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CalPERS v. IAC: Clear Win for Investors Protecting Shareholder Voting Rights

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Last Friday, litigation by the California Public Employees' Retirement System against IAC/InterActiveCorp and its chairman, Barry Diller, achieved a significant victory for shareholder voting rights. After months of contentious litigation, defendants effectively conceded the case by abandoning their plan to entrench Diller's control of the company by issuing a new class of nonvoting stock.

CalPERS v. IAC/InterActiveCorp is a clear win for investors and a powerful illustration of how institutional investors have been successfully using litigation to defend their right to vote on corporate affairs.

For decades, activist corporate founders and controllers have sought ways to entrench their positions atop the corporate hierarchy by granting themselves and other insiders "supervoting rights." Such arrangements, known as "dual-class" or "multi-class" stock structures, diminish the voting power of institutional and individual investors alike, and can distort managerial incentives by providing controllers voting power out of line with their actual economic interests in public companies. This dynamic has worsened in recent years, as several companies have authorized new classes of non-voting stock as a means to allow controllers to monetize their economic interests without reducing their voting control. Given these harmful corporate governance practices, institutional investors are pursuing litigation to halt planned multi-class structures.

The CalPERS suit, which resulted in Diller and IAC's withdrawal of their plan to dilute investors' voting rights through a proposed multi-class arrangement, arose from one of the more egregious attempts in recent memory of insiders seeking to entrench themselves through non-voting shares. Last year, Diller, the controlling shareholder and Chairman of the Board of IAC, attempted to create a new, non-voting class of stock that would solidify his power and ensure his ability to pass control of the business to his heirs. At the time, IAC had Class A common shares that afforded one vote per share, and supervoting Class B shares that had ten votes per share. Through his ownership of Class B shares, Diller owned less than 8% of the company's stock, yet wielded a disproportionate 44% of the company's voting power. However, because IAC used stock for executive compensation and to fund acquisitions, Diller's control over IAC would diminish as the Company made such further issuances of voting stock. By devising a plan to create and distribute new, non-voting Class C stock instead, Diller created a mechanism to solidify his and his heirs' control in perpetuity.

In November 2016, IAC informed investors that the IAC Board of Directors had approved the plan to issue the Class C stock. Within weeks, CalPERS filed a class action suit in the Delaware Chancery Court alleging breaches of fiduciary duty and requesting an order preventing the company from issuing the non-voting stock. CalPERS's complaint in the case highlighted that Diller achieved board approval of the issuance of IAC non-voting stock by threatening to use his voting power to prevent the company from making valuable and necessary acquisitions that used IAC stock as consideration.

By shedding the light of litigation on IAC's non-voting share plan, CalPERS achieved a significant victory for shareholders' core right to vote. This result should make founders and controllers considering copying the trend of non-voting stock issuances think twice, as institutional investors will act decisively to defend and assert their right to vote when faced with these threats. Such protective actions will continue to promote open and responsive capital markets, and the longterm value creation that comes with them.