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Family Firms: Linking the Benefits of Control and Corporate Purpose

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Motivating Question

- Large presence of family-controlled firms in the U.S. – family owned firms make up ~33% of the S&P 500 and ~44–50% of the S&P 1500. See Cheng & Dai, Family Ownership and CEO Turnovers (2013); Villalonga & Amit, Family Control of Firms and Industries (2010).
- Persistent concern that controlling shareholders can expropriate investors.
 - Particularly true for dual class companies with a wedge between ownership and control.
 - And in the U.S., 89% of dual class firms are family owned. See Anderson, Ottolenghi, Reeb, and Savor (2023).
- And yet, there doesn't seem to be much evidence of agency costs in these dual-class family-owned firms.
 - In fact, empirical evidence reveals that investors in dual-class family-firms earn a high risk premium and abnormal positive returns. See Anderson, Ottolenghi, Reeb, and Savor (2023); see also Kachner, Stalk, and Bloch (2012).

How do controlled family firms achieve these successes despite the prospect of agency costs?

Two Novel Explanations

- 1. Controlled family firms may harness corporate purpose to mitigate agency costs. *Cf. Hwang and Lund, Purpose and Nonprofit Enterprise (2025).*
- 2. Controlled family firms may avoid the pathologies of shareholder voting. *Cf. Lund and Talley, Shareholder Democracy and the Rise of Controlling Shareholders (working paper).*

Purpose, Agency Costs, and Family Control



- Family firms tend to be purposeful firms. See, e.g., [PWC Survey of Family Owned Business](#) (2025); Yilmaz et al. (2024)
- Hwang & Lund, **Purposeful Enterprise Theory**: An authentic and specific corporate purpose can serve as a substitute for shareholder control and monitoring.
 - Purpose provides direction for management that is confronting tradeoffs.
 - Purpose can support stakeholder enforcement.
 - Purpose is a powerful motivator.

Therefore, the purpose that accompanies family ownership and control can mitigate agency cost issues inherent in controlled firms.

Controlled Family Firms and the Pathologies of Shareholder Voting



Two trends:

- 1. Increasing importance of voting in corporate law
- 2. Increasing incidence of controlled firms (many of which are family owned).

Our argument is that these two trends are no coincidence - the rise of controlled firms may have to do with the growing weight that is placed on voting in corporate law.

Trend #1: Renewed faith in SH voting to aggregate information & SH preferences



Cleansing

- *Corwin* and progeny elevated an informed, uncoerced, disinterested SH vote into a shield foreclosing meaningful later merits review;

Squeeze-Outs:

- DGCL § 251(h) was amended to allow 50% majority SH approval for two-step squeezeout mergers

Hostile Takeovers

- Control contests are funneled through the ballot box / proxy fights, rather than tender offers (permissive scrutiny of defensive measures)

Universal Proxy

- SEC has imposed a universal-proxy requirement for director elections; no slate voting in contested elections;

Broker Voting

- NYSE Rule 452 narrows “routine” matters in which brokers votes for uninstructed shares of beneficial owners

Retail Voting

- Ongoing experiments with pass-through and mirrored voting protocols that place enhanced weight on formal vote tabulation.

Trend #1 continued

Hon. Leo Strine (Del. Supreme Court in *Corwin*):

- “Delaware corporate law has long been **reluctant to second-guess** the judgment of a disinterested stockholder majority....”
- “[T]he disinterested equity owners—**can easily protect themselves** at the ballot box by simply voting no”
- “[T]he stockholders **control their own destiny** through informed voting”

Prof. Jon Macey:

- “[A]n informed shareholder vote constitute[s] a **final, conclusive and determinative** demonstration of the fairness of a transaction....”
- “[C]ourts should **not substitute their own business judgment** for that of the shareholders...”

Profs. Oliver Hart & Luigi Zingales

- Company and asset managers should pursue policies consistent with the preferences of their investors. **Voting by shareholders on corporate policy is one way to achieve this.**

Elon Musk:

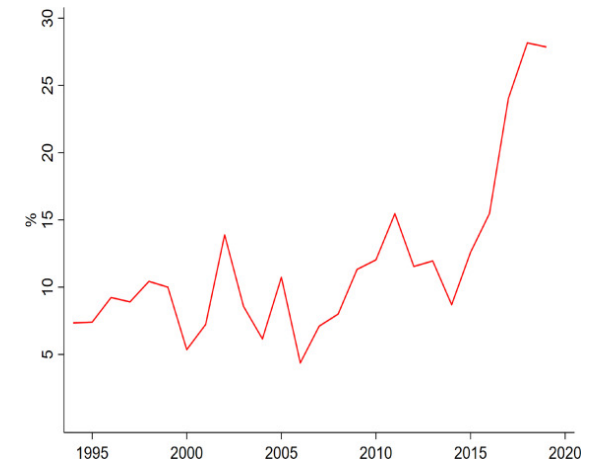
- “[S]hareholders should **control company votes, not judges**”
- “I recommend incorporating in Nevada or Texas if you prefer **shareholders to decide matters**”

Trend #2: The Rise of Controllers

Takes multiple forms

- Dual Class Capital Structures:
 - While overall prevalence is still modest (around 10% of U.S. public firms, *IPO flow* has increasingly featured dual-class structures—e.g., now over 20% of U.S. IPOs in 2020 are dual-class (and ~60% of IPO capital raised).
- Amassing/retaining significant block-holdings
 - Public companies with at least one >5% SH increased from ~60% to ~79% from 2001 - 2015
- Contractual Control devices
 - Board nomination rights in ~ 25% of IPOs
 - Contractual veto rights in ~ 7%
 - Likely increased since DGCL § 122(18)

Dual Class IPO Structures
(Aggarwal et al., 2022)



Our core argument...

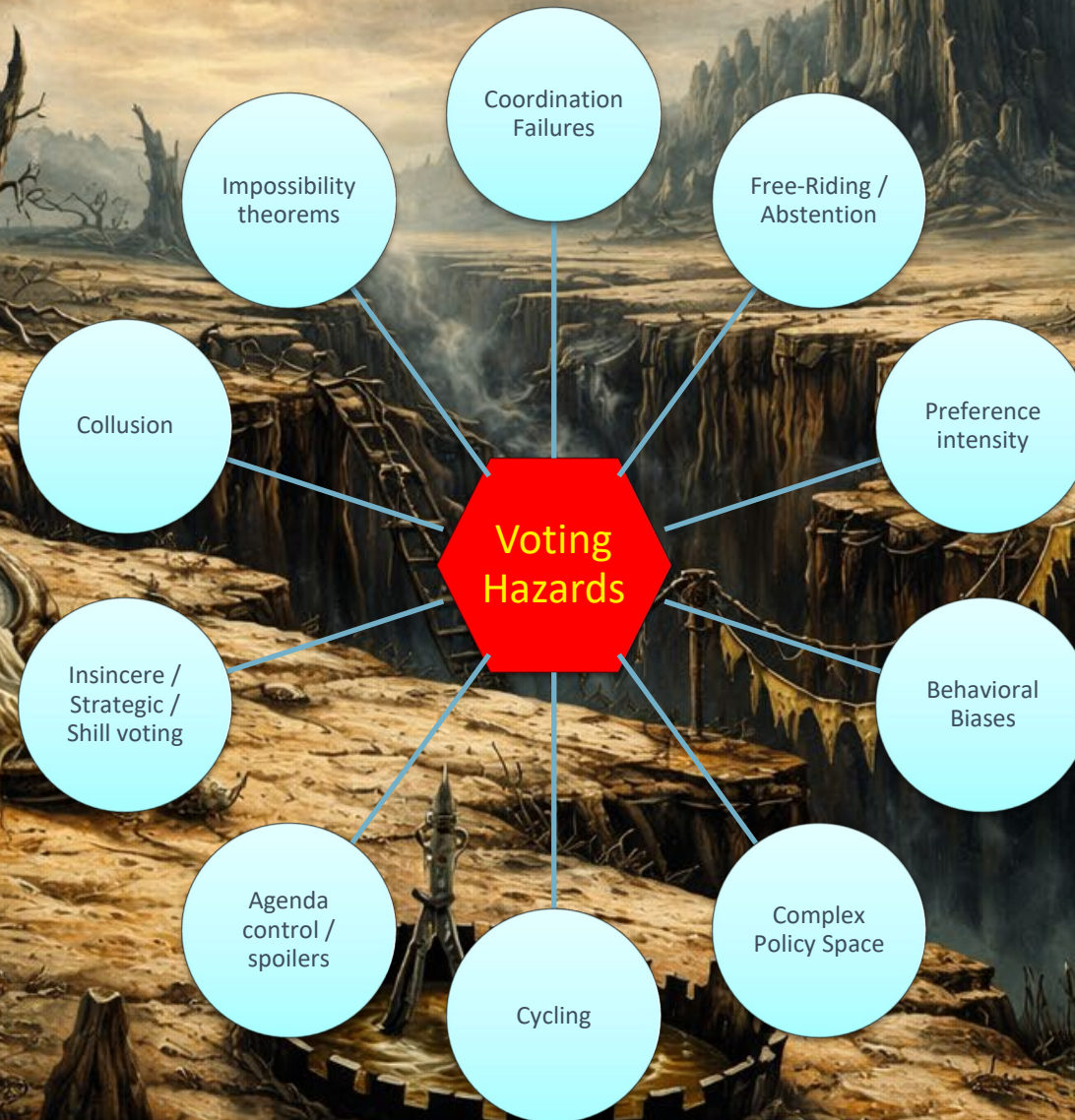
- Trend #1 and Trend #2 have an unappreciated relationship (at least for many firms):



- Why's that?
 - Courts / corporate governance pundits / law and finance commentators have not fully appreciated how complicated, unpredictable, opaque, and incoherent shareholder voting can be as a preference/information aggregation mechanism

Top-10 List of Voting Hazards and Pitfalls

(familiar to social choice theorists, but frequently neglected by law & finance types)



Cycling and Agenda Control

Condorcet Paradox



	SH1	SH2	SH3
Status Quo (SQ)	-\$100	0	+\$100
Option A	+\$100	-\$100	\$0
Option B	\$0	+\$100	-\$100

$A > B > SQ$ $B > SQ > A$ $SQ > A > B$

- One-on-one Contests: No Consistent Winner Emerges
 - 1) **A vs. SQ**: SQ Wins by 2-1 margin (SH2 & SH3 in majority)
 - 2) **B vs. SQ**: B Wins by 2-1 margin (SH1 & SH2 in majority)
 - 3) **A vs. B**: A Wins by 2-1 margin (SH1 & SH3 in majority)
- Multi-Stage/Runoff Contests: If voting is sincere at all stages...
 - a) **A vs. SQ, winner faces B**; B prevails. Favored by SH2
 - b) **B vs. SQ, winner B faces A**; A prevails. Favored by SH1
 - c) **A vs. B, winner faces SQ**; SQ prevails. Favored by SH3



Non-Transitive Cycling

Even more problematic!

- Players may vote strategically in the first stage to rig the finals (e.g., for A vs. SQ in 1st stage, SH3 insincerely votes for their less preferred option A)
- Players may engage in costly efforts to set agenda;

Gibbard-Satterthwaite Theorem

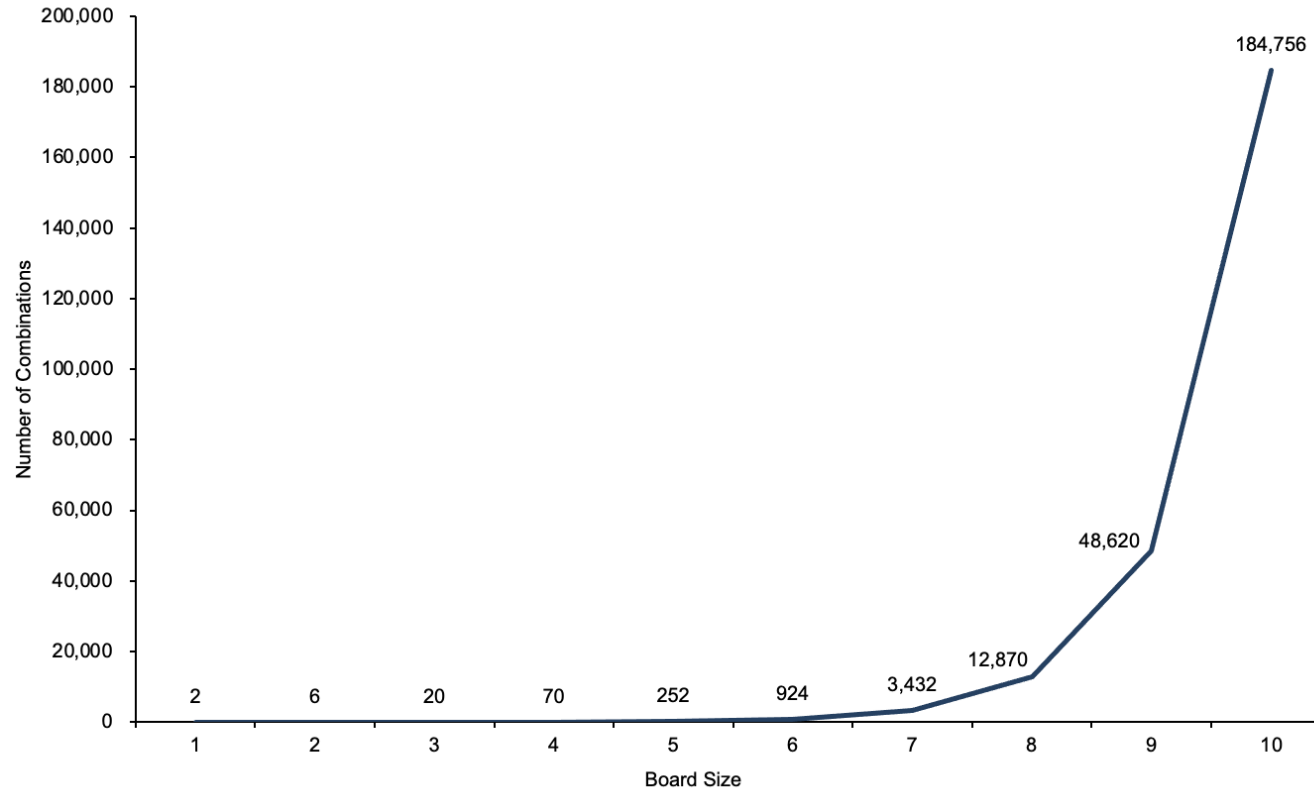


- Cousin to Arrow's theorem that focuses on voting protocols:
 - Gibbard (1973); Satterthwaite (1975); see also Dumett (1984); Sen (2001).
- In any deterministic voting regime with unrestricted voter preferences, at least one of the following conditions must hold:
 1. The policy choice set contains no more than 2 alternatives/candidates;
 2. The regime is not straightforward (i.e. there is no single categorically best strategy that does not depend on other voters' preferences / behavior = insincere voting);
 3. The regime is a dictatorship; i.e., a single voter fully determines the winner
- **In other words:** If there are ≥ 3 possible policy alternatives, and you want your voting protocol to be stable & consistent (e.g., non-random / no influence costs / sincere voting / no spoilers), **then it must be a dictatorship (either outright or *de facto*).**

How Pathologies Can Manifest: Director Elections



Possible Choice Combinations After the Universal Proxy Rule



Note: The figure shows the number of possible choice combinations faced by a stockholder after the Universal Proxy Rule, assuming that there is a full incumbent slate and full challenger slate, and that the stockholder votes to elect the maximum number of candidates allowed, which equals the board size. For example, when the board size is 7, the number of possible choice of combinations is equal to 3,432.

Bottom line: rise of controllers + importance of voting are related trends

- Rise of corporate controllers are an unsurprising structural response to the inability stockholder voting to bear the considerable weight have increasingly heaped upon it
 - Because, at least for some certain firms, corporate dictators are **the only pressure-relief valve available to avoid costly/unpredictable voting shenanigans**



Implications for Family Firms



- Controllers can sometimes introduce real downsides (e.g., agency costs, tunneling, etc.). But even so, blind faith in voting can sometimes be costlier!
- When law & regulation romanticize voting, they inadvertently increase the private & collective returns to ensuring coherence through dictatorship (notwithstanding its own costs)
 - **Controlled family firms avoid these problems by appointing a dictator that brings coherence to corporate decision making.**

Conclusion

Two additional (and novel) explanations for the success of controlled family firms in the marketplace:

1. Controlled family firms harness the benefits of purposeful enterprise
2. Controlled family firms benefit from mitigating pathologies related to voting



Thank you!

Coordination Failures (cash equiv. welfare payoffs)



	SH1	SH2	SH3
Status Quo (SQ)	\$0	\$0	\$0
Option A	\$100	\$100	\$100

- Assume the SHs have perfect information about the above payoffs
- Value-maximizing choice is Option A (\$300 versus \$0 in welfare value)
- **And yet:** There exist voting equilibria that fail to get us to A:
 - 1 pure-strategy equilibrium where all vote in favor of A; A Wins
 - 1 pure-strategy equilibrium where all vote in favor of SQ; SQ Wins
 - 3 pure-strategy equilibria where 2 SHs vote for A and one votes for SQ; A Wins
- **Mo' voters, mo' problems:** E.g., assume 5 SHs all with these identical preferences:
 - 22 pure-strategy equilibria, 6 selecting SQ and 16 selecting Option A
 - Continuum of (partial) mixed strategy equilibria, some selecting SQ and others selecting A
- ***But “most” equilibria (and perhaps the most intuitive ones) lead to the optimal outcome...***

...so that's kinda good, right?

Preference Heterogeneity & Intensity



	SH1	SH2	SH3
Status Quo (SQ)	\$0	\$0	\$0
Option A	\$100	\$100	-\$500

- Assume again that SHs have perfect information about these payoffs
- Socially maximizing choice flips to SQ (\$0 versus -\$300)
- **And yet:** The voting equilibria DO NOT CHANGE MUCH
 - 1 pure-strategy equilibrium where all vote in favor of A: A Wins
 - 1 pure-strategy equilibrium where all vote in favor of SQ: SQ Wins
 - 1 pure-strategy equilibrium where SH1 & SH2 vote for A and SH3 votes for SQ: A Wins
- **Holding aside its coordination challenges, preference aggregation by voting struggles to accommodate differential intensities of preferences**

Information Aggregation & Rational Abstention

The “Swing Voter Curse”



Nature

“Good” State

	SH1	SH2	SH3
Status Quo (SQ)	\$0	\$0	\$0
Option A	\$100	\$100	\$100

“Bad” State

	SH1	SH2	SH3
Status Quo (SQ)	\$0	\$0	\$0
Option A	-\$100	-\$100	-\$100

- The “Good” and “Bad” states each occur with 50% probability *ex ante*.
- Voters have three strategies {SQ, A, abstain}; strict majority required to switch from SQ to A;
- All SHs receive independent signals about whether “Good” or “Bad” state will emerge
 - SH1 and SH2’s signals are 90% accurate; SH3’s signal is 60% accurate.
 - Each SH bears a small individual cost of \$5 to observe their signal and cast vote
- **1st Best Solution:** All SHs use signals & vote sincerely. Exp. net joint gain = \$125.40 - \$15 = **\$110.40**
 - NB: Instance of Condorcet Jury Theorem ⇔ Use all available cost-justified signals
- **“Best” Equilibrium:** SH1 & SH2 vote sincerely & SH3 abstains. Exp. net gain = \$120 - \$10 = **\$110**
 - Why abstain? SH3’s vote matters only as tie-breaker; voting benefits SH3 by \$3.60, but costs \$5
 - The externality problem grows larger with more SH3s and/or with smaller SH3 stakes
 - *NB: In 2024, participation rates in SH voting were 78% for institutions and 30% for retail investors*

How might SH voting be reformed to dampen voting pathologies?



- Long-shots (at best):
 - Pass-Through Voting: Actually amplifies the collective problem (though empirical study of pass-through experiments can help diagnose direction/magnitude of problem)
 - Mirror Voting: More promising, but “rulifies” the Swing-Voter Curse while sharpening strategic manipulation incentives for those who choose to remain active voters
- What might work better?
 - Better information / tailored / unbiased / competitive proxy advice
 - Super-Majority voting (e.g, Caplin & Nalebuff’s 64% mean voter theorem; status-quo bias?)
 - Ranked Choice Voting / Condorcet Winners (Maskin; existence/top-cycles?)
 - Quadratic/Square-Root Voting (Weyl/Posner; securities pricing?/coalition proof?)
 - **Voting-Auction Hybrids: Vickrey-Groves-Clark (VGC) mechanisms (can say more in Q/A)**
- Side Note: Some of these are cumbersome fits with traditional corporate governance models
 - But nearly all of them could be implemented with SH agreements under DGCL § 122(18)!
 - See Lund & Talley, “Should Corporate Law Go Private?” (2026) (yes, a pathetic skill)