords in London and New York Are Bracing for a Market Fallout*, BLOOMBERG (Sept. 27, 2019), https://www.bloomberg.com/news/articles/2019-09-27/wework-landlords-in-london-new-york-bracing-for-market-fallout [https://perma.cc/NS73-QAEQ] (discussing the concern of Landlords as WeWork's demand begins to fall); Platt & Edgecliffe-Johnson, *supra* note 13, (discussing widespread effects of WeWork's financial collapse); *see also* Peter Eavis, '*It's Definitely Pretty Empty': Why Saving WeWork Will Be Hard,* N.Y. TIMES (Oct. 24, 2019), https://www.nytimes.com/2019/10/24/business/wework-growth.html [https://perma.cc/9Z3N-ED3M] (pointing out that not only was WeWork New York's largest private tenant, it had also committed to take on an additional 2.6 million square feet in 2019).

331. Fan, *supra* note 63, at 600.

332. *See* Avery Hartmans, *Airbnb Now Has More Listings Worldwide than the Top Five Hotel Brands Combined,* BUS. INSIDER (Aug. 10, 2017), https://www.businessinsider.com/airbnb-total-worldwide-listings-2017-8 [https://perma.cc/9DUB-DEJT] (noting 4 million

local economies.[333]

None of the foregoing arguments made for a company's responsibility to stakeholders depends on the distinction between public and private corporations. While a firm's capital structure presumably gives rise to obligations to the provider of capital, as a general matter, a firm may be obliged to stakeholders whether or not its capital structure means it is classed as "public" or "private."

That said, as unicorns proliferate, they may even jeopardize the capacity of markets to function as mechanisms for public choice. Professor De Fontenay observes that the ability of so many large private companies to avoid mandatory disclosure constitutes "free riding" on the information disclosed by public companies.[334] The securities laws' mandatory disclosure requirements produce price and other valuation information that is important to the functioning of the economy. Unicorns' large-scale opt out from that structure shrinks the pool of disclosing companies and threatens the quality and usefulness of the information available to the financial markets.

In sum, an enterprise large enough to be a unicorn has widespread and profound economic and social effects.[335] Shoddy governance in such a firm, harms more than just the profit-seeking diversified investors often idealized by corporate finance.

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listings worldwide in 2017).

333. Fan, *supra* note 63, at 600. The potential impact of an Airbnb failure became clear with the onset of the Covid-19 pandemic. *See* Kristen Grind et al., *Airbnb's Coronavirus Crisis: Burning Cash, Angry Hosts and an Uncertain Future,* WALL ST. J. (Apr. 8, 2020), https://www.wsj.com/articles/airbnbs-coronavirus-crisis-burning-cash-angry-hosts-and-an-uncertain-future-11586365860 [https://perma.cc/RUE7-JEJZ] (cataloging the losses suffered by hosts and travelers). Nevertheless, Airbnb announced in August 2020 that it had submitted a confidential draft registration statement to the SEC. Press Release, Airbnb, Airbnb Announces Confidential Submission of Draft Registration Statement (Aug. 19, 2020), https://news.airbnb.com/airbnb-announces-confidential-submission-of-draft-registration-statement/ [https://perma.cc/XJ6B-98B9].

334. *See* de Fontenay, *supra* note 173, at 451 (calling the current structure "inherently unstable").

335. *See* Fan, *supra* note 63, at 602 (pointing out that unicorns may, for example spur economic development because their "sheer size and demand for the services they provide create a need for infrastructure and services that assist these companies, influencing the growth of businesses in other industries."). In fact, there is a growing market niche in providing infrastructure and services to the unicorns themselves. *See Pickaxes and Shovels: 35 Startups Providing Infrastructure for the On-Demand Boom*, CB INSIGHTS (Jul. 14, 2015), https://www.cbinsights.com/blog/infrastructure-for-on-demand-startups/ [https://perma.cc/L96T-DCGN] (describing companies specializing in route and vehicle optimization, as well as background checks and security).

IV. COUNTERARGUMENT: BAD GOVERNANCE IS A FAIR PRICE FOR INNOVATION

It might be argued that more rigorous governance of unicorns could stifle innovation and prevent visionary founders from developing new disruptive technologies and business models.[336] Startups are special, one might say, and often dramatically change or even create new sectors of the economy. A more rigid conception of how a company is to run, with conventional requirements regarding governance and financial performance, could prevent change. Therefore, such an argument would conclude, start-ups need to retain their freedom.[337]

Some commentators argue that risky endeavors are often a life work for the founders of a start-up.[338] All their eggs are in one basket, and the payoff is contingent on their first-mover advantage. The disclosure and transparency that result from reporting company status would allow copycat competitors to steal that advantage. "Stealth mode" is necessary to develop revolutionary new products.[339] Without first mover advantages, the motivation for founders to risk everything would be substantially reduced, and innovation would suffer accordingly.[340]

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336. Companies often argue that their founders' ideas and innovations are integral to the company's success, even when the escapades of those founders create problems, if not liabilities. *See, e.g.*, Nikola Corp., Quarterly Report (Form 10Q), at 55 (Aug. 4, 2020) (asserting that its founder and CEO, Travis Milton, "is the source of many, if not most, of the ideas and execution driving Nikola," and that if the company lost Milton it would be "significantly disadvantaged"). This perception of Milton's essential vision was challenged by the problems posed by his behavior less than a month later. *See, e.g.*, Ben Foldy & William Boston, *Nikola Founder Trevor Milton Resigns as Executive Chairman amid Fraud Allegations,* WALL ST. J. (Sept. 21, 2020) (discussing Milton's removal from the company and allegations that Milton misrepresented the capabilities of the company technology).

337. *See, e.g.*, Justin Fox, *Elon Musk's Brain Isn't Like Yours,* BLOOMBERG OPINION (Sept. 10, 2018), https://www.bloombergquint.com/opinion/elon-musk-s-quirks-are-worth-the-trouble-for-tesla [https://perma.cc/GFW2-VK9A] (reviewing Melissa Schilling's book *Quirky* which suggests, for example, that Elon Musk's outrageous behavior is related to his extreme creativity).

338. *See* Karen Firestone, *How Hard Do Company Founders Really Work?,* HARVARD BUS. REV. (Dec. 17, 2014), https://hbr.org/2014/12/how-hard-do-company-founders-really-work [https://perma.cc/W3YM-UHDY] (discussing her own experiences and those of other start-up founders she surveyed).

339. *See* Fan, *supra* note 63, at 608 (detailing what metrics a unicorn should and should not disclose).

340. *See, e.g.*, Shlomit Yanisky Ravid & Xiaoqiong Liu, *When Artificial Intelligence Systems Produce Inventions: An Alternative Model for Patent Law at the 3A Era*, 39 CARDOZO L. REV. 2215, 2254 (2018) (surveying first-mover advantage); Rajshree Agarwal & Michael Gort, *First-Mover Advantage and the Speed of Competitive Entry, 1887-1986*, 44 J. L. & ECON. 161, 162–65 (2001) (providing a historical overview).

Apart from being highly speculative, these arguments offer at best a romanticized vision of the technology founder. They also fail to explain why major investors receive information, but other investors and employee shareholders do not.[341] Most importantly, a great many companies both achieve their founders' visions and have decent governance. There is no necessary causal connection between bad governance and a creative vision.[342]

V. HOW MIGHT BETTER GOVERNANCE BE ACHIEVED?

A. Corporation Law

1. Fiduciary Duties Should Prevent Self-Dealing

How might we achieve better governance? Arguably, no changes in the terms of the law are needed to foster and enforce effective corporate governance in any corporation. What may be needed, however, are changes in how those terms are understood and enforced. As agents of the corporation, unicorn executives and directors, like executives and directors of any company, owe fiduciary duties of care and loyalty to the corporation. Therefore, for example, conflict of interest transactions—like many of the transactions in which WeWork engaged—should be challengeable. Unlikely to be "cleansed" by a vote of disinterested and independent directors or ratified by disinterested shareholders, such arrangements should not be permitted.[343] Neumann's nepotistic hiring practices, the leases he arranged for property he owned, and his sale of the "We Company" name to the company itself, could have been challenged. Neumann could have been required to reimburse the company for the damages it suffered from those transactions. In fact, self-dealing as pronounced as that engaged in by Neumann should have been deterred in the first place.[344]

341. Fan, *supra* note 63, at 608–09.

342. For example, Microsoft was the winner of the Ethical Boardroom's "Best Corporate Governance" designation in 2018. *See* Ethical Boardroom, *Corporate Governance Winners 2018 – The Americas*, ETHICALBOARDROOM.COM (2018), https://ethicalboardroom.com/corporate-governance-winners-2018-the-americas/ [https://perma.cc/U43N-9AR6] (naming winners in many different sectors).

343. *See, e.g.*, *In re* UNFOUSA Inc. S'holders Litig., 953 A.2d 963 (Del. Ch. 2007) (finding that the board likely breached its fiduciary duties in approving a related-party transaction).

344. One WeWork spokesman reportedly said that all related-party deals were reviewed and approved by the board or an independent committee and disclosed to investors. Brown, *supra*, note 7.

2. Fiduciary Duties Should Make Unicorn Directors Vigilant

Similarly, unicorn directors, even those appointed by and connected to powerful founders, have a duty to oversee and monitor the operations of the corporations. This duty is not excused just because its founder has a particular vision, or just because the founder has the voting power to remove directors at will. The oversight duty, the idea that directors should have a solid idea of the fundamentals of the business and the arrangements being made by it, is a fundamental duty of all directors.[345]

3. Fiduciary Duties Should Compel Managers to Make Informed, Disinterested, Decisions in the Best Interests of the Unicorn

Directors and managers enjoy a great deal of protection because courts presume,[346] under the business judgement rule, that board decisions are informed, disinterested, and in the best interests of the company.[347] The business judgment rule protects many if not most decisions made by corporate managers. But even today, that protection is not limitless. It is a rebuttable presumption.[348] For example, to be granted the protection of the business judgment rule, directors are required to fulfill their fiduciary duty of care, notably by informing themselves about the decisions they are called on to make.[349] This is true of all corporations, private or public, regardless of size.[350]

345. According to one report, the WeWork board raised concerns about leasing property owned by Neumann in 2013, and the deal was reconfigured. The next year, however, Neumann got control of the company with 10-votes-a-share Class B shares, and WeWork proceeded with a number of transactions in which it leased property owned by Neumann. Brown, *supra*, note 7.

346. This presumption is not limited to Delaware courts. *See Business Judgment Rule – In general*, 3A FLETCHER CYC. CORP. §1036 (describing the business judgment rule as a common-law judicial standard of review).

347. Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984).

348. Smith v. Van Gorkom, 488 A.2d 858 (Del. 1985) (finding in favor of plaintiff shareholders, who successfully rebutted the presumption that the directors were informed).

349. *Id.*

350. *Id.* at 872 (making no distinction regarding corporate size); *see also* Francis v. United Jersey Bank, 431 A.2d 814, 822 (N.J. 1981) (holding that "directors are under a continuing obligation to keep informed about the activities of the corporation" in the context of a small family-owned corporation). However, enforcement of those duties is less frequent in private companies. *See* Duhigg, *supra* note 16 (noting that lawsuits alleging harm to minority shareholders from board inaction are much less common in the context of private companies).

4. Hurdles to Stronger Corporation Law as a Solution

A rejuvenated corporation law would be an avenue for improved unicorn governance, but it seems unlikely. Most unicorns, indeed, most large public companies,[351] are incorporated in Delaware. WeWork, SpaceX,[352] Airbnb,[353] Doordash,[354] Zume,[355] and Theranos, all are (or were) incorporated in Delaware. Delaware is a popular state of incorporation not only because of its well-developed corporation law jurisprudence, but also because it is considered management-friendly.[356] In the last few decades, the Delaware Chancery Court and Supreme Court have consistently declined to second-guess management decisions.[357] Holding executives and directors liable for violations of their state-law fiduciary duties is at best difficult. Not only is Delaware judicial precedent deferential to management, but as discussed above, the prosecution of shareholder derivative suits is procedurally difficult.[358] Despite Justice Strine, Delaware is unlikely to

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351. For example, more than 66% of the Fortune 500 have chosen Delaware as their legal home. *About the Division of Corporations,* DEL. DIV. CORP (last visited Nov. 22, 2020), https://corp.delaware.gov/aboutagency/ [https://perma.cc/SPM6-CTRQ].

352. *See* SpaceExploration Techs. Corp., *Notice of Exempt Offering of Securities (Form D)* (Mar. 30, 2009), *available at* https://www.sec.gov/Archives/edgar/data/1181412/000118141209000003/xslFormDX01/primary_doc.xml [https://perma.cc/4BKK-99CW] (listing the company's state of incorporation as Delaware).

353. *See* Airbnb, Inc., *Notice of Exempt Offering of Securities (Form D)* (Oct. 23, 2012), https://www.sec.gov/Archives/edgar/data/1559720/000155972012000002/xslFormDX01/primary_doc.xml [https://perma.cc/L9V8-8JPD] (listing the company's state of incorporation as Delaware).

354. *See* Doordash Inc., *SEC Registration*, https://sec.report/CIK/0001792789 [https://perma.cc/B63J-4GQP] (listing the company's state of incorporation as Delaware).

355. *See* Zume, Inc., *SEC Registration*, https://sec.report/CIK/0001690914 [https://perma.cc/TAF4-5FL4] (listing the company's state of incorporation as Delaware).

356. *See* Alana Semuels, *The Tiny State Whose Laws Affect Workers Everywhere*, ATLANTIC (Oct. 3, 2020), https://www.theatlantic.com/business/archive/2016/10/corporate-governance/502487/ [https://perma.cc/85AD-6BWP] (claiming that Delaware is friendly to business). *But see Why Businesses Choose Delaware*, DELAWARE.GOV (last visited Nov. 21, 2020), https://corplaw.delaware.gov/why-businesses-choose-delaware/ [https://perma.cc/36TE-MYY3] ("Delaware is neither 'management-friendly' nor "stockholder-friendly.'").

357. *See* Laura Bower Braunsberg, *Asking the Right Question: The Mixed Consideration Denominator Problem*, 40 DEL. J. CORP. L. 989, 993 (2016) (quoting In re Cox Commc'ns, Inc. S'holders Litig., 879 A.2d 604, 614 (Del. Ch. 2005)) ("[T]he central idea of Delaware's approach to corporation law is the empowerment of centralized management, in the form of boards of directors and the subordinate officers they choose, to make disinterested business decisions.").

358. *See* Amy Deen Westbrook, *Double Trouble: Collateral Shareholder Litigation Following Foreign Corrupt Practices Act Investigations*, 73 OHIO ST. L. J. 1217, 1229–31 (2012) (outlining some of the procedural difficulties).

make things worse for managers.[359]

Of course, there are 49 other states. About 20 of those have enacted a corporation law based on the Model Business Corporation Act, which is drafted by a committee of the American Bar Association.[360] Although the two approaches share much,[361] the MBCA has subtle differences including requiring pre-demands in derivative suits,[362] and an explicit rule to be applied in the case of board conflicts of interest.[363]

Some states have gone even further. In 2018, California passed new corporate governance requirements related to board composition.[364] Its "Women on Boards" law went into effect in 2019 and required all public companies headquartered in California to have least one female director on their boards by December 31, 2019.[365] One or two or more women are required, depending on the size of a company's board, by December 31, 2021.[366] By basing the requirement on headquarters, not state of incorporation, California captured many of the giant technology companies that are based there, including former unicorns such as Facebook and Alphabet (then Google).[367] Other states are following with respect to diversity,[368] although the California measure is currently being challenged in court.[369] The willingness of some states to push back against Delaware's

359. Delaware does not have a "constituencies statute" enabling corporations to allow their directors to consider stakeholders, but it does allow for the incorporation of public benefit corporations. DEL. CODE ANN. tit. 8 §§ 361-68 (2019).

360. *See Corporate Laws Committee*, AM. BAR ASS'N (last visited Nov. 22, 2020), https://www.americanbar.org/groups/business_law/committees/corplaws/ [https://perma.cc/L6ZZ-TE4D] (displaying which states have enacted a Model Business Corporation Act-derived corporation law).

361. *See* Jeffrey M. Gorris, Lawrence A. Hamermesh, & Leo E. Strine, Jr., *Delaware Corporate Law and The Model Business Corporation Act: A Study in Symbiosis,* 74 LAW & CONTEMP. PROBLEMS 106, 106 (2011) (arguing that the two approaches complement each other and do not differ significantly).

362. Model Bus. Corp. Act §7.42

363. Model Bus. Corp. Act, Subchapter F, §§8.60-8.63.

364. CAL. CORP. CODE §301.3 (2019).

365. CAL. CORP. CODE §301.3(a) (2019).

366. CAL. CORP. CODE §301.3(b) (2019).

367. A companion measure made it clear that the law applies to corporations incorporated in other states (e.g., Delaware). CAL. CORP. CODE § 2115.5 (2019).

368. Washington State's board gender diversity law went into effect on June 11, 2020. *See* Lori A. Oliver & Jessica M. Norris, *Corporate Governance Emerging Best Practices Series: Gender-Diverse Boards*, NAT'L L. REV. (Aug. 18, 2020), https://www.natlawreview.com/article/corporate-governance-emerging-best-practices-series-gender-diverse-boards [https://perma.cc/429S-5NHJ] (outlining the requirements of the law and predicting that similar laws will be enacted throughout the nation).

369. *See* Kayla Epstein*, This State Requires Company Boards to Include Women. A New Lawsuit Says That's Unconstitutional,* WASH. POST (Nov. 14, 2019), https://www.washingto

erosion of corporate governance requirements may bode well for unicorn stakeholders.

B. More Applicable (and Applied) Securities Law

1. More Provisions of the Federal Securities Laws Should Apply to Unicorns

Unicorn governance could also be improved through more stringent application of the federal securities laws in the private company context. In the last few decades, federal securities regulation has impacted corporate governance in ways that were once exclusively the province of state law. [370] The Sarbanes-Oxley Act,[371] the Dodd-Frank Act,[372] and a number of other measures[373] have been enacted, shaping the governance of at least large, and generally publicly traded, corporations.

Many of those measures were put in place to curtail executive

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npost.com/business/2019/11/14/this-state-requires-company-boards-include-women-new-lawsuit-says-thats-unconstitutional/ [https://perma.cc/6Z39-DA8F] (describing several suits filed against the new law). *See* Alisha Haridasani Gupta, *California Companies Are Rushing to Find Female Board Members*, N.Y. TIMES (Dec. 17, 2019, updated Jan. 14, 2020), https://www.nytimes.com/2019/12/17/us/california-boardroom-gender-quota.html [https://perma.cc/A9EH-XA2Z] (reporting that two suits had been filed arguing that the law is unconstitutional). In August 2020, the California legislature passed an additional diversity bill requiring California-based public corporations to have at least one board member from an underrepresented community by the end of 2021, with more required in subsequent years. *See* Anne Steele, *California Lawmakers Back Mandate for Racial Diversity on Corporate Boards,* WALL ST. J. (Aug. 31, 2020), https://www.wsj.com/articles/california-lawmakers-mandate-racial-diversity-on-corporate-boards-11598915372 [https://perma.cc/FNM4-HNZ3] (explaining the requirements of the bill). Governor Newsome signed the legislation on September 30, 2020. *See* Levi Sumagaysay, *California Will Require Public Companies to Have Diverse Boards,* MARKETWATCH (Sept. 30, 2020), https://www.marketwatch.com/story/california-will-require-public-companies-to-have-diverse-boards-11601504807 [https://perma.cc/27KJ-T2NZ] (quoting Governor Newsome as stating, "It is clear we can no longer wait for corporations to figure it out on their own").

370. Scholars began to speak of the "federalization" of corporation law. *See*, *e.g.*, Jill E. Fisch, *Leave It to Delaware: Why Congress Should Stay Out of Corporate Governance,* 37 DEL. J. CORP. L. 731 (2013) (arguing that Delaware's approach is superior to a federal approach).

371. Sarbanes-Oxley Act of 2002, Pub. L. No. 107–204, 116 Stat. 745 (codified as amended in scattered sections of 15 U.S.C. and 18 U.S.C.).

372. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

373. For example, changes to the federal tax code. *See*, *e.g.*, Orsolya Kun, *Corporate Inversions: The Interplay of Tax, Corporate, and Economic Implications*, 29 DEL. J. CORP. L. 313 (2004) (highlighting potential governance implications from corporate expatriations for tax purposes).

misbehavior and inadequate governance of publicly traded companies. However, the key antifraud provision of the securities laws, Rule 10b-5,[374] prohibits misleading statements and misrepresentations by all companies, public and private.[375] Rule 10b-5 prohibits untrue statements or omissions of material facts or anything that operates as a fraud or deceit upon any person "in connection with the purchase or sale of *any* security."[376]

When a unicorn sells a security (debt or equity) to an investor, the SEC has the power to ensure that investors are not misled with regard to the affairs of the company. SEC Rule 10b-5 enforcement requires a showing that a person made a material misrepresentation or omission in connection with the purchase or sale of a security, with scienter.[377] Theoretically, if investors can show those elements, as well as reliance, economic loss, and loss causation,[378] they may have a private right of action to seek compensation for damages resulting from the misleading representations by such person.

The SEC has indicated that it will scrutinize unicorns closely.[379] By some accounts, the SEC has increased oversight of unlisted firms in the last few years.[380] For example, the SEC fined Zenefits and its founder, Parker Conrad, over $1 million in 2017 for making false and misleading statements

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374. 17 C.F.R. § 240.10b-5 (2020).

375. *See* Kayla Stavinoha, *How Unreal Is the Unicorn Now? The Need for Regulation in the Wild-Wild-West of Private Companies*, 59 WASHBURN L. J. 171, 189–90 (2020) (discussing Rule 10b-5 and its application in the private context).

376. 17 C.F.R. § 240.10b-5 (2020) (emphasis added).

377. *See*, *e.g.*, S.E.C. v. Blatt, 583 F.2d 1325 (5th Cir. 1978) (explaining the elements the SEC must demonstrate to enjoin defendants from actions violating Rule 10b-5).

378. Dura Pharmaceuticals, Inc. v. Broudo 544 U.S. 336, 341–42 (2005) (setting out the requirements for a private suit).

379. This was emphasized in 2016 by then-SEC Chair Mary Jo White with respect to unicorn corporate governance, at the SEC-Rock Center on Corporate Governance Silicon Valley Initiative:

> It is axiomatic that all private and public securities transactions, no matter the sophistication of the parties, must be free from fraud. Exchange Act Section 10(b) and Rule 10b-5 apply to all companies and we must be vigorous in ferreting out and punishing wrongdoers wherever they operate . . . . [In the unicorn context] the risk of distortion and inaccuracy is amplified because start-up companies, even quite mature ones, often have far less robust internal controls and governance procedures than most public companies.

SEC Chair Mary Jo White, Keynote Address at the SEC-Rock Center on Corporate Governance Silicon Valley Initiative, SEC (Mar. 31, 2016), *available at* https://www.sec.gov/news/speech/chair-white-silicon-valley-initiative-3-31-16.html [https://perma.cc/L4LE-GFBT].

380. Matt Robinson et al., *WeWork Is Facing SEC Inquiry into Possible Rule Violations,* BLOOMBERG (Nov. 15, 2019), https://www.bloomberg.com/news/articles/2019-11-15/wework-is-said-to-face-sec-inquiry-into-possible-rule-violations [https://perma.cc/VT66-YBG2].

in violation of the Securities Act.[381] The SEC charged Daniel Mattes, the former CEO of identity verification service Jumio, with making false claims about the company's financial results.[382] Mattes settled those allegations in April 2019 for over $17 million.[383] The SEC also charged Theranos, its former CEO Holmes, and its former President Balwani with lying about the Theranos technology while raising hundreds of millions of dollars from investors.[384] Holmes settled with the SEC for $500,000.[385] There were reports that WeWork could face similar scrutiny for violating SEC rules.[386] At this time, however, when a private company is involved, SEC action is the exception and not the rule.[387]

2. The Securities Laws Could Be Amended to Require Companies of a Certain Size to File

Another approach would be to amend current securities laws to require companies to begin reporting once they reach a certain size. At present, the decision to file——to become a publicly traded company, with the constraints entailed thereby——is in the discretion of management. As discussed above, firms historically made an IPO when they needed large amounts of capital, usually for expansion. More recently, companies have gone public in order for employees compensated with equity to "cash out."[388]

381. YourPeople, Inc., Exchange Act Release No. 10429 (Oct. 26, 2017) (SEC Cease and Desist Order), *available at* https://www.sec.gov/litigation/admin/2017/33-10429.pdf [https://perma.cc/M2FN-FJTQ] (fining Zenefits and Conrad for violations of Section 17(a)(2) of the Securities Act, which is substantially the same as Section 10b-5).

382. *See SEC Charges Former CEO of Silicon Valley Startup with Defrauding Investors*, SEC (Apr. 2, 2019), https://www.sec.gov/news/press-release/2019-50 [https://perma.cc/L9YW-22VY] (asserting that Mattes enriched himself at investors' expense by making false claims about Jumio's financial results).

383. *Id.*

384. *See* Theranos, *CEO Holmes, and Former President Balwani Charged with Massive Fraud*, SEC (Mar. 14, 2018), https://www.sec.gov/news/press-release/2018-41 [https://perma.cc/22EB-FMF7] (charging Theranos, Holmes, and Balwani with making numerous false and misleading statements in investor presentations. Holmes settled with the SEC in 2018, paying a $500,000 fine).

385. *Id.*

386. Robinson, *supra* note 380. No reports of scrutiny followed, however.

387. *See* Stavinoha, *supra* note 375, at 189 (noting that there have been few SEC Rule 10b-5 enforcement actions against private companies). The SEC has this power but uses it sparingly. *See* Jean Eaglesham, *Unicorns' Pre-IPO Profit Claims Get Scrutinized*, WALL ST. J. (Sept. 22, 2019), https://www.wsj.com/articles/unicorns-pre-ipo-profit-claims-get-scrutinized-11569172817 [https://perma.cc/6UQY-N6WM] (attributing SEC forbearance to the fact that unicorn investors tend to be big and sophisticated).

388. *See* Richard A. Booth, *Going Public, Selling Stock, and Buying Liquidity*, 2

As suggested above, companies may not need more cash than they can get in the private markets, and therefore may postpone doing an IPO for a long time, perhaps indefinitely. As a result, companies escape the discipline imposed by the public markets.

There are a number of possible ways to think about a firm's size for purposes of requiring filing as a public company. One plausible approach, rooted in contemporary practice, considers the valuation of the enterprise as a whole.[389] The law might require firms valued above a certain amount, perhaps $1 billion, to file. Such a valuation trigger would have the collateral benefit of creating an incentive for companies to operate with lower (more conservative) valuations.[390] More conservative valuations might mean companies take longer to reach the threshold that triggers filing, as the lower numbers might reduce the "hype" surrounding certain companies.[391] The $104 billion valuation reportedly tossed out there by Morgan Stanley[392] while pitching its IPO services certainly did not help curb the excesses at WeWork.

Another size-based possibility would look at the company's "public float" (*i.e.,* the unicorn shares traded on one of the secondary market platforms).[393] Presumably, the risk to investors (if not to all stakeholders) is

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ENTREPRENEURIAL BUS. L. J. 649, 661–63 (2008) (pointing out that "going public . . . permits insiders to cash out of the business [and enables] a company to use equity as compensation").

389. *See* Fan*, supra* note 63, at 605–10 (suggesting that enhanced disclosure might be structured as providing more information on the Form D, making unicorns' restated certificates of incorporation more easily attainable, having a plain English version of the key certificate of incorporation terms, and providing periodic financial information similar to what is provided to unaccredited investors in private placements).

390. Corporate insiders have substantial control in setting valuations. *See* Kevin Kelleher, *Here's the Major Downside of So Many $1-Billion 'Unicorn' Startups*, TIME (April 7, 2015), http://time.com/3773591/unicorn-startups-downside/ [https://perma.cc/YL36-MVJS] (calling private valuations "more art than science"). *See also* Nick Bilton, *Is Silicon Valley in Another Bubble . . . and What Could Burst It?,* VANITY FAIR (Sept. 1, 2015), https://www.vanityfair.com/news/2015/08/is-silicon-valley-in-another-bubble [https://perma.cc/8BJL-RBJT] (noting "[t]his is hubris").

391. *See, e.g.,* Frances Coppola, *WeWork's IPO: The Triumph Of Hype Over Fundamentals* FORBES (Aug. 15, 2019) https://www.forbes.com/sites/francescoppola/2019/08/15/weworks-ipo-the-triumph-of-hype-over-fundamentals/?sh=41e05bfd2f75 [https://perma.cc/8ADP-6N55] (noting that WeWork raised enormous amounts of money and attracted two of the world's biggest banks as an office space leasing company that had never made a profit).

392. Platt & Edgecliffe-Johnson, *supra* note 13.

393. *See Spurring Job Growth Through Capital Formation While Protecting Investors*: *Hearing Before the S. Comm. on Banking, House., & Urban Affairs,* 112th Cong. 15 (2011) (statement of John C. Coffee, Jr., Adolf A. Berle Professor of Law at Colum. L. Sch.) (proposing public reporting if a company's public float exceeds $50 million or the 2000 shareholders threshold is passed); *Hearing Before the S. Comm. on Banking, House., & Urban Affairs,* 112th Cong. 10 (2012) (statement of Jay R. Ritter, Cordell Professor of Finance, Warrington College of Bus. Admin., Univ. of Florida) (suggesting a reporting requirement

magnified by secondary market trades in which investors have little or no opportunity to receive information from the company. Therefore, using those trades as a trigger would make sense.

Some also propose continued exemptions from registration if the companies maintain strict restrictions on transfer or commit to some kind of public disclosure.[394] Such a proposal would maintain the exemption for family-owned and controlled companies[395] that, despite their many stakeholders, do not seem to be beset by the same level of corporate governance problems as this new class of unicorns.[396]

Once the requirement to file is triggered by either the number of shareholders or the company's total valuation, unicorns would be disciplined by the required disclosure and transparency and, perhaps even more importantly, GAAP accounting for actual money earned.[397]

C. New Federal Legislation

A final way to improve unicorn governance may be simply to impose new federal legislation to address it. Perhaps Delaware and its sibling states are not going to act, but recent history suggests that Congress might.[398] High-profile excesses like those reported at Uber, Theranos, Zenefits and now WeWork could put pressure on the government to address the issue.

For example, in 2018, Senator Elizabeth Warren proposed the Accountable Capitalism Act.[399] The act would make all companies with

once a public float amount is exceeded and advocating maintaining the then-500 shareholders cap).

394. Michael D. Guttentag, *Patching a Hold in the JOBS Act: How and Why to Rewrite the Rules that Require Firms to Make Periodic Disclosures*, 88 IND. L.J. 1151, 207–11 (2013).

395. *See* Usha R. Rodrigues, *The Once and Future Irrelevancy of Section 12(g),* 2015 U. ILL L. REV. 1529, 1554–55 (2015) (discussing the stability of a number of family owned/controlled companies).

396. Some examples might include Cargill, Koch Industries, Albertsons, and Deloitte. Certainly, these companies also have issues, but they are substantially more stable than many of the unicorns.

397. *See* Eaglesham, *supra* note 387 (pointing out that going public means that they have to report numbers based on standard accounting rules, which often reveal losses, sometimes huge ones).

398. In the last two decades, Congress has enacted measures related to corporate governance several times. *See, e.g.,* Sarbanes-Oxley Act of 2002, Pub. L. No. 107–204, 116 Stat.745 (among other things, requiring enhanced reporting and certification of company financials and prohibiting loans to executives); Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, H.R. 4173, 111th Cong. (2010) (among other things, requiring companies to offer shareholders a non-binding "say-on-pay" with respect to executive compensation).

399. S. 3348, 115th Cong. (2018). The bill faced strong criticism and did not advance.

annual gross receipts above $1 billion subject to a federal corporate governance regime.[400] The federal regime would, among other things, require the board to consider the interests of all stakeholders, including employees, customers, suppliers, investors, and local communities.[401] Although somewhat narrow and controversial, the proposed act does indicate an interest by some lawmakers in bringing our largest companies under control. Unicorns could be a related target.

Alternatively, a measure like California's Women on Boards law could be imposed at a federal level. A number of European countries have similar measures.[402] Addressing the homogeneity in company decision-making and funding structures would hopefully result in an improvement in all corporate governance, including unicorns. And the improved governance would help protect stakeholders.

Another approach might be to roll back some of the JOBS Act measures. Restoring the 500-holder trigger or ceasing to allow the general solicitation for Rule 506(c) placements might drive more unicorns into the public markets. Still, given other demands upon the federal government's attention, even modest federal legislation to govern unicorns seems unlikely.

IV. CONCLUSION: ANY WILL WORK, NONE SOON

The issue is not that unicorn governance cannot be improved, but that we simply have not taken steps to do so. As the number of unicorns continues to swell, and their impacts are felt by more stakeholders, the need for sound corporate governance may rouse lawmakers to act.

There is little reason, however, to be optimistic that new laws will be passed anytime soon. Reporters at the *Wall Street Journal* are more

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See, *e.g.,* Milton Ezrati, *Senator Warren's Accountable Capitalism Bill Has Big Problems,* FORBES (Feb. 4, 2019), https://www.forbes.com/sites/miltonezrati/2019/02/05/senator-warrens-accountable-capitalism-bill-has-big-problems/#64b1751c471b [https://perma.cc/5NN6-PP3A] (explaining negative unintended consequences of the proposed legislation).

400. S. 3348, 115th Cong. §2(2) (2018) (defining "Large Entity").

401. S. 3348, 115th Cong. §5(c)(1) (2018) (establishing standards of conduct for directors and instructing them to consider various stakeholder interests).

402. *See generally* VERA JOUROVA, European Comm., GENDER BALANCE ON CORPORATE BOARDS > EUROPE IS CRACKING THE GLASS CEILING 7–8 (Jul. 2016) (providing a chart showing which European countries have quotas or other measures requiring or promoting gender diversity on corporate boards); *see also Legislative Quotas Can Be Strong Drivers for Gender Balance in Boardrooms*, EUROPEAN INSTITUTE FOR GENDER EQUALITY, (Jun. 28, 2019), https://eige.europa.eu/gender-statistics/dgs/data-talks/legislative-quotas-can-be-strong-drivers-gender-balance-boardrooms [https://perma.cc/XPM8-4CMV] (reporting that the proportion of women on boards of the EU's largest companies more than doubled between 2010 and 2019).

responsible for uncovering the mischief at WeWork than any of the traditional gatekeepers or regulators. Investment banks, law firms, and some of the world's largest funds did little to discourage the WeWork excesses, and in fact by some reports encouraged them. The SEC received a confidential draft of the WeWork Form S-1 in December 2018. The document, after the SEC had had an opportunity to request revisions, was still riddled with mistakes and misstatements when it was released in August 2019. It is certainly true that the SEC raised a number of questions about the document, but it seems that bad publicity, not the SEC's initiative, scuttled the offering.

In all likelihood, unicorns will continue to lurch through the economy, including the financial markets, for the foreseeable future. There probably will be many more scandals, more lost investment, and more "collateral" damage to stakeholder interests. None of this is entirely new. In the late 19th century, the United States witnessed the rise of enormous "trust" companies that were established by "robber barons." The early 20th century came to understand the dangers of giant, monopolistic entities run by a few individuals, eventually inspiring government "trust-busting" policies. Maybe, someday, unicorns will cause losses of sufficient magnitude to inspire legal reform of their governance. But that is hardly something for which to hope.