SAFEGUARDING SHAREHOLDERS WHEN THE SUPERSTAR CEO BECOMES A LIABILITY

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I. INTRODUCTION

Elon Musk is one of a class of high-profile CEOs and entrepreneurs who have become synonymous with the companies they lead. Various modifiers are used to describe these corporate leaders—iconic,[1] narcissist,[2] rock star,[3] celebrity,[4] cults of personality[5]—but the gist is the same. John Carreyrou, the *Wall Street Journal* investigative journalist whose reporting directly contributed to the fall of one such superstar CEO, Theranos's Elizabeth Holmes,[6] calls it "the myth of the brilliant founder."[7] Similarly, in his book detailing the arc of Travis Kalanick as CEO of Uber, Mike Isaac of the *New York Times* observes that "founder

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1. Tom C.W. Lin, *The Corporate Governance of Iconic Executives*, 87 NOTRE DAME L. REV. 351, 351 (2011).

2. Charles A. O'Reilly et al., *When 'Me' Trumps 'We': Narcissistic Leaders and the Culture They Create*, 7 ACAD. OF MGMT. DISCOVERIES 3 (2021), https://www.gsb.stanford.edu/faculty-research/publications/when-me-trumps-we-narcissistic-leaders-cultures-they-create.

3. Jennifer S. Fan, *The Landscape of Startup Corporate Governance in the Founder-Friendly Era*, 18 N.Y.U. J.L. & BUS. 317, 353–54 (2022).

4. Agustin Ferrari Braun, *The Elon Musk Experience: Celebrity Management in Financialised Capitalism*, 14 CELEBRITY STUD. 602, 602 (2022).

5. Gabriel Perna, *Theranos, Elizabeth Holmes and Cult of Personality CEOs*, CHIEF EXEC., https://chiefexecutive.net/john-carreyrou-theranos-elizabeth-holmes/2/ (last visited Jan. 24, 2024).

6. *See generally* JOHN CARREYROU, BAD BLOOD: SECRETS AND LIES IN A SILICON VALLEY STARTUP (2018) (documenting the rise and fall of Holmes as CEO of Theranos).

7. Perna, *supra* note 5; *see also* ELIOT BROWN & MAUREEN FARRELL, THE CULT OF WE: WEWORK, ADAM NEUMANN, AND THE GREAT STARTUP DELUSION 56 (2021) (referring to "the cult of the founder").

worship" in Silicon Valley was a natural evolution from the counterculture in the Bay Area during the 1960s.[8] These corporate leaders speak passionately, in broad platitudes, and their public statements go well beyond simply product development, earnings reports, or market share. Instead, they extol the positive benefits that will inure to society from the products or services their company is providing.[9] In other words, these leaders often sound more like politicians leading a movement than CEOs leading a corporation. There is little doubt that startups can benefit from this myth, as Silicon Valley has a proclivity to search constantly for the next Steve Jobs—someone who not only will grow a successful and highly profitable business, but also will somehow change the world.

Problems arise when the same celebrity CEO, through personal misconduct, ill-considered public statements, or simply ineffective management, overstays his or her welcome and becomes more damaging than beneficial to the corporation. Politicians are accountable to the voters who elect them. But the equivalents of John and Jane Q. Public in the corporate structure—the shareholders—typically are not able to directly register their displeasure as to the CEO's performance, even though they are the constituents most harmed when that performance fades. Who, then, will hold the superstar CEO accountable?

Under basic principles of corporate governance, the CEO answers to the board of directors, which has the power to appoint corporate officers, set their compensation, and terminate them for poor performance or misconduct that puts the corporate interests at risk.[10] However, when CEOs have risen to a level of prominence that goes well beyond simply their position as leader of a company,

8. MIKE ISAAC, SUPER PUMPED: THE BATTLE FOR UBER 75 (2019).

9. Typically, the focus is on the societal progress that will result from the disruptive impacts of the company's work (i.e., blood-testing, shared workspace, ride-sharing, or electric vehicles). In recent times, this has shifted to the altruistic benefits of capitalism itself: if only the founder and CEO can amass as much personal wealth as possible, that fortune will be put to good use solving the world's biggest problems, and we all will be better off for it. *See* Gideon Lewis-Kraus, *Sam Bankman-Fried, Effective Altruism, and the Question of Complicity,* THE NEW YORKER (Dec. 1, 2022), https://www.newyorker.com/news/annals-of-inquiry/sam-bankman-fried-effective-altruism-and-the-question-of-complicity.

10. Generally, both the Delaware General Corporation Law ("DGCL") and the Model Business Corporation Act ("MBCA") give the board of directors broad power over the internal affairs of the corporation, which includes the ability to hire and fire corporate officers. *See infra* pt. II.

there are elements that are likely to make it more difficult for the board to act when called upon to check the behavior of those same CEOs.[11] If internal controls fail to hold officers accountable, that responsibility may fall to external actors. Shareholders do have the power to sue officers, directors, or both on behalf of the corporation for breach of fiduciary duty, and regulators should function as a backstop when corporate boards have failed to properly oversee the actions of their officers. However, by the time matters end up in court, it is often too late for shareholders to receive the full value of their investment in the corporation, much less see the business in which they invested achieve the great heights that the CEO envisioned.

Part II of this Article will build upon previous research to develop a character profile of the superstar CEO. Part III considers the board's role in overseeing the CEO, which is based in both the fiduciary duty of care and, if the directors are conflicted, the duty of loyalty. It also delves into the evolution over the past few decades concerning how startups are financed, which has made it more challenging for board members to appropriately exercise the duties of oversight that they owe to shareholders and the corporation. Part IV of this Article turns to the role of the courts, most commonly through the shareholder derivative suit, and regulators, specifically the Securities and Exchange Commission ("SEC"), in protecting shareholders when boards fail to act. Because these external checks may not be effective, it is crucial for corporate boards to institute strong governance practices to ensure that they are not hypnotized by the siren of the superstar CEO.[12]

This Article is not intended to be critical of strong entrepreneurial leadership. Recent history has witnessed the impact of numerous visionary business leaders such as Bill Gates, Jeff Bezos, Steve Jobs, and—yes—Elon Musk, who, through the force of their ideas, skillful management, and power of personality, have changed the way we live and work. Rather, this Article is

11. Fan, *supra* note 3, at 354.

12. *See* Noam Wasserman, *FTX and the Problem of Unchecked Founder Power*, HARV. BUS. REV. (Dec. 1, 2022), https://hbr.org/2022/12/ftx-and-the-problem-of-unchecked-founder-power (noting that for each degree of control a founder retains in a startup, the company's value is lower by an average of twenty percent); Brent T. Wilson, *Theranos and the Tale of the Disappearing Board of Directors*, IDAHO ST. BAR (Mar. 11, 2020), https://isb.idaho.gov/blog/theranos-and-the-tale-of-the-disappearing-board-of-directors/; Mike Myatt, *Rogue CEOs and Board Accountability,* N2GROWTH, https://www.n2growth.com/rogue-ceos-board-accountability/ (last visited Feb. 13, 2024).

intended to use other celebrity CEO founders— "wannabe world changers"—as cautionary tales to stress the importance of traditional corporate governance principles in protecting the investing public. The success of the companies that Elon Musk leads, and more importantly, the lofty societal goals for which those companies are the vehicles, depend in great part upon his and his boards' willingness to work within those guardrails, rather than crash through them.[13]

II. CHARACTER PROFILE OF THE SUPERSTAR CEO

Although all entrepreneurs are—or should be—convinced by the power of their ideas and the potential for their business's success, not every startup founder rises to the realm of the superstar. Indeed, there are several characteristics that these leaders tend to share. First, they are confident in their vision of their firm, often to the point of overconfidence, which ultimately can plant the seeds of their downfall. Second, they are charismatic, which attracts both investment from venture capitalists and media attention that cultivates their image. Third, they tend to become viewed as indispensable to their company's success, and indeed interchangeable with the company itself, such that it becomes difficult to imagine the firm existing without them. And fourth, they are focused single-mindedly on business success and have little time or regard for corporate governance rules that are designed to provide internal checks and balances. Each of these characteristics contributes to the oversight difficulties outlined later in this Article. Elon Musk displays all of these attributes.[14] They have helped grow his companies and made him one of the wealthiest and most recognizable figures in the world. However, they also have contributed to some of the legal difficulties in which he and his businesses have been mired over the past few years.

13. *Cf.* Faiz Siddiqui, Rachel Lerman & Jeremy B. Merrill, *Teslas Running Autopilot Involved in 273 Crashes Reported Since Last Year*, WASH. POST (June 15, 2022, 4:50 PM), https://www.washingtonpost.com/technology/2022/06/15/tesla-autopilot-crashes/.

14. Braun, *supra* note 4, at 602 ("Musk's companies (including car manufacturer Tesla, aerospatial enterprise SpaceX, construction service The Boring Company, and neurotechnological developer Neuralink) cannot be separated from his celebrity image of [] visionary genius.").

A. Overconfidence

One common characteristic among celebrity founder CEOs is overconfidence.[15] Certainly, a strong belief in one's own personal abilities, as well as the market power and potential societal benefits of the products and services one's firm is creating, is an essential quality of a successful founder CEO. If the CEO does not have faith in the business's ability to deliver on its promises, then it is difficult to see how they can attract either investors or talented employees who are willing to work the long hours required to build a successful company.[16] Indeed, high confidence can more than double a CEO candidate's chances of being chosen by a board for the position.[17] And among founders, the data actually are mixed, with some studies suggesting that heightened confidence is a necessary characteristic to spur innovation and can improve employee loyalty and relationships with suppliers, and others concluding that it is more likely to lead to biased decision-making.[18] At any rate, studies have shown repeatedly that entrepreneurs are brimming with confidence about all sorts of things—the likelihood of the success of their ventures, their ability to prevent bad outcomes, and even their own lifespans![19]

However, the confidence that is necessary for someone to be attracted to entrepreneurship in the first place can prove disastrous when the CEO succumbs to overconfidence, both in their own decision-making abilities and in the firm's likelihood of

15. Lin, *supra* note 1, at 374–76; Troy A. Paredes, *Too Much Pay, Too Much Deference: Behavioral Corporate Finance, CEOs, and Corporate Governance*, 32 FLA. ST. U. L. REV. 673, 689–90 (2005).

16. Jayne W. Barnard, *Narcissism, Over-Optimism, Fear, Anger, and Depression: The Interior Lives of Corporate Leaders*, 77 U. CIN. L. REV. 405, 413–14 (2008) ("[O]ver-optimism, at least in the short run, is often essential to leadership success. That is, to be effective as motivators and spokesmen for their companies, CEOs must be—or at least must seem to be—optimistic.").

17. Elena Lytkina Botelho, Kim Rosenkoetter Powell, Stephen Kincaid & Dina Wang, *What Sets Successful CEOs Apart*, HARV. BUS. REV. (2017), https://hbr.org/2017/05/what-sets-successful-ceos-apart.

18. Priscilla S. Kraft, Christina Günther, Nadine H. Kammerlander & Jan Lampe, *Overconfidence and Entrepreneurship: A Meta-analysis of Different Types of Overconfidence in the Entrepreneurial Process*, 37 J. BUS. VENTURING 4 (July 2022); Kenny Phua, T. Mandy Tham & Chishen Wei, *Can Being Overconfident Make You a Better Leader?*, HARV. BUS. REV. (June 18, 2018), https://hbr.org/2018/06/can-being-overconfident-make-you-a-better-leader; Jordan Whitehouse, *The Curse of Overconfidence*, SMITH BUS. INSIGHT (May 10, 2023), https://smith.queensu.ca/insight/content/The-Curse-of-Overconfidence.php.

19. James Surowiecki, *Epic Fails of the Startup World*, THE NEW YORKER (May 19, 2014), https://www.newyorker.com/magazine/2014/05/19/epic-fails-of-the-startup-world.

success.[20] Such overconfidence can be particularly dangerous when coupled with deferential employees, investors, and, as has become more common in the past couple of decades, board members.[21] Indeed, a recent meta-analysis of the conflicting research posits "that the three types of overconfidence (i.e., overprecision, overestimation, and overplacement) generally stimulate individuals to engage in entrepreneurship but impair their performance after the venture has been founded."[22] This makes sense, as many of the superstar CEOs who have led once-promising companies down the wrong path have suffered the effects of overconfidence in the post-launch phase.

A recent and highly publicized example of CEO overconfidence was Elizabeth Holmes of Theranos. A Stanford dropout who nurtured dreams of becoming an entrepreneur since she was a little girl,[23] Holmes founded Theranos with the lofty goal of changing the medical industry through the development of blood-testing technology that would make the process of diagnosing serious medical conditions earlier, easier, and more efficient.[24] She was bolstered in her efforts when, using "just the right mix of contrition and charm," she managed to survive an early attempt by the board to replace her as CEO based on their suspicions that she was overstating the abilities of Theranos's technology and, correspondingly, its revenue projections.[25] She focused on the societal importance of Theranos's work, telling employees, for example, that one testing vehicle on which the company was working was "the most important thing humanity has ever built."[26] The financial press fell hard for Holmes,[27] and by the age of 30, she became the youngest self-made female billionaire (on paper) in the

20. Robert Paul Singh, *Overconfidence: A Common Psychological Attribute of Entrepreneurs Which Leads to Firm Failure*, 23 NEW ENGLAND J. ENTREPRENEURSHIP 25, 28–29 (2020).

21. Lin, *supra* note 1, at 376; *see also infra* pt. II (discussing shift in power to corporate founders).

22. Kraft et al., *supra* note 18. "Overprecision refers to excessive certainty regarding the accuracy of your beliefs. Overestimation involves overemphasizing your actual ability, performance, level of control or chance of success. Overplacement is the exaggerated belief that you are better than others." Whitehouse, *supra* note 18.

23. CARREYROU, *supra* note 6, at 9.

24. Perna, *supra* note 5.

25. CARREYROU, *supra* note 6, at 51.

26. *Id.* at 103.

27. *Id.* at 208–09.

world.[28] She convinced herself, and many others—the science be damned—that a pinprick of blood inserted into a portable machine really could run a full range of diagnostic tests that would tell the user the likelihood of contracting a wide range of serious illnesses. Her overconfidence in Theranos's mission and her own abilities, however, caused Holmes to habitually refuse to listen to, ignore, or cover up bad news about the company's blood-testing technology,[29] and/or chastise or fire employees who brought that news to her.[30] The very optimism and confidence that made Holmes so attractive undermined the company she was charged with leading.[31]

Elon Musk has not lacked confidence. Indeed, his certainty in his own abilities and his companies' success has manifested itself in a number of different ways. Bloomberg reporter and Musk biographer Ashlee Vance put it bluntly: "I think Elon thinks he cannot fail. If there's anything Elon believes in, it's himself."[32] There is no doubt that Musk's confidence has pushed his ventures, and their employees, to newer and greater heights. His public statements have, on occasion, wildly overstated when certain goals might be achieved, such as when self-autonomous driving cars would become ubiquitous[33] and how soon people would be able to travel to Mars.[34] Musk simply is not fazed by failure: he "embraces astonishing amounts of present-day risk in the rational assumption of future gains."[35] Even his own compensation plan at Tesla shows his willingness to bet on his own leadership. The structure of the arrangement—performance-based equity incentives—is quite common, but it is the targets—a "market value [of at least] $100 billion by 2028, otherwise Musk receives nothing,

28. Matthew J. Belvedere, *Fear of Blood Inspired Youngest Female Billionaire*, CNBC (Sept. 29, 2015, 11:19 AM), https://www.cnbc.com/2015/09/29/fear-of-blood-inspired-youngest-female-billionaire.html.

29. *See, e.g.*, CARREYROU, *supra* note 6, at 155–59, 227.

30. *Id.* at 37, 142–43.

31. Don A. Moore, *Perfectly Confident Leadership*, 63 CAL. MGMT. REV. 58, 61 (2021).

32. Peter Kafka, *"I Think He's Battling with His Own Self": Inside Elon Musk's Brain*, VOX (Nov. 15, 2022, 3:10 PM), https://www.vox.com/recode/2022/11/15/23460730/elon-musk-twitter-tesla-biography-ashlee-vance-peter-kafka-column.

33. Christopher Cox, *Elon Musk's Appetite for Destruction,* N.Y. TIMES MAG. (Jan. 17, 2023), https://www.nytimes.com/2023/01/17/magazine/tesla-autopilot-self-driving-elon-musk.html.

34. Lisa Eadicicco, *Elon Musk Just Made These 5 Bold Claims About the Future*, TIME (June 2, 2016, 10:43 AM), https://time.com/4354864/elon-musk-mars-driverless-cars-apple-tesla-spacex/.

35. Cox, *supra* note 33.

with further targets . . . on up to $650 billion"—that show hubris.[36] But Musk's overconfidence, while a major part of his success, may have some costs as well, such as the diversion of resources from Tesla and SpaceX that was brought on by his 2022 purchase of, and continued leadership of, Twitter.[37] Running a social media company is nothing like building electric vehicles or rockets, but Musk's confidence in his own ideas and work ethic lead him to take on new challenges that may have deleterious effects on his existing ventures.

B. Charisma

A second common characteristic among superstar CEOs is charisma.[38] "Society is easily wooed by a charismatic leader with a big vision. It's hard to resist an optimist who promises a lucrative future—a messiah for profits lying just over the next horizon."[39] It is well-accepted that corporate boards often overrate charisma when searching for outside leadership, irrationally placing too much emphasis on the CEO's ability to impact the company's bottom line.[40] However, charisma is often a key component of a founder's ability to survive beyond a startup business's formative stages. Charisma and confidence are, of course, related, as "[i]ndividuals are more likely to follow a CEO who shows self-confidence and appears to be in control."[41] But the importance of charisma extends beyond a CEO's decision-making or managerial skills; rather, the leader's likability and popularity come to define the company.[42] Charisma helps attract capital from venture capitalists and angel investors in early rounds of funding, which in

36. Alex Edmans, *Why Elon Musk's Compensation Plan Wouldn't Work for Most Executives*, HARV. BUS. REV. (2018), https://hbr.org/2018/01/why-elon-musks-compensation-plan-wouldnt-work-for-most-executives.

37. *See, e.g.*, Brett Ryder, *Will Elon Musk-Owned Twitter End Up as a "Deal From Hell"?*, ECONOMIST (Oct. 11, 2022), https://www.economist.com/business/2022/10/11/will-elon-musk-owned-twitter-end-up-as-a-deal-from-hell.

38. *See, e.g.*, RAKESH KHURANA, SEARCHING FOR A CORPORATE SAVIOR x (2002) ("[T]he kind of candidate considered qualified for the role of corporate savior is one who is thought to possess 'charisma.'").

39. BROWN & FARRELL, *supra* note 7, at 392.

40. KHURANA, *supra* note 38, at xi (citing Enron's Jeffrey Skilling as a cautionary example).

41. Paredes, *supra* note 15, at 730.

42. Patricia Sánchez Abril, *The Evolution of Business Celebrity in American Law and Society*, 48 AM. BUS. L.J. 177, 200 (2011).

turn attracts media attention, creating a self-fulfilling cycle.[43] Some have pointed to the rise of the 24-hour business network in the 1980s and 1990s, and the subsequent onset of social media in the 2000s, for this newfound focus on the CEO's personality.[44] In contrast to most of the twentieth century, when most CEOs were respected corporate statesmen who eschewed public attention,[45] many modern corporate leaders have their own cult-like followings. While this has benefits for both corporations and CEOs themselves, it also shines a spotlight on the CEO's private life.[46] The CEO's own personal failings, bad behavior, or even health problems become imputed to the corporation and have the potential to damage the brand.[47]

During Theranos's rise to Silicon Valley unicorn,[48] much of the interest in the company was tied to interest in Elizabeth Holmes herself. She was encouraged to "dress the part" to look more like Steve Jobs, and she began wearing a black turtleneck and black slacks to work most days.[49] Holmes often relied on her own story of having a fear of blood and needles as a little girl and having lost family members prematurely to bolster her claims that Theranos's blood-testing technology would change the world.[50] Her charm,

43. Two-time Pulitzer Prize finalist Sebastian Mallaby has noted that "without some degree of that vision/storytelling ability, you're unlikely to get anywhere. So I wouldn't be too negative about charisma. But charisma without the substance? Then that is a problem." Bill Borrows, *Are We All Just Suckers for Charismatic Founders?*, MGMT. TODAY (May 4, 2022), https://www.managementtoday.co.uk/just-suckers-charismatic-founders/long-reads/article/1750807.

44. Sánchez Abril, *supra* note 42, at 198–201; Patricia Sánchez Abril & Ann M. Olazábal, *The Celebrity CEO: Corporate Disclosure at the Intersection of Privacy and Securities Law*, 46 HOUS. L. REV. 1545, 1552–53 (2010).

45. Sánchez Abril, *supra* note 42, at 186.

46. *Id.* at 202.

47. Tom C.W. Lin, *Executive Private Misconduct*, 88 GEO. WASH. L. REV. 327, 344–46 (2020).

48. Venture capitalist Aileen Lee coined the term "unicorn" in 2013 to refer to a startup with a valuation of $1 billion or greater. Aileen Lee, *Welcome to the Unicorn Club: Learning from Billion-Dollar Startups*, TECHCRUNCH (Nov. 2, 2013, 2:00 PM), https://techcrunch.com/2013/11/02/welcome-to-the-unicorn-club/.

49. Vanessa Friedman, *The Rise and Fall of Elizabeth Holmes and the Black Turtleneck*, N.Y. TIMES (Mar. 16, 2018), https://www.nytimes.com/2018/03/16/fashion/elizabeth-holmes-black-turtleneck-theranos.html. Holmes is certainly not the only startup CEO who has sought to emulate Jobs. *See* BROWN & FARRELL, *supra* note 7, at 56 ("Distinctive sartorial choices, like the Steve Jobsian black turtlenecks, were a plus. A little bit of crazy never hurt. Founders needed to inspire.").

50. Nick Bilton, *Exclusive: How Elizabeth Holmes's House of Cards Came Tumbling Down*, VANITY FAIR (Sept. 6, 2016), https://www.vanityfair.com/news/2016/09/elizabeth-holmes-theranos-exclusive ("Finally, it seemed, there was a female innovator who was

attractiveness, and seemingly altruistic vision for Theranos wowed venture capitalists and attracted board members who themselves had enormous successes in government, business, academia, and the military. Oddly, however, none of the Theranos board members themselves had experience with the science of blood tests, and none of the venture capitalist firms that had invested in Theranos had specific expertise in healthcare.[51] Holmes cultivated her image carefully, elucidated her vision for Theranos so eloquently, and cloaked the problems with the blood-testing technology with such secrecy that she was able to reach enormous heights—until, of course, internal whistleblowers and a tenacious *Wall Street Journal* investigation brought her down.[52] Even long after Holmes's fall from grace and her January 2022 conviction for defrauding investors, for which she is now serving an eleven-year prison sentence,[53] Holmes's charm was on full display in a *New York Times* profile about her domestic life as she prepared to enter prison.[54] Although the *Times* was widely criticized in the press for that piece,[55] it is proof that the natural charisma of the celebrity CEO remains even long after the gig is up.

Other celebrity CEOs have ridden the wave of personal fame to the benefit of both themselves and the companies they were leading, only to see both fall due to their own bad behavior. Uber CEO Travis Kalanick had previous experience as a startup CEO.[56]

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indeed able to personify the Valley's vision of itself—someone who was endeavoring to make the world a better place.").

51. CARREYROU, *supra* note 6, at 274.

52. *The Wall Street Journal* has compiled a complete history of its coverage and investigation of Theranos's downfall, led by investigative reporter John Carreyrou. Michael Siconolfi, *Elizabeth Holmes to Report to Prison: A History of the WSJ Theranos Investigation*, WALL ST. J. (May 26, 2023, 8:33 PM), https://www.wsj.com/articles/elizabeth-holmes-sentencing-a-history-of-the-wsj-theranos-investigation-11668741222.

53. Lekan Oyekanmi & Michael Liedtke, *Elizabeth Holmes Enters Texas Prison to Begin 11-year Sentence for Notorious Blood-testing Hoax*, AP (May 30, 2023, 5:42 PM), https://apnews.com/article/elizabeth-holmes-theranos-prison-fraud-texas-71bcdf58a0db73252cc2697fb9f73c8a.

54. Amy Chozick, *Liz Holmes Wants You to Forget About Elizabeth*, N.Y. TIMES (May 7, 2023), https://www.nytimes.com/2023/05/07/business/elizabeth-holmes-theranos-interview.html ("Ms. Holmes is unlike anyone I've ever met—modest but mesmerizing. If you are in her presence, it is impossible not to believe her, not to be taken with her and be taken in by her.").

55. *See, e.g.*, Benjamin Mazer, *Elizabeth Holmes Isn't Fooling Anyone*, THE ATL. (May 10, 2023), https://www.theatlantic.com/health/archive/2023/05/elizabeth-holmes-prison-new-york-times-profile/674016/.

56. Kalanick dropped out of college to found the file-sharing company Scour, which went bankrupt. He had greater success with his second venture, another file-sharing company called Red Swoosh, which started in 2001 and was sold in 2007 for $19 million. Kalanick

Once he had control of Uber, Kalanick became obsessed with growth at all costs to crowd out competitors. Many of the business decisions he made turned out well, such as tying the ride and payment experience to a user-friendly mobile app,[57] and introducing a dynamic pricing model to charge riders more during peak times.[58] Ultimately, the board decided to remove Kalanick, primarily due to the toxic culture of misogyny, harassment, and excess that developed at Uber under his leadership.[59] Dov Charney, founder and CEO of the urban hipster clothing company American Apparel, similarly was fired by his board after a series of sexual harassment lawsuits were filed against the company and him.[60] And Adam Neumann, CEO of the shared workspace startup WeWork, took a "steadfastly un-rock 'n' roll" business, the leasing of commercial property,[61] and through the force of his personality sold it as a "tech-enabled physical social network," fashioning himself as "a community builder, not a landlord."[62] Known for his extravagance and self-aggrandizement, Neumann ultimately lost his leadership position when WeWork had to postpone its initial public offering ("IPO").[63] The company eventually went public through a special purpose acquisition company ("SPAC") at less

personally netted about $2 million from the sale. Tom Huddleston, Jr., *5 of the Most Fascinating Revelations from New Uber Tell-all Book 'Super Pumped'*, CNBC (Sept. 5, 2019, 4:54 PM), https://www.cnbc.com/2019/09/05/fascinating-revelations-from-uber-tell-all-book-super-pumped.html.

57. ISAAC, supra note 8, at 59–60.

58. Borrows, *supra* note 43.

59. *See generally id.* The CEO who replaced Kalanick observed that "[t]he 'moral compass of the company' was not pointing in the right direction under Kalanick." Matthew J. Belvedere, *'Moral Compass' Was Off at Uber Under Co-founder Kalanick, Says New CEO Dara Khosrowshahi*, CNBC (Jan. 23, 2018, 6:36 AM), https://www.cnbc.com/2018/01/23/uber-moral-compass-under-co-founder-kalanick-was-off-new-ceo-says.html.

60. Hadley Freeman, *American Apparel Founder Dov Charney: 'Sleeping with People You Work with Is Unavoidable'*, GUARDIAN (Sept. 10, 2017, 11:00 AM), https://www.theguardian.com/lifeandstyle/2017/sep/10/american-apparel-dov-charney-sexual-harassment. The quote that led to the headline in this Article suggests that Charney did not learn much of a lesson from the experience, although it must be noted that he never was found guilty of sexual harassment. *Id.*

61. Borrows, *supra* note 43.

62. REEVES WIEDEMAN, BILLION DOLLAR LOSER: THE EPIC RISE AND SPECTACULAR FALL OF ADAM NEUMANN AND WEWORK 86 (2020).

63. Taylor Telford, *Adam Neumann's Chaotic Energy Built WeWork. Now It Might Cost Him His Job As CEO.*, WASH. POST (Sept. 23, 2019, 1:47 PM), https://www.washingtonpost.com/business/2019/09/23/adam-neumanns-chaotic-energy-built-wework-now-it-might-cost-him-his-job-ceo/.

than twenty percent of its initial value, and Neumann, despite having been let go, profited handsomely from the transaction.[64]

Elon Musk possesses a different type of charisma that likely explains the enormous success of his companies and his staying power relative to the other examples just discussed. One commentator described Musk as having "moderate[]" levels of charisma: he is a visionary, but with an operational mindset and an "impressive command of even the granular details to make [his vision] a reality."[65] Elon Musk is not like Elizabeth Holmes, who did not fully understand the complicated nature of blood-testing, or Adam Neumann, who was selling shared workspace as "a capitalist kibbutz."[66] Rather, he "is brilliant. He's involved in just about everything. He understands everything. . . . It's amazing to watch the amount of knowledge he has accumulated over the years."[67] However, some concern exists that the same skill set that allowed Musk to grow SpaceX, Tesla, and other ventures so successfully makes him ill-suited to run his newest venture, Twitter, which he purchased and took private in 2022.[68]

C. Synonymous with the Corporate Brand

The third common attribute among this cohort of corporate leaders is that their personal brand becomes interchangeable with the firm itself, and they are seemingly indispensable, such that it is difficult to imagine the corporation existing without them.[69] These leaders "are viewed as alter egos, or leading indicators, of

64. Matt Durot, *WeWork's Ousted Cofounder Adam Neumann Regains Billionaire Status as Company Goes Public Via SPAC*, FORBES (Oct. 21, 2021, 6:00 AM), https://www.forbes.com/sites/mattdurot/2021/10/21/weworks-ousted-cofounder-adam-neumann-regains-billionaire-status-as-company-goes-public-via-spac/?sh=42279eae22a6.

65. Eric Mack, *The Leadership Problem the Most Charismatic Bosses Face*, INC. (May 31, 2017), https://www.inc.com/eric-mack/elon-musk-may-succeed-because-hes-not-overly-charismatic.html.

66. Gabriel Sherman, *"You Don't Bring Bad News to the Cult Leader": Inside the Fall of WeWork*, VANITY FAIR (Nov. 21, 2019), https://www.vanityfair.com/news/2019/11/inside-the-fall-of-wework.

67. ASHLEE VANCE, ELON MUSK: TESLA, SPACEX, AND THE QUEST FOR A FANTASTIC FUTURE 237–38 (2015).

68. *See* Sean O'Kane, *Elon Musk Is 'Not Suited' to Run Twitter, Investor Says*, BLOOMBERG (Dec. 21, 2022, 8:36 PM), https://www.bloomberg.com/news/articles/2022-12-21/tesla-investor-gerber-says-musk-not-suited-to-run-twitter#xj4y7vzkg; Raffaella Sadun, *The Myth of the Brilliant, Charismatic Leader*, HARV. BUS. REV. (Nov. 23, 2022), https://hbr.org/2022/11/the-myth-of-the-brilliant-charismatic-leader (noting the "chaotic approach" Musk has taken since his Twitter takeover).

69. *See* Lin, *supra* note 1, at 354–55.

their firms," such that they "become a primary factor, if not *the* primary factor, in an individual's or institution's decision to invest."[70] This characteristic should not be confused with the "alter ego" requirement to pierce the corporate veil; rather, the CEO is viewed as the "doppelganger[]" of the firm[71] and becomes the company's most valuable asset.[72] After all, it is easier to make an investment decision based upon a CEO's personal story than it is to seek out and understand information about the corporation's financial picture.[73] Indeed, some scholars have theorized that the democratization of the stock market in recent decades has been an important factor in driving the rise of the CEO as celebrity.[74] Of course, when others view the CEO as indispensable to the business, the CEO often cannot help but have the same feelings as well. This is not necessarily bad for business: "narcissism conscientiously deployed often begets success."[75]

Elon Musk is linked inextricably with the companies he runs. Although he technically was not a founder of Tesla, his vision drove the company forward at a time when traditional automakers were not interested in electric vehicles.[76] This has merged Musk's personal brand with Tesla's, for better or for worse—and for early investors in Tesla, and advocates for the increased use of electric vehicles more generally, that has mostly been for the better.[77] In its own SEC filings, Tesla stated that it is "highly dependent on the services of Elon Musk," and acknowledged that if it were to lose Musk's services, the loss would "disrupt [Tesla's] operations, delay the development and introduction of [its] vehicles and services, and negatively impact [its] business, prospects and operating results

70. Lin, *supra* note 47, at 343–44.

71. Victoria L. Schwartz, *Corporate Privacy Failures Start at the Top*, 57 B.C. L. REV. 1693, 1714 (2016).

72. Tom C.W. Lin, *Executive Trade Secrets*, 87 NOTRE DAME L. REV. 911, 925 (2012).

73. Schwartz, *supra* note 71, at 1714. Prof. Schwartz posits that the treatment of corporate CEOs as public figures attracts individuals into those roles who place less of a premium on personal privacy. This, in turn, results in decision-making on the corporation's behalf that deemphasizes privacy rights. *Id.* at 1712–18.

74. Sánchez Abril & Olazábal, *supra* note 44, at 1552–54.

75. Barnard, *supra* note 16, at 410.

76. *See generally* Tad Friend, *Plugged In*, NEW YORKER (Aug. 17, 2009), https://www.newyorker.com/magazine/2009/08/24/plugged-in.

77. Andrew Ross Sorkin, *Want to Bring Back Jobs, Mr. President-Elect? Call Elon Musk*, N.Y. TIMES (Dec. 5, 2016), https://www.nytimes.com/2016/12/05/business/dealbook/manufacturing-jobs-donald-trump-elon-musk.html (stating that Musk "is arguably the one person in the nation more responsible than anyone else for generating a vision for the reemergence of manufacturing in the United States en masse" and "is revered among most of his peers here in Silicon Valley and elsewhere").

as well as cause [its] stock price to decline."[78] Musk refers to Tesla as "my company" and has stated that without him, "the company wasn't going to make it."[79] Indeed, sometimes it is hard to tell if it is Elon Musk talking or Tesla talking. And when he (or Tesla) talks, they talk in grandiose language about the impact that he (or it) will have on our society. It is not enough to have a goal of selling more electric vehicles or making them more affordable and accessible to a larger number of consumers. Rather, the "acceleration of sustainable energy is absolutely fundamental, because this [presumably, climate change] is the next potential risk for humanity."[80] Similarly, autonomous vehicles will not simply save us time and make us more productive, they will potentially "save millions of lives."[81] And an investor in Tesla is not just someone who purchased Tesla stock, but rather is "the broadest definition of investor, as in the people & life of Earth."[82] One can see how the CEO, the corporation, and a world-changing movement become indistinguishable from one another.

Musk is certainly not the first CEO to be considered synonymous with the company he runs, nor will he be the last.[83] Indeed, he is not even the first American carmaker to fit this mold.[84] However, the view of Musk or any CEO as "indispensable" to the firms they lead is at odds with the traditional structure of a corporation managed by an informed and engaged board of directors and operated by capable officers who were appointed by those directors, all for the benefit of the shareholders/owners. It

78. *In re* Tesla Motors Stockholder Litig., No. 12711-VCS, 2018 WL 1560293, at *2 (Del. Ch. Mar. 28, 2018).

79. *Id.*

80. Catherine Clifford, *Elon Musk: This Is the "Why" of Tesla*, CNBC (Feb. 4, 2019, 12:14 PM), https://www.cnbc.com/2019/02/04/elon-musk-on-the-why-and-purpose-behind-tesla.html.

81. *Id.*

82. Elon Musk (@elonmusk), TWITTER (Feb. 13, 2023, 4:55 PM), https://twitter.com/elonmusk/status/1625252299085082625?lang=en.

83. Lin, *supra* note 47, at 343–44 ("Jeff Bezos is Amazon. Warren Buffett is Berkshire Hathaway. Mark Zuckerberg is Facebook. Jamie Dimon is J.P. Morgan.").

84. Joann Muller, *Elon Musk Is Channeling Henry Ford in Auto Manufacturing*, AXIOS (Aug. 14, 2020), https://www.axios.com/2020/08/14/elon-musk-tesla-ford. Indeed, some see Musk's purchase of Twitter and his own expression of intolerant views via tweet to be following Henry Ford down a darker path. Kenneth G. Pringle, *Henry Ford Bought a Newspaper. It's a Warning for Elon Musk.*, BARRON'S (Feb. 1, 2023, 10:12 AM), https://www.barrons.com/articles/elon-musk-henry-ford-twitter-tesla-51675221419; David Zipper, *Elon Musk Went from Being Like Henry Ford in a Good Way to a Bad Way*, SLATE (Jan. 10, 2023, 5:45 AM), https://slate.com/technology/2023/01/elon-musk-henry-ford-twitter-history-nazis.html.

can also lead firms, particularly at the startup stage, to dispense with good corporate governance practices to give the founder more power to implement his or her vision. These decisions can have unfortunate consequences as the company matures.[85]

D. Eschewing Corporate Governance

Fourth, and perhaps most importantly for purposes of this Article, superstar CEOs often are focused single-mindedly on business success, having little time or regard for corporate governance rules that are designed to provide internal checks and balances.[86] Granted, a CEO of a complex organization like a publicly held corporation (or a startup with its sights set on that goal) should focus on leading, rather than managing. But as venture capitalists Marc Andreessen and Ben Horowitz have observed, founder CEOs "have to be partly delusional to start a company given the prospects of success and the need to keep pushing forward in the wake of the constant stream of doubters."[87] The single-minded approach to implementing the CEO's vision, which includes securing the capital (both monetary and human) necessary to do so, does not leave much time to be concerned with corporate formalities. If others around the CEO, such as angel seed investors, do not insist on some level of board independence and oversight, the superstar CEO is probably not going to do it for them.[88]

The best examples of CEOs who deprioritized the importance of an independent board who could hold the officers accountable are, naturally, the ones who never made it to the IPO stage (even if, in some cases, their corporations did). Elizabeth Holmes filled the Theranos board with older, accomplished gentlemen who had in common the traits of being accomplished in their fields, enamored with her and her vision, and lacking knowledge about the healthcare industry in general, much less the unprecedented (and, as it turned out, only theoretical) blood-testing technology that Theranos was trying to develop.[89] Sam Bankman-Fried of the

85. *See generally supra* pt. II.
86. Fan, *supra* note 3, at 353–54.
87. *Id.* at 368–69 (quoting SCOTT KUPOR, SECRETS OF SAND HILL ROAD 47–48 (2019)).
88. The impacts of this corporate governance breakdown at the various stages of a firm's maturity are explored in Part III of this Article.
89. *Supra* note 49 and accompanying text.

digital currency exchange FTX did not even do that much; FTX was incorporated in Antigua and Barbuda, not Delaware, and headquartered in the Bahamas, and its "board" consisted of Bankman-Fried and two college friends.[90] There was literally no oversight as FTX overleveraged itself, mismanaged funds, and then collapsed after a digital bank run on its crypto holdings.[91] While these are two of the most extreme examples (these CEOs are, after all, either already serving, or facing the prospect of serving, lengthy prison sentences), there certainly are others in recent memory. Uber's corporate charter designated eleven board seats, but while Travis Kalanick was serving as CEO, only seven of the seats were filled: three by Kalanick, his co-founder Garrett Camp, and an early employee, Ryan Graves, and a fourth by Arianna Huffington, who was an independent director but served as a key ally to Kalanick.[92] Only two board seats were filled by outside investors, and "[b]y leaving four seats empty, Kalanick [further] increased his control: If the outside directors ever challenged him, he could quickly stack the board with allies."[93] Many founders not only work around or disregard the board, but also control it.[94] The ability of a founder to maintain controlling shareholder status raises even greater challenges to ensuring mechanisms exist to protect shareholders.[95]

Although superstar CEOs are complex actors, some common traits among them include overconfidence, charisma, a close identification with their company's brand, and a lack of concern for ensuring a sound corporate governance structure. It is up to the corporation's board of directors, which has the legal responsibility

90. Lila MacLellan, *Investor Chamath Palihapitiya Once Advised Sam Bankman-Fried to Form a Board. FTX's Response? 'Go F—k Yourself'*, FORTUNE (Nov. 18, 2022, 11:15 AM), https://fortune.com/2022/11/18/ftx-board-investor-chamath-palihapitiya-sam-bankman-fried-board-directors-crypto/.

91. Allison Morrow, *'Complete Failure:' Filing Reveals Staggering Mismanagement Inside FTX*, CNN (Nov. 18, 2022, 5:23 AM), https://www.cnn.com/2022/11/17/business/ftx-ceo-complete-failure/index.html.

92. Steve Blank, *When Founders Go Too Far,* HARV. BUS. REV. (Nov.–Dec. 2017), https://hbr.org/2017/11/when-founders-go-too-far.

93. *Id.*

94. *See infra* pt. III.B.

95. In his 2012 book *The Founder's Dilemmas*, Noam Wasserman describes a series of decisions made early in the stages of a company's growth, which become a decision tree from which the entrepreneur cannot climb down. One startup founder interviewed for the book analogizes a startup to a marathon that is run in a series of successive one hundred-yard dashes. Each of these bursts of activity requires fateful decisions that will bind the company going forward, planting seeds for either success or failure. NOAM T. WASSERMAN, THE FOUNDER'S DILEMMAS 10 (2012).

to manage the firm's affairs, to harness the many strengths of this type of CEO while providing a check on the CEO's weaknesses in order to protect shareholders. As Tom Lin wrote, an "imperial model of corporate governance"—one in which the CEOs, "like corporate emperors and empresses, hold[] primacy over shareholders, directors, and managers during their reign"—"offers great promises to the governed, but those promises can be illusory, empty, and full of peril."[96]

III. THE BOARD'S ROLE IN OVERSEEING THE SUPERSTAR CEO

This Part focuses on what should be the first line of defense against an overreaching superstar CEO: the board of directors that is charged under the corporation statutes of all fifty states with overseeing that CEO and other senior employees of the firm. In addition to setting forth the basic tenets of corporate governance, this Part explores and synthesizes recent scholarship on governance challenges that are unique to startups, particularly in this era of increased private capital sources and founder-friendly early investors.

A. The Board's Traditional Oversight Role

Corporations exist at the largesse of the state, with all states having passed corporations statutes in the latter half of the nineteenth century.[97] Many states have corporate statutes based upon the Model Business Corporation Act ("MBCA") or one of its revisions.[98] Major holdouts from the MBCA include California, New York, and Delaware.[99] Over sixty percent of Fortune 500 companies and the vast majority of publicly held corporations (including, for example, over ninety percent of the corporations

96. Lin, *supra* note 1, at 362.

97. *See generally* LAWRENCE M. FRIEDMAN, *The Law of Corporations*, *in* A HISTORY OF AMERICAN LAW 495–511 (4th ed. 2019) (discussing the development of corporate law in the second half of the nineteenth century).

98. *State Enactment of MBCA*, AM. BAR ASS'N, https://www.americanbar.org/content/dam/aba/administrative/business_law/corplaws/enactment-table.pdf (last visited Jan. 28, 2024).

99. *Id.*

that went public in 2021) are incorporated in Delaware.[100] This makes its corporations statute, the Delaware General Corporation Law ("DGCL"), just as (or more) influential as the MBCA, even though the MBCA has been adopted in about two-thirds of states.[101] Even states that have adopted the MBCA look to Delaware as persuasive authority on matters of corporate law.[102]

Regardless of jurisdiction, the corporations statutes contemplate three primary roles in the corporate structure: the shareholders, the directors, and the officers.[103] Shareholders are the owners of the corporation. They have control over certain fundamental corporate transactions (i.e., mergers, amendments to the corporate charter, the sale of substantially all corporate assets, dissolution of the corporation), but otherwise elect directors to make the key decisions regarding the direction of the corporation.[104] Directors are the managers of the corporation, who are elected by, and answerable to, the shareholders. State corporations statutes grant directors, operating collectively as the board, broad power to manage the affairs of the corporation.[105] Officers are the senior employees of the corporation who oversee its day-to-day operations and are appointed by, and serve at the pleasure of, the directors.[106]

Directors, officers, and controlling shareholders[107] all owe fiduciary duties to the corporation itself and the shareholders.

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100. Charlotte Morabito, *Here's Why More Than 60% of Fortune 500 Companies Are Incorporated in Delaware*, CNBC (Mar. 13, 2013, 8:00 AM), https://www.cnbc.com/2023/03/13/why-more-than-60percent-of-fortune-500-companies-incorporated-in-delaware.html.

101. *State Enactment of MBCA*, *supra* note 98.

102. *See, e.g.*, Sanford v. Waugh & Co., 328 S.W.3d 836, 846 (Tenn. 2010).

103. Jade Yeban, *Corporate Structure: From Directors to Shareholders*, FINDLAW, https://www.findlaw.com/smallbusiness/incorporation-and-legal-structures/corporate-structure-directors-to-shareholders.html (last visited Jan. 28, 2024).

104. Jason Gordon, *Rights and Role of Shareholders of the Corporation – Explained*, THE BUS. PROFESSOR (Apr. 5, 2023), https://thebusinessprofessor.com/en_US/business-governance/role-of-shareholders-of-the-corporation.

105. DEL. CODE ANN. tit. 8, § 141(a) (2023); MODEL BUS. CORP. ACT § 8.01(a) (AM. BAR ASS'N 2023). Indeed, this essential role of the directors is recognized in Tesla's own corporate governance materials. *Corporate Governance Guidelines*, TESLA, https://digitalassets.tesla.com/tesla-contents/image/upload/IR-Corporate-Governance-Guidelines (last visited Jan. 28, 2024).

106. *Understanding the Roles of Officers and Directors in a Corporation*, ALLBUSINESS, https://www.allbusiness.com/officers-roles-within-a-corporation-532-1.html (last visited Jan. 28, 2024).

107. A controlling shareholder, at least in Delaware, is defined as one who owns a majority interest in the corporation or who owns a minority of shares but nonetheless "exercises control over the business affairs of the corporation." Kahn v. Lynch Commc'n Sys., 638 A.2d 1110, 1113–14 (Del. 1994). "For a dominating relationship to exist in the absence

These duties are unyielding and place the directors in a trustee-like position relative to the shareholders and the corporation.[108] Fiduciary duties serve as a restraint on the broad power of directors to manage the corporation by ensuring certain minimum standards of conduct.[109] The two predominant corporate doctrinal regimes, the MBCA and DGCL, both identify two fiduciary duties: the duty of care and the duty of loyalty.[110] The duty of care is owed by all directors and requires that they act with reasonable care, prudence, and in the best interests of the corporation.[111] This does not mean, however, that the board's good-faith decisions regarding the direction of the corporation will be second-guessed if those decisions turn out poorly. Rather, honest errors in judgment are protected by the business judgment rule, a deferential standard of review under which courts will defer to the board's decisions on business matters so long as they have some rational purpose.[112] The business judgment rule presumption places the burden on plaintiffs to plead one of the rare circumstances where liability under the duty of care might lie. These include the "corporate waste" doctrine (where the board's decision is found not to have

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of controlling stock ownership, a plaintiff must allege domination by a minority shareholder through actual control of corporation conduct." *Id.* at 1114 (quoting Citron v. Fairchild Camera & Instrument Corp., 569 A.2d 53, 70 (Del. 1989)).

108. The classic description of the nature of fiduciary duties was written by Justice Benjamin Cardozo: It is "the duty of the finest loyalty . . . something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior." Meinhard v. Salmon, 164 N.E. 545, 546 (N.Y. 1928).

109. Megan W. Shaner, *The (Un)Enforcement of Corporate Officers' Duties*, 48 U.C. DAVIS L. REV. 271, 296 (2014); *see also* Leo E. Strine, Jr., *The Inescapably Empirical Foundation of the Common Law of Corporations*, 27 DEL. J. CORP. L. 499, 501 (2002).

110. The law of fiduciary duties under the DGCL has developed through caselaw in the Delaware courts. *See generally* William M. Lafferty, Lisa A. Schmidt & Donald J. Wolfe, Jr., *A Brief Introduction to the Fiduciary Duties of Directors Under Delaware Law*, 116 PENN ST. L. REV. 837 (2012). In contrast, the fiduciary duties are set forth directly by statute in MBCA states, with some variation. For example, in Tennessee, an MBCA state, the title of the Tennessee Code Annotated pertaining to corporations statutes states that directors shall discharge their duties: "(1) In good faith; (2) With the care an ordinarily prudent person in a like position would exercise under similar circumstances; and (3) In a manner the director reasonably believes to be in the best interests of the corporation." TENN. CODE ANN. § 48-18-301 (2023); Sanford v. Waugh & Co., 328 S.W.3d 836, 844 (Tenn. 2010). The Tennessee Code goes on to state that officers and controlling shareholders have the same duties as directors. TENN. CODE ANN. § 48-18-403 (2023).

111. TENN. CODE ANN. § 48-18-301 (2023).

112. *See, e.g.*, Cede & Co. v. Technicolor, Inc., 634 A.2d 345, 361 (Del. 1993); Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984).

had any rational purpose)[113] and gross negligence in the process the board used to make its decision.[114] Moreover, the DGCL allows corporations to include language in their corporate charters that eliminates personal liability for breaches of the duty of care by their directors.[115] These so-called "raincoat provisions" were recently extended to officers by a 2022 revision to the DGCL.[116] MBCA states have a similar provision in their corporate statutes.[117]

The fiduciary duty of loyalty "requires a director to put the interests of the corporation and its stockholders ahead of the director's own personal interests which are not shared by the stockholders generally."[118] Unlike the duty of care, the duty of loyalty applies only to directors and officers in certain circumstances.[119] These include: where the directors have been shown to have acted in bad faith (e.g., *Caremark* oversight and monitoring cases);[120] the usurping of corporate opportunities by directors for their own advantage;[121] and conflict-of-interest transactions involving directors who are not independent and/or controlling shareholders.[122] In the last category, the defendants in

113. *See generally* Harwell Wells, *The Life (and Death?) of Corporate Waste*, 74 WASH. & LEE L. REV. 1239 (2017) (discussing the origin of corporate waste and explaining its survival).

114. Smith v. Van Gorkom, 488 A.2d 858, 873 (Del. 1985).

115. DEL CODE ANN. tit. 8, § 102(b)(7) (2023).

116. *See* S.B. 273, 151st Gen. Assemb. (Del. 2022) (revising DEL. CODE ANN. tit. 8, § 102(b)(7)); *see also* Theodore N. Mirvis, David A. Katz & Sabastian V. Niles, *Delaware Approves Permitting Exculpation of Officers from Personal Liability*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Aug. 4, 2022), https://corpgov.law.harvard.edu/2022/08/04/delaware-approves-permitting-exculpation-of-officers-from-personal-liability/.

117. *See, e.g.*, TENN. CODE ANN. § 48-12-102(b)(3) (2023).

118. Lafferty et al., *supra* note 110, at 845 (citing Cede & Co. v. Technicolor, Inc., 634 A.2d 345, 361 (Del. 1993)).

119. *Id.*

120. *In re* Caremark Int'l Inc. Deriv. Litig., 698 A.2d 959, 971 (Del. Ch. 1996). Originally thought to be a violation of the duty of care, the language in *Caremark* regarding the "bad faith" of directors has led courts subsequently to classify it as a breach of the duty of loyalty. Stone v. Ritter, 911 A.2d 362, 370 (Del. 2006). For many years, *Caremark* claims were thought to exist only in theory, but they have seen a recent resurgence in Delaware courts. *See, e.g.*, Marchand v. Barnhill, 212 A.3d 805, 822 (Del. 2019) (allowing oversight claims against the directors of Blue Bell Creameries to proceed past the motion to dismiss stage); *In re* McDonald's Corp. Stockholder Deriv. Litig., 289 A.3d 343, 358 (Del. Ch. 2023) (extending *Caremark* liability to officers as well as directors).

121. *See, e.g.*, Broz v. Cellular Info. Sys., Inc., 673 A.2d 148, 154 (Del. 1996).

122. "An 'interested transaction' is a transaction in which one or more directors approving the transaction receives a benefit (whether financial or otherwise) that is (i) not shared by the stockholders of the corporation as whole and (ii) subjectively material to that director's decision to approve the transaction." Lafferty et al., *supra* note 110, at 845 n.33.

the conflict-of-interest transaction bear the burden of proving the "entire fairness" of the transaction to shareholders.[123] Moreover, the defendants cannot be exculpated from liability for breaches of the fiduciary duty of loyalty, because such activity falls outside of the scope of the "raincoat provisions" described in section 102(b)(7) of the DGCL and comparable statutory provisions in MBCA states.[124]

If the directors or officers breach their fiduciary duties, then shareholders can bring a derivative suit on behalf of the corporation to enforce those duties and recover damages caused by the breach. However, this is an imperfect enforcement mechanism.[125] Thus, it is it even more important for the board to be proactive in overseeing potentially damaging behavior by the CEO and other officers.

In summary, the directors have clear fiduciary duties to the corporation and the shareholders, as well as duties to oversee officers like the CEO who make day-to-day business decisions for the corporation. This places the board, as both "manager and monitor,"[126] in the best position to protect shareholders from either misfeasance or malfeasance on the part of the CEO.

B. Challenges to Corporate Governance Principles in Startup Culture

Many celebrity CEOs either are founders of the corporation or, like Elon Musk with Tesla, got involved very early on during the startup phase. Although the fiduciary duties and oversight responsibilities that directors owe the shareholders and corporation are well-established, there are particular obstacles to ensuring sound corporate governance with corporate startups. These are tied to changes that have occurred over the past few decades in the way startups are financed. "Longstanding theories of corporate ownership and governance do not capture the special features of startups."[127]

123. *See* Weinberger v. UOP, Inc., 457 A.2d 701, 710 (Del. 1983).
124. MODEL BUS. CORP. ACT § 2.02(b)(4) (AM. BAR ASS'N 2023).
125. See further discussion of the limitations of the courts as a check on the CEO *infra* pt. IV.A.
126. Shaner, *supra* note 109, at 304–05.
127. Elizabeth Pollman, *Startup Governance*, 168 U. PA. L. REV. 155, 155 (2019).

Traditionally, founders have tended to gradually either share control with investors or lose control as startups go through multiple rounds of funding and begin to mature.[128] This is because venture capitalists increase their ownership share and add board seats with each round of funding. Moreover, once a startup began looking toward the IPO, venture capitalists often would replace the creative founder of the company with someone more experienced in managing a complex organization.[129] This was viewed as essential to attracting institutional investors during the IPO stage.[130] However, in recent years, startups have been staying private longer for a variety of reasons, most notably the increased availability of capitalization through private markets.[131] When venture capitalist Aileen Lee coined the term "unicorn" in 2013 to describe privately held companies with a valuation of over $1 billion, only thirty-nine companies met that threshold. By January 2022, the number of unicorns was over nine hundred.[132]

By 2010, venture capitalists began to challenge the traditional wisdom of replacing the founder with a hand-picked successor.[133] The success of certain founders well beyond the IPO stage, such as Jeff Bezos at Amazon, Bill Gates at Microsoft, Mark Zuckerberg at Facebook, and, of course, Steve Jobs at Apple,[134] was "impossible [for venture capitalists] to ignore."[135] Venture capitalists "began to see founders not as a problem that needed to be solved but as a valuable asset that needed to be retained."[136] The need of tech-heavy startups to continuously innovate and bring the innovations to market made it sensible to keep in place CEO founders, "whose creativity and restlessness, comfort with disorder, and propensity for risk taking are more valuable at a time when companies need

128. *Id.* at 181.

129. Blank, *supra* note 92.

130. *Id.* ("Part of the IPO process was the road show, for which the bankers would fly the company CEO and CFO around the country to present to institutional investors; the last thing institutions wanted to see was an inexperienced founder at the helm of a company.").

131. Fan, *supra* note 3, at 335–37; Pollman, *supra* note 127, at 175.

132. Matthew Wansley, *Taming Unicorns*, 97 IND. L.J. 1203, 1204 (2022).

133. BROWN & FARRELL, *supra* note 7, at 55.

134. Actually, Steve Jobs, co-founder of Apple, was fired by the board in 1985, only to return twelve years later and help build Apple into one of the world's most innovative and valuable companies. Blank, *supra* note 92; Matt Weinberger, *This Is Why Steve Jobs Got Fired from Apple — and How He Came Back to Save the Company*, BUS. INSIDER (July 31, 2017, 2:17 PM), https://www.businessinsider.com/steve-jobs-apple-fired-returned-2017-7.

135. BROWN & FARRELL, *supra* note 7, at 55.

136. Blank, *supra* note 92.

to retain a start-up culture even as they grow large."[137] Influential VCs such as Andreesen Horowitz began marketing themselves as "founder friendly," which, of course, won over founders who wanted to stay in control.[138] Corporate America's decade of improvements around conflicts of interest and shareholder oversight "regressed dramatically in Silicon Valley in the 2010s amid a boom of founder control."[139] Whether this is a positive trend for long-term company growth is debatable,[140] but there have been two clear impacts of this change on corporate governance.

First, because companies are staying private longer, they are not subject to disclosure requirements under the federal securities laws which are designed to protect investors and provide greater incentive for board and regulatory oversight.[141] If a publicly traded company has inherent mismanagement and misconduct issues, the market for information will theoretically bring such problems to light. Short-sellers are the bloodhounds of the market, sniffing out negative information about a public company. Although these efforts are purely self-serving, designed to identify inefficiencies in the market that could be monetized, a positive impact is to protect shareholders from otherwise undiscovered corporate misconduct.[142] Private companies, on the other hand, have no such incentive structures in place to expose mismanagement or misconduct. If, as U.S. Supreme Court Justice Louis Brandeis famously said, "sunlight is the best disinfectant,"[143] then the trend of having startups stay private longer, thus delaying their

137. *Id.*

138. *Id.* ("Understandably, advertising your firm as 'founder friendly' creates a competitive advantage in a business where success has much to do with your ability to source and negotiate deals with founders."). Moreover, in general, venture capitalists are not incentivized to root out or expose corporate misconduct due to their asymmetric risk preferences. Wansley, *supra* note 132, at 1207.

139. BROWN & FARRELL, *supra* note 7, at 391.

140. Noam Wasserman, *FTX and the Problem of Unchecked Founder Power*, HARV. BUS. REV. (Dec. 1, 2022), https://hbr.org/2022/12/ftx-and-the-problem-of-unchecked-founder-power (noting that for each degree of control a founder retains in a startup, the company's value is lower by an average of 20 percent).

141. *See generally* Wansley, *supra* note 132 (arguing for greater disclosure requirements for private corporations); James J. Park, *Investor Protection in an Age of Entrepreneurship*, 12 HARV. BUS. L. REV. 107, 136 n.140 (2022).

142. Wansley, *supra* note 132, at 1205–06.

143. Jesse Eisenger, *In an Era of Disclosure, an Excess of Sunshine but a Paucity of Rules*, N.Y. TIMES (Feb. 11, 2015), https://archive.nytimes.com/dealbook.nytimes.com/2015/02/11/an-excess-of-sunlight-a-paucity-of-rules/; *Brandeis and the History of Transparency*, SUNLIGHT FOUND. (May 26, 2009), https://sunlightfoundation.com/2009/05/26/brandeis-and-the-history-of-transparency/.

compliance with the disclosure requirements of the federal securities laws, may have the effect of insulating bad behavior by CEOs.

Second, in the later stages of private funding, or even after the company does go public, boards often remain filled with directors who are highly deferential to the CEO. This happens for various reasons. The most obvious is that the board may still be populated by early investors in the firm, including friends, family, and angel seed investors, who believe strongly in the founder CEO's vision.[144] "[S]elf-selected boards and managers . . . likely will be reluctant to question or second-guess the decisions of their revered chief executive officer and chairman."[145] Even if the CEO has packed the board with allies, it may be good business for investor board members to support the founder. Market dynamics over the past couple of decades have changed, such that "[w]hereas once too many start-ups chased limited amounts of capital from a relatively small number of VC firms, today, some would argue, too much capital is chasing too few quality start-ups."[146] This creates disincentives for venture capitalists serving in their director roles to exercise monitoring and oversight of the CEO.[147] As Benchmark Capital and former Uber board member Bill Gurley observed: "Silicon Valley board rooms have mostly become applauding audiences of clapping hands."[148]

"It is in the face of this narrative—[where] larger-than-life founders . . . with a single-minded focus are able to do as they please—where the corporate governance mechanisms may begin to function poorly. The investor directors may . . . give[] the founder-management director more control than is prudent."[149] "Where nonbelievers might consider such a choice irrational, the 'cult of the founder' suggests that no matter what the chief executive may decide, he was probably right because he was the right guy to begin with."[150] Theranos was one of the most infamous examples of this board obsequiousness: on the rare occasions when board members asked questions pushing back at all on Elizabeth Holmes, they

144. Pollman, *supra* note 127, at 202; Shaner, *supra* note 109, at 304–11.
145. Lin, *supra* note 1, at 365.
146. Pollman, *supra* note 127, at 205 (quoting Blank, *supra* note 92).
147. *Id.* at 205–06.
148. *Id.* at 206.
149. Fan, *supra* note 3, at 369.
150. ISAAC, *supra* note 8, at 77.

were chastised or even encouraged to resign.[151] "Independent" board members, each of whom had enormous successes in their own fields, treated Holmes like doting grandfathers rather than asking probing questions about Theranos's blood-testing technology.[152]

In some modern startups, the CEO's power is derived from not only his or her influence, but also the outsized voting power they have preserved for themselves through the stages of capitalization. They do this by implementing a dual-class stock structure, which gives management the ability both to choose directors who are friendly to them and to fire those who might question them. Specifically, startups, particularly those "in the highest echelon of unicorns,"[153] may issue two (or more) classes of shares: Class A shares to the public and Class B super-voting shares to the founders and their allies.[154] The founders of Google and Facebook became models for this approach when they successfully implemented dual-class stock structures in their IPOs.[155] Employing this structure, through which the Class B shares held by the founders and other key investors represented ten votes to every one vote controlled by holders of the Class A shares sold to the public, ensured that Google's founders, Larry Page and Sergey Brin, maintained control of the corporation long after it went public in 2004.[156] Mark Zuckerberg employed a similar strategy through early rounds of funding at Facebook and the company's IPO in 2012; to this day, he still owns a controlling percentage of shares of the company.[157]

Some celebrity CEOs even have had dual-class stock structures in place prior to the IPO stage. Travis Kalanick at Uber limited the amount of information provided to investors and held super-voting shares worth ten votes, while investors only received common shares worth one vote.[158] "No investors could meddle in how he spent Uber's money, no shareholders could tell him who to hire, who to fire, and so on. Uber was Travis Kalanick's company—

151. CARREYROU, *supra* note 6, at 36–38.
152. *Id.* at 36, 207.
153. Pollman, *supra* note 127, at 182.
154. Jerry Davis, *The Simple Reason Tech CEOs Have So Much Power*, FAST CO. (Apr. 3, 2021), https://www.fastcompany.com/90620747/dual-class-voting-tech-ceo-power.
155. ISAAC, *supra* note 8, at 76.
156. *Id.*
157. *Id.* at 77.
158. ISAAC, *supra* note 8, at 97.

and if you were lucky, he would let you invest."[159] Elizabeth Holmes, at Theranos, similarly "owned more than 250 million shares of Class B stock, a super-voting class of shares that afforded her 100 votes per-share," and as a result owned fifty-one percent of the company in 2014.[160] So not only did Holmes control the activities of the corporation as CEO, but also she retained the power to fire the board of directors if she so chose.[161]

C. Board Oversight at Elon Musk's Tesla

How does Elon Musk's history at Tesla compare to some of these other celebrity CEOs? To start, Musk definitely learned lessons from his earliest ventures, Zip2 and X.com. Both startups were, by any objective measure, successful: Zip2 was sold in 1999 to Compaq for over $300 million, and X.com eventually became PayPal and was sold to eBay in 2002 for $1.5 billion in stock.[162] However, Musk was removed as CEO from both companies.[163] This led him to vow that he would never lose control of SpaceX or Tesla.[164] Despite the enormous growth in those two companies since he founded them, he has come close to that goal. Although Musk's stake in SpaceX has dropped below fifty percent in recent years, he still controls the privately held company through a voting trust.[165]

Tesla is an even more interesting story. Contrary to popular lore, Elon Musk was not a founder of Tesla. The company was formed in 2003 by Martin Eberhard and Marc Tarpenning.[166] After

159. *Id.* at 97–98. See further discussion of the make-up of Uber's board, *supra* pt. II.

160. Heather Somerville, *Prosecution Focuses on Holmes's Control at Theranos,* WALL ST. J. (Nov. 30, 2021, 7:41 PM), https://www.wsj.com/livecoverage/elizabeth-holmes-trial-theranos/card/8W5FAVfMOfNalo3tYR10.

161. Elizabeth Lopatto, *Elizabeth Holmes Admits That She Was CEO of Theranos, The Company She Founded*, THE VERGE (Nov. 30, 2021, 10:32 PM), https://www.theverge.com/2021/11/30/22811246/elizabeth-holmes-texts-control-theranos-money.

162. Raisa Bruner, *A Complete Timeline of Elon Musk's Business Endeavors*, TIME (Apr. 27, 2022, 3:55 PM), https://time.com/6170834/elon-musk-business-timeline-twitter/.

163. Samuel Leeds, *3 Leadership Lessons to Learn From Elon Musk*, ENTREPRENEUR (June 17, 2021), https://www.entrepreneur.com/living/3-leadership-lessons-to-learn-from-elon-musk/374462.

164. Kafka, *supra* note 32.

165. Micah Maidenberg, *Elon Musk's SpaceX Stake Moves Lower, But Executive Retains Control*, WALL ST. J. (Dec. 23, 2022, 7:00 AM), https://www.wsj.com/articles/elon-musks-spacex-stake-moves-lower-but-executive-retains-control-11671761294.

166. *Tesla: A History of Innovation (and Headaches)*, FORBES (Sept. 29, 2022, 4:12 PM), https://www.forbes.com/sites/qai/2022/09/29/tesla-a-history-of-innovation-and-headaches/?sh=286d80a11873.

investing $6.5 million and becoming chairman of the board in 2004 (a position he held until 2018), Musk led subsequent rounds of funding.[167] By 2007, Tesla had private financing to the tune of $105 million.[168] Musk officially took the helm of Tesla as CEO in 2008, with the electric-vehicle manufacturer on the verge of collapse after the Great Recession.[169] Shortly thereafter, the U.S. Department of Energy loaned Tesla $465 million (Tesla repaid the loan, plus $12 million in interest, by 2013) and auto giant Daimler acquired a 10% stake in the company.[170] In June 2010, Tesla went public with a valuation of about $2.22 billion.[171] Having navigated the early stages of Tesla's capitalization and participated in all rounds of funding, Musk still held thirty-six percent of Tesla's stock at the time of the IPO, which dropped to about twenty-eight percent afterward.[172] The percentage of Musk's ownership has decreased steadily over time; in 2018, when the Delaware Chancery Court held him to be a controlling shareholder of Tesla as part of Tesla's acquisition of SolarCity, he owned 22.1 percent of Tesla stock.[173] Notably, having maintained his controlling interest in Tesla the old-fashioned way, Musk has spoken out against the use of super-voting rights through dual class structures, specifically criticizing Facebook, now Meta, for "an equity structure that makes it such that [Mark Zuckerberg's] great-great-grandchildren will still control the company."[174]

Tesla's stock price languished for nearly ten years after its IPO. However, as Tesla took control of more of the market share for electric vehicles, and particularly during the COVID pandemic, Tesla's stock price skyrocketed.[175] Specifically, it increased more than thirty times its value between August 2019 and November

167. *Id.*
168. *Id.*
169. *Id.*
170. *Id.*
171. *Id.*
172. Lynn Cowan, *Tesla Roars Out of the Garage*, WALL ST. J. (June 30, 2010, 12:01 AM), https://www.wsj.com/articles/SB10001424052748704103904575336853549268476.
173. *In re* Tesla Motors Stockholder Litig., No. 12711, 2018 WL 1560293, at *2 (Del. Ch. March 28, 2018).
174. *Elon Musk on Income Inequality, Cryptocurrency and His Tweets: Excerpts From the 2021 Person of the Year Interview*, TIME (Dec. 13, 2021, 7:44 AM), https://time.com/6127757/elon-musk-interview-person-of-the-year-2021/.
175. Rakesh Sharma, *Why Tesla (TSLA) Skyrocketed During the Pandemic*, INVESTOPEDIA (Dec. 2, 2021), https://www.investopedia.com/why-tesla-skyrocketed-during-pandemic-5211590.

2021, when it peaked at about $410/share.[176] The stock price then dropped precipitously throughout late 2021 and all of 2022—a time period corresponding with Musk's flirtation with and eventual purchase of Twitter—hitting a low of about $101/share at the end of 2022.[177]

This story of Tesla's valuation helps put into context the activity (or inactivity) of Tesla's board during this time period. Two significant events took place in 2018 that suggested Tesla's board was deferring heavily to its CEO, who by that point had reached celebrity status.[178] First, the Board awarded a massive compensation package to Musk in 2018 that became the basis for a shareholder derivative suit.[179] Second, Musk's social media postings became more indiscriminate and ubiquitous, with the most egregious example being his infamous "funding secured" tweet on August 7, 2018.[180] This led to an immediate SEC enforcement action that culminated in a settlement agreement, in which Musk agreed to step down as chairman of Tesla's board and submitted to having a "Twitter sitter" at Tesla screen all of his tweets related to the automaker.[181] It also led to a class action securities fraud case that ended with a trial in early 2023, in which Musk was held not liable.[182] As to the offending tweet, board members at the time testified at that trial that they had no duty to oversee Musk because the tweet was sent in his individual capacity, not his capacity as CEO or board chair.[183]

176. Will Daniel, *Elon Musk Has Lost $100 Billion in Net Worth this Year Alone as Tesla's Stock Plunges*, FORTUNE (November 22, 2022, 12:29 PM), https://fortune.com/2022/11/22/elon-musk-lost-100-billion-net-worth-this-year-tesla-stock-drop/.

177. *Id.*

178. Claudia Assis & Jessica Marmor Shaw, *Elon Musk is More Famous than Ever, and Maybe More Dangerous*, MARKETWATCH (Sept. 7, 2018, 11:02 AM), https://www.marketwatch.com/story/elon-musk-is-more-famous-than-ever-and-maybe-more-dangerous-2018-08-31.

179. Tornetta v. Musk, 250 A.3d 793 (Del. Ch. 2019).

180. On that day, Musk tweeted to his millions of followers: "Am considering taking Tesla private at $420. Funding secured." Elon Musk (@elonmusk), TWITTER (Aug. 7, 2018, 12:48 PM), https://twitter.com/elonmusk/status/1026872652290379776?lang=en/.

181. *Elon Musk Settles SEC Fraud Charges; Tesla Charged with and Resolves Securities Law Charge*, SEC. & EXCH. COMM'N (Sept. 29, 2018), https://www.sec.gov/news/press-release/2018-226.

182. Faiz Siddiqui, *Elon Musk Found Not Liable in Federal Trial Over 'Funding Secured' Tweet*, WASH. POST (Feb. 3, 2023, 5:56 PM EST), https://www.washingtonpost.com/technology/2023/02/03/elon-musk-tesla-verdict/.

183. Hyunjoo Jin & Jody Godoy, *Musk Did Not Need Tesla Board to Review Buyout Tweets, Directors Testify*, REUTERS (Feb. 1, 2023, 6:18 PM EST), https://www.reuters.com/legal/tesla-directors-testify-funding-secured-trial-2023-02-01/.

Tesla's board in 2018 consisted of twelve directors, including Musk himself, his brother, Kimbal, and his good friend, James Murdoch, as well as several other close allies of Musk's.[184] Even the independent directors tended to have some interest in one of Musk's other business ventures, as either a significant investor or a board member. To its credit, Tesla instituted a major shakeup of its board in 2019, reducing the board from twelve to seven directors and letting the terms of multiple Musk allies expire.[185] The company's reason for the changes was a desire "to operate more nimbly and efficiently," but there had been criticism over the directors' close ties to Musk.[186] And this new, more "nimble" board sat by in 2022 and 2023 while Mr. Musk diverted not only his time and energy but other corporate resources to his new purchase, Twitter.[187]

IV. Courts and Regulators as Imperfect Protectors of Shareholders

If the board of directors fails to sufficiently protect shareholders when the superstar CEO's relationship with the corporation turns sour, then someone else needs to step in. The two most obvious candidates to stand in the breach are courts and regulators. As discussed, shareholders do retain the right to sue to protect the corporation's interests when they believe the board and/or the CEO are breaching their fiduciary duties.[188] Superstar

184. Tesla, Inc., Notice of 2018 Annual Meeting of Stockholders (Schedule 14A) (June 5, 2018).

185. Neal E. Boudette, *Tesla to Shrink Board of Directors by Four People*, N.Y. TIMES (Apr. 19, 2019), https://www.nytimes.com/2019/04/19/business/tesla-directors-resign.html#.

186. *Id.*

187. Peter Eavis & Isabella Simonetti, *Elon Musk's Twitter Role Puts Tesla Board Under New Scrutiny*, N.Y. TIMES (Nov. 22, 2022, 12:01 PM EST), https://www.nytimes.com/2022/11/22/business/elon-musk-tesla-board-twitter.html; Letter from Elizabeth Warren, Senator, to Tesla Board (Dec. 18, 2022), https://www.warren.senate.gov/imo/media/doc/2022.12.18%20Letter%20to%20Tesla%20Board%20on%20Musk%20Concerns.pdf.

188. Shaner, *supra* note 109, at 311 ("Stockholder power in the corporate enterprise has been described as being comprised of three things: the rights to vote, sell, and sue"). It goes without saying that the right to simply sell their shares gives shareholders an out if they are unhappy with the direction a CEO is taking a company. However, unless a shareholder is the first out the door, then the shareholder's interest will be negatively affected if the CEO's actions are depressing the corporation's share price. Thus, some protection is warranted.

CEOs have not been immune to the shareholder derivative suit.[189] Moreover, regulators have stepped in when boards have not, as in the case of the 2018 SEC settlement with Mr. Musk over the "funding secured" tweets.[190] However, there are significant limitations in relying on the courts and government regulators to rein in the superstar CEO. The cost of time and corporate resources that are involved in litigation means that damage will be done to shareholders, and their investments, even if the shareholders ultimately prevail. This is why it is so important for corporate boards to institute strong governance practices to ensure that they are not hypnotized by the siren of the superstar CEO.

A. Courts as Protectors of Shareholders

There is no doubt that the courts have the power to bring wayward or overreaching CEOs back into line—even if that CEO is one of the richest men in the world.[191] However, there are so many obstacles impeding shareholders from having their day in court that it makes the courts flawed protectors of good corporate governance.

If the directors or officers have breached their fiduciary duties, then the duties can be enforced by the shareholders through the derivative suit, in which a shareholder brings a claim on behalf of the corporation for actions by the officers and directors that have injured the corporation.[192] The shareholder derivative action finds its origins in the English Court of Chancery but developed uniquely in the United States during the nineteenth century.[193] In a derivative suit, the shareholder brings a claim against third parties or, more commonly, corporate fiduciaries (usually officers

189. *See, e.g.*, McElrath v. Kalanick, Del. 224 A.3d 982, 989 (2020); *In re* Tesla Motors Inc. S'holder Litig., No. 12711, 2018 WL 1560293, at *2 (Del. Ch. March 28, 2018).

190. Lora Kolodny, *SEC Rebuffs Elon Musk's Attempt to Get Out of 'Funding Secured' Settlement*, CNBC (Feb. 23, 2023, 7:17 PM EST), https://www.cnbc.com/2023/02/23/sec-rebuffs-musks-attempt-to-get-out-of-funding-secured-settlement.html.

191. *See* Lauren Hirsch, *Elon Musk Seems to Answer to No One. Except for a Judge in Delaware.*, N.Y. TIMES (Oct. 26, 2022, 3:00 AM EST), https://www.nytimes.com/2022/10/26/technology/musk-twitter-delaware-judge-mccormick.html.

192. Ann M. Scarlett, *Shareholder Derivative Litigation's Historical and Normative Foundations*, 61 BUFF. L. REV. 837, 841–42 (2013).

193. *See id. (*detailing the origins and development of the derivative suit both England and the United States). *See also* Ross v. Bernhard, 396 U.S. 531, 534–35 (1970) (considering both the history and legal and equitable nature of the derivative suit in determining that it gives rise to a constitutional right to jury trial under the Seventh Amendment).

or directors) who have allegedly wronged the corporation.[194] Unlike in a direct action, where the shareholder sues to remedy an injury that he or she has suffered personally, in the derivative action the shareholder "step[s] into the corporation's shoes . . . to seek in its right the restitution he could not demand in his own."[195] In other words, the derivative suit represents the third "arrow" in the "quiver" available to the shareholder to express his or her displeasure with the activities of corporate management—"vote, sell, or sue."[196] The derivative action has two primary goals: compensation of shareholders for injuries inflicted on the corporation and deterrence of future bad acts by corporate management.[197]

The derivative suit has long been compared to the class action, which is another "form of representative litigation long recognized by courts in the United States" where "one or a few persons stand for another or group of persons" and assert claims on their behalf.[198] And like the class action, the derivative action has long had both its supporters and its detractors.[199] On the one hand, derivative suits have been praised as "ingenious";[200] "a needed

194. JAMES D. COX & THOMAS LEE HAZEN, BUSINESS ORGANIZATIONS LAW 439–40 (3d ed. 2011).

195. Cohen v. Beneficial Loan Indus. Corp., 337 U.S. 541, 548 (1949); *see also* Scarlett, *supra* note 192.

196. *See, e.g.*, Robert B. Thompson, *Shareholders as Grown-Ups: Voting, Selling, and Limits on the Board's Power to "Just Say No,"* 67 U. CIN. L. REV. 999, 1001–03 (1999) (describing the three options and asserting that "[c]umulatively, these shareholder rights define a limited shareholder role in corporate governance"); Andrew C.W. Lund, *Rethinking Aronson: Board Authority and Overdelegation*, 11 U. PA. J. BUS. L. 703, 708 (2009); *see also* COX & HAZEN, *supra* note 194, at 349 (describing the three classes of shareholder rights as "(1) rights as to control and management, (2) proprietary rights, and (3) remedial and ancillary rights").

197. Carol B. Swanson, *Juggling Shareholder Rights and Strike Suits in Derivative Litigation: The ALI Drops the Ball*, 77 MINN. L. REV. 1339, 1345 (1993).

198. Scarlett, *supra* note 192, at 841; *see also* Ross, 396 U.S. at 541 ("Derivative suits have been described as one kind of 'true' class action. We are inclined to agree with the description, at least to the extent it recognizes that the derivative suit and the class action were both ways of allowing parties to be heard in equity who could not speak at law."). Of course, a major distinction is that the lead plaintiff in a class action has suffered some direct injury along with the other class members, whereas the injury in a shareholder derivative suit is the corporation's alone.

199. Carol B. Swanson, *Corporate Governance: Sliding Seamlessly into the Twenty-First Century*, 21 J. CORP. L. 417, 437 (1996) ("Both ingenuous and uniquely complicated, shareholder derivative suits have been controversial since their inception . . . Although some view derivative litigation as providing an invaluable procedural remedy for shareholders seeking accountability, others caution that the corporation, not courts, should resolve internal business conflicts.").

200. Swanson, *supra* note 199, at 1340 (quoting ROBERT C. CLARK, CORPORATE LAW § 15.1 (1986)).

policeman" that "serve[s] a basic and increasing need in the contemporary economy";[201] and, perhaps most famously, as a "potent tool[] to redress the conduct of a torpid or unfaithful management."[202] On the other hand, derivative suits have been disparaged as "nuisance suits whose 'principal beneficiaries . . . are attorneys'";[203] and as having "little, if any, beneficial accountability effects"[204] while placing "a high cost constraint and infringement upon the board's authority."[205]

The unique nature of the derivative suit, and concerns about its potential abuses, have given rise to several procedural obstacles that shareholder plaintiffs must overcome before a court will consider the merits of their derivative claims.[206] The most significant of these—or at the very least, the most litigated—is the demand requirement,[207] which in Delaware is embodied in both the common law and Delaware Chancery Rule 23.1. Rule 23.1 requires the plaintiff to "allege with particularity the efforts, if any, made . . . to obtain the action the plaintiff desires from the directors or comparable authority and the reasons for the plaintiff's failure to obtain the action or for not making the effort."[208] Delaware's demand requirement "is a recognition of the fundamental precept," enshrined in the DGCL, "that directors manage the business and affairs of corporations."[209] This

201. Daniel J. Dykstra, *The Revival of the Derivative Suit*, 116 U. PA. L. REV. 74–75, 78 (1967).

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

203. Robert B. Thompson & Randall S. Thomas, *The Public and Private Faces of Derivative Lawsuits*, 57 VAND. L. REV. 1747, 1748 (2004); *see also* Roberta Romano, *The Shareholder Suit: Litigation Without Foundation?*, 7 J.L. ECON. & ORG. 55, 65 (1991).

204. Robert B. Thompson & Randall S. Thomas, *The Public and Private Faces of Derivative Lawsuits*, 57 VAND. L. REV. 1747, 1748 n. 2 (2004).

205. Stephen M. Bainbridge, CORPORATION LAW & ECONOMICS 404 (2002).

206. *See, e.g.*, Dykstra, *supra* note 201, at 75 ("The hurdles referred to are neither simple nor insignificant. They carry such names as 'security for expenses,' 'contemporaneous ownership' and 'demands on directors and shareholders.' They are, for the most part, the by-products of the 'strike suit' and represent reactions to abuse of the judicial process by stockholders whose motive in bringing suit is personal gain rather than corporate benefit."); *see also* Pogostin v. Rice, 480 A.2d 619, 624 (Del. 1984) ("[B]ecause the derivative action impinges on the managerial freedom of directors, the law imposes certain prerequisites to the exercise of this remedy.").

207. *Cf.* Lund, *supra* note 196, at 703 ("[T]he demand requirement in derivative litigation is one of the most consequential doctrines in corporate law.").

208. DEL. CH. R. 23.1; *see also* FED. R. CIV. P. 23.1 (requiring the same of derivative suits that are filed in federal court).

209. Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984); *see also* DEL. CODE ANN. tit. 8, § 141(a) (2020) ("The business and affairs of every corporation organized under this chapter shall be managed by or under the direction of a board of directors. . . .").

requirement exists both "to insure that a stockholder exhausts his intracorporate remedies" and "to provide a safeguard against strike suits."[210] The "net effect" of Rule 23.1 "is to reduce the overall volume of litigation, constrain the extent of interference with managerial decision-making, and limit the resource-drain that excessive litigation would impose."[211]

Whatever the merits of Delaware's demand requirement, shareholder plaintiffs pursuing their derivative action will rarely, if ever, make a demand on the board. This is because Delaware's courts have held that a demand on the board by the shareholder is a concession that a majority of the board is disinterested enough to consider the demand, thus waiving the issue of board independence in the subsequent litigation.[212] Wanting to avoid the waiver caused by making a demand—particularly since the request of the board will almost certainly be rejected[213]—plaintiffs file suit and then litigate the issue of whether demand should be excused as futile (or, in the language of Rule 23.1, their "reasons for . . . not making the effort"). The test for demand futility recently was clarified by the Delaware Supreme Court.[214]

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210. *Aronson*, 473 A.2d at 811–12. The American Law Institute's *Principles of Corporate Governance* cites four purposes of the demand rule. The rule: (1) "protects the court from unnecessarily hearing a case that is not ripe for decision or that might be mooted by subsequent board action"; (2) "provides an opportunity for the board to determine if it will pursue other remedies or take other appropriate corrective actions"; (3) "permits the corporation to take over the suit and control the litigation"; and (4) "provides the corporation with an opportunity to reject the proposed action or, if it is filed, to seek its early dismissal." PRINCIPLES OF CORPORATE GOVERNANCE: ANALYSIS AND RECOMMENDATIONS § 7.03 cmt. c (AM. L. INST. 1992).

211. *In re* El Paso Pipeline Partners, L.P. Derivative Litig., 132 A.3d 67, 94 (Del. 2015) (*rev'd*, El Paso Pipeline GP Co., LLC v. Brinckerhoff, 152 A.3d 1248 (Del. 2016)).

212. *See* Spiegel v. Buntrock, 571 A.2d 767, 777 (Del. 1990) ("By electing to make a demand, a shareholder plaintiff tacitly concedes the independence of a majority of the board to respond."); Levine v. Smith, 591 A.2d 194, 212 (Del. 1991) (same); John C. Coffee, Jr., *New Myths and Old Realities: The American Law Institute Faces the Derivative Action*, 48 BUS. LAW. 1407, 1413 (1992).

213. *See, e.g.*, Daniel J. Morrissey, *The Path of Corporate Law: Of Options Backdating, Derivative Suits, and the Business Judgment Rule,* 86 OR. L. REV. 973, 997 (2007) ("[I]n practice boards typically reject demands out of hand, claiming that these suits are not in the corporation's best interest.").

214. United Food & Comm. Workers Union & Participating Food Indus. Emps. Tri-State Pension Fund v. Zuckerberg, 262 A.3d 1034, 1058 (Del. 2022) (clarifying the three-part test as "(i) whether the director received a material personal benefit from the alleged misconduct that is the subject of the litigation demand; (ii) whether the director would face a substantial likelihood of liability on any of the claims that are the subject of the litigation demand; and (iii) whether the director lacks independence from someone who received a material personal benefit from the alleged misconduct that is the subject of the litigation demand or who would face a substantial likelihood of liability on any of the claims that are the subject of the litigation demand").

Eschewing the Delaware approach, the MBCA has adopted a "universal demand" requirement.[215] This provision states that a shareholder may not file a derivative suit on behalf of the corporation unless they first make a written demand to the board of directors to take action and wait ninety days for the board to respond to the demand.[216] The ninety-day waiting period only may be waived if the board rejects the demand or if irreparable injury would inure to the corporation from the delay in filing.[217] The universal demand requirement was adopted to reduce the time and expense involved in litigating the demand issue and to give the board a chance to fairly and timely respond to the allegations.[218] It is unclear whether it has had that intended effect.[219] But, at any rate, there is no doubt that the demand requirement raises significant obstacles to protecting shareholders from acts of malfeasance or misfeasance of a celebrity CEO.

Other obstacles to using the courts to protect the shareholders include the collective action problem, which disincentivizes shareholders from banding together to bring derivative actions, and information asymmetry.[220] Shareholders in large, decentralized corporations have little incentive, time, or financial resources to pursue claims for breach of fiduciary duty against the officers or directors.[221] It may be easier and more desirable for shareholders, even "large institutional shareholders[,] to sell their shares when they perceive inadequacies of corporate governance,

215. Stanley Keller, *Recent Decisions Relevant to the MBCA*, AM. BAR ASS'N (Dec. 5, 2022), https://www.americanbar.org/groups/business_law/resources/business-law-today/2022-december/recent-decisions-relevant-to-the-mbca/.

216. MODEL BUS. CORP. ACT § 7.42 (AM. BAR ASS'N 2008).

217. *Id.* § 7.42 (2).

218. *Id.* § 7.42 cmt.1 (official comment).

219. *See, e.g.*, Jeffrey M. Gorris et al., *Delaware Corporate Law and the Model Business Corporation Act: A Study in Symbiosis*, 74 LAW & CONTEMP. PROBS. 107, 118 (2011). The authors characterize the attempt by the MBCA's drafters to improve upon Delaware's demand practice as "likely wishful thinking" because "[t]he same issues litigated in demand futility cases (for example, director disinterestedness and independence) must still be litigated, based on pleadings alone, when the corporation moves to dismiss the derivative proceeding." *Id.*; *see also* Morrissey, *supra* note 213, at 999 ("[T]he requirement of universal demand and the Delaware rule allowing it to be excused may amount to much the same thing.").

220. Shaner, *supra* note 109, at 316–18.

221. *Id.* at 316 ("[T]he lack of economic incentives and other time, money and resource constraints continue to deter individual, institutional, and activist stockholders alike from engaging in consistent, meaningful monitoring of management.").

rather than fix them."[222] Finally, the information available to stockholders to even make a determination as to whether to bring a derivative suit may be extremely limited, particularly if the corporation is still privately held.[223]

Finally, the shareholder derivative suit is unlikely to make shareholders or the corporation whole if the CEO's behavior has really caused damage to the firm and, concomitantly, to the value of the shareholders' investment. To be sure, shareholders may buy stock in a corporation for a variety of reasons: because they are attracted to the corporate mission, believe in or use the products or services of the corporation, or think the corporation is making the world a better place. But the primary (and often exclusive) reason to buy shares of a corporation is because you believe it will bring you a return on your investment. When the impact of a celebrity CEO's bad behavior directly impacts the value of that investment by lowering the stock price, a shareholder derivative suit is an imperfect mechanism to remedy that. The procedural obstacles and time lag described above are one reason; another is that, even if in the uncommon circumstance that the shareholder derivative suit is successful, it does not follow that the award or settlement will necessarily be monetary. Indeed, nonmonetary settlements are far more common, and a significant number of awards include nonmonetary relief in the form of corporate governance reforms.[224] These reforms could include changing the composition of the board or reforming corporate policies with regard to executive composition or shareholders' rights to bring proposals at the annual shareholder meeting.[225] Although the promise of a fee award for plaintiff's attorneys ensures that derivative suits will continue to be filed, and they may continue to serve their primary purpose of deterring bad behavior by corporate

222. *Id.* at 317 (quoting Alan Greenspan, Chairman, Fed. Reserve Bd., Federal Reserve Board's Semiannual Monetary Policy Report to the Congress, Testimony Before the Committee on Banking, Housing, and Urban Affairs (July 16, 2002), http://www.federalreserve.gov/boarddocs/hh/2002/july/testimony.htm).

223. *Id.* at 318 ("[L]ike the board of directors, stockholders are at an informational disadvantage that seriously weakens their ability to monitor officer conduct and ensure compliance with fiduciary obligations.").

224. Jessica Erickson, *The Lost Lessons of Shareholder Derivative Suits*, 77 WASH. & LEE L. REV. 1131, 1151 (2020) (citing Roberta Romano, *The Shareholder Suit: Litigation Without Foundation?*, 7 J.L. ECON. & ORG. 55 (1991)).

225. *Id.*

actors (after all, nobody wants to be sued), the derivate suit is limited in its ability to actually protect shareholders.[226]

It is true that shareholders can also bring direct claims for damages to their interest in the corporation. But direct claims are not an appropriate mechanism for enforcing fiduciary duties. A "stockholder's claimed direct injury must be independent of any alleged injury to the corporation."[227] A breach of fiduciary duty damages the corporation as a whole and the shareholders collectively, rather than individually. For all of these reasons, the courts are imperfect protectors of a shareholder's investment in a corporation if the value of that investment is threatened by the actions of a CEO who is unchecked by the board of directors.

B. Regulators as Protectors of Shareholders

An alternative mechanism to protect shareholders from superstar CEOs who have received insufficient oversight from their boards are regulators who have the mission of protecting the investing public. Through Section 10(b) of the Securities and Exchange Act, and Rule 10b-5 implementing that Section, the SEC is authorized to regulate fraud, deceit, or materially misleading disclosures or omissions made by the directors or officers of public companies. However, as described earlier in this article, many of the worst acts by superstar CEOs, which caused significant liabilities and harm to investors, occurred in companies (Theranos, WeWork, FTX) that had not held an IPO. Recognizing the rise of private markets in the twenty-first century and the propensity of startups to stay private longer, the SEC recently has explored ways to expand its regulatory reach beyond public companies.

The robust statutory and regulatory scheme created to protect investors after the market crash of 1929 includes both the Securities Act of 1933, which governs the issuing of securities, and the Securities Exchange Act of 1934, which regulates the behavior of public companies outside of primary securities offerings by requiring the companies to make regular public disclosures to keep investors informed and monitoring the truthfulness of those

226. *But see* Stephen P. Farris et al., *Derivative Lawsuits as a Corporate Governance Mechanism: Empirical Evidence on Board Changes Surrounding Filings*, 42 J. FIN. & QUANTITATIVE ANALYSIS 143 (2007) (arguing that shareholder derivative suits are an effective corporate governance mechanism to protect the legal rights of investors).

227. Tooley v. Donaldson, Lufkin & Jenrette, Inc., 845 A.2d 1031, 1039 (Del. 2004).

disclosures.[228] The SEC was created as part of the Exchange Act with a tri-fold mission of "protecting investors, maintaining fair, orderly, and efficient markets, and facilitating capital formation."[229] Section 10(b) of the Exchange Act makes it illegal "[t]o use or employ, in connection with the purchase or sale of any security . . . any manipulative or deceptive device or contrivance" that contravenes any SEC rule.[230] Rule 10b-5, promulgated under the authority granted to the SEC by the Exchange Act, makes it unlawful, in connection with the purchase or sale of any security, to engage in any business practice that operates as a fraud or deceit on anyone or "[t]o make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading."[231] Courts have long implied a private right of action to enforce Rule 10b-5.[232] Thus, in addition to criminal enforcement of the rule through the SEC's Enforcement Division, shareholders can sue public companies and their officers and directors directly or collectively on behalf of the class for alleged violations of the rule. In order to prove liability under Rule 10b-5, either the SEC or the plaintiff must prove: (1) a material misrepresentation (or omission); (2) scienter, i.e., a wrongful state of mind; (3) a connection with the purchase or sale of a security; (4) reliance, often referred to in cases involving public securities markets (fraud-on-the-market cases) as "transaction causation"; (5) economic loss; and (6) "loss causation," i.e., a causal connection between the material misrepresentation and the loss.[233]

Regulation of corporate actors through Rule 10b-5 has traditionally fallen along a public-private divide.[234] In other words,

228. *See* Elisabeth de Fontenay & Gabriel Rauterberg, *The New Public/Private Equilibrium and the Regulation of Public Companies*, 2021 COLUM. BUS. L. REV. 1199, 1210–12 (2021); Elizabeth Pollman, *Private Company Lies*, 109 GEO. L.J. 353, 361–62 (2020).

229. *Mission*, SEC, https://www.sec.gov/about/mission (last modified Dec. 26, 2023).

230. 15 U.S.C. § 78j(b).

231. 17 C.F.R. § 240.10b-5 (2014); *see also* Jay B. Kasner and Mollie Melissa Kornreich, *Section 10(b) Litigation, The Current Landscape*, ABA BUS. L. TODAY (Oct. 20, 2014), https://www.americanbar.org/groups/business_law/resources/business-law-today/2014-october/section-10-b-litigation-the-current-landscape/.

232. Kasner & Kornreich, *supra* note 231; *see* Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 730–31 (1975) (reaffirming an implied private right of action but limiting it to actual purchases and sellers of securities).

233. Dura Pharms., Inc. v. Broudo, 544 U.S. 336, 341–42 (2005) (citations omitted).

234. Fontenay & Rauterberg, *supra* note 228, at 1210–12; Pollman, *supra* note 228, at 363–65.

publicly held corporations are subject to the dual requirements of disclosure and truth in those disclosures set forth in the federal securities laws, while privately (or closely) held corporations are not. A recent article described three "triggers" for companies to be considered "public" pursuant to the federal securities laws: "(1) they offer to sell their securities to the general public; (2) they grow large enough that their assets or shareholders of record exceed specified thresholds; or (3) at least one class of their securities is traded on a national securities exchange."[235] The first and third categories are familiar, but the second may be less so. It refers to Section 12(g) of the Exchange Act, which, as amended by the Jumpstart Our Business Startups ("JOBS") Act of 2012, requires a company to register its securities and engage in periodic reporting if it has over $10 million in total assets and two thousand or more shareholders (or five hundred or more "unaccredited investor" shareholders).[236] Thus, if the superstar CEO is able to navigate the early stages of firm growth and the transition to being a publicly held Delaware C-corporation—a move that for most large, successful firms still is likely inevitable[237]—then their statements and actions, if false or materially misleading, could leave them caught between the Scylla and Charybdis of the SEC Enforcement Division and the plaintiff's securities lawyer.

As CEO (and previously Chairman of the Board) of Tesla, Elon Musk is no stranger to the SEC. Indeed, he has publicly referred to the SEC as "bastards" and said point-blank, "I do not respect the SEC."[238] This frustration has stemmed primarily from the enforcement action the SEC filed against him based upon his August 7, 2018 Tweet that he "was considering taking Tesla private at $420 a share."[239] This statement, which was not approved in any way by Tesla's board, had an immediate impact on Tesla's stock price, as it closed that day up nearly eleven percent from the previous day's closing on significant trading volume.[240]

235. Fontenay & Rauterberg, *supra* note 228, at 1211.

236. *Id.* at n.40 (citing 15 U.S.C. § 78l(g)(1)(A)).

237. *Id.* at 1219.

238. David Gura, *Can the SEC Stand Up to the Richest Man on the Planet?*, NPR (June 4, 2022, 8:01 AM), https://www.npr.org/2022/06/04/1102327987/elon-musk-sec-tweets-lawsuit-power.

239. *See* Musk, *supra* note 180.

240. Complaint ¶ 2, U.S. Sec. & Exch. Comm'n v. Musk, Civil Action No. 1:18-cv-8865 (S.D.N.Y. Sept. 27, 2018). Musk followed the "$420 Tweet" with more Tweets over the next few hours, including one that stated: "Investor support is confirmed. Only reason why this is not certain is that it's contingent on a shareholder vote." *Id.*

Moving at lightning speed by its standards,[241] the SEC filed a complaint in federal court in New York a mere seven weeks after the public statements were made by Musk on Twitter.[242] The complaint alleged that Musk violated Rule 10b-5 by falsely and materially indicating that he alone could decide whether Tesla could go private and at what share price.[243]

The SEC action settled quickly with both Musk and Tesla, which the SEC argued should have had greater internal controls and monitoring over its CEO's social media activity.[244] In the settlement with the SEC, Musk and Tesla agreed that: (1) Musk would step down as Chairman of Tesla's board for a period of at least three years; (2) Tesla would appoint two new independent directors to its board; (3) Tesla would appoint a "Twitter sitter" to review all of Musk's communications; and (4) Musk and Tesla would each pay a separate $20 million penalty.[245] In other words, the SEC externally imposed some of the strong corporate governance practices that Tesla's board had declined to adopt itself. There were open questions as to how effective these measures would be, given Musk's idiosyncratic and anti-authoritarian nature, which has led him to challenge and even subvert orders by regulators and courts in the past.[246] And as noted above, Musk publicly expressed his exasperation with the SEC action, with his lawyers going so far as to complain to the federal judge overseeing the case that the SEC was "targeting Mr. Musk and Tesla for unrelenting investigation" and "chill[ing] his exercise of First Amendment rights" because he was "an outspoken critic of the government."[247] He also pursued an appeal that would have overturned the district court judge's approval of the settlement.[248]

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241. Benjamin Bain, *SEC's Move Against Elon Musk Was Unusually Quick*, BLOOMBERG L. (Sept. 27, 2018, 8:02 P.M.), https://www.bloomberg.com/news/articles/2018-09-28/sec-s-move-against-elon-musk-was-unusually-quick-experts-say.

242. *Id.*

243. *Id.*

244. *Elon Musk Settles SEC Fraud Charges*, *supra* note 181.

245. *Id.*

246. Cat Zakrzewski, *Musk May Have Violated FTC Privacy Order, New Court Filing Shows*, WASH. POST (Sept. 12, 2023, 4:21 PM), https://www.washingtonpost.com/technology/2023/09/12/elon-musk-consent-order-ftc/.

247. Chris Isidore, *Elon Musk Says the SEC is Gunning for His Free Speech Rights*, CNN (Feb. 17, 2022, 2:27 PM), https://www.cnn.com/2022/02/17/business/elon-musk-sec-first-amendment/index.html.

248. Larry Neumeister, *Federal Appeals Court Rules Elon Musk Must Abide by SEC Settlement Over Tesla Tweets*, PBS (May 15, 2023, 6:22 PM), https://www.pbs.org/newshour/

However, that appeal was unsuccessful,[249] and at the time of this writing, Musk has not been re-elected Chairman of Tesla's board[250] and still has a member of Tesla's communications team monitoring his public statements regarding the company.[251] In this case, at least, the egregiousness of the violation combined with the speed with which the SEC responded to Musk's false and misleading public statements did effectively protect Tesla's shareholders from their CEO's bad acts.

While the infrastructure for regulating the activities and disclosures of public companies is well-established, it is much less so for private companies. This has become increasingly important over time because the number of public companies has been decreasing over the past couple of decades, both in terms of the number of IPOs offered and the amount of capital raised.[252] SEC Commissioners have been transparent in their public remarks about the trend: former SEC Chairman Jay Clayton observed that private capital raising is "dominating" and "outraising" the public markets,[253] and while Commissioner Allison Herren Lee described that with the growth in private markets—"[p]erhaps the single most significant development in securities markets in the new millennium"—we are "watching a growing portion of the U.S. economy go dark, a dynamic the Commission has fostered."[254] Indeed, "it is, quite naturally, impossible to know the extent" of securities fraud in the private markets,[255] although the incentives to engage in such activity—encouraging growth at any cost—can

nation/federal-appeals-court-rules-elon-musk-must-abide-by-sec-settlement-over-tesla-tweets.

249. U.S. Sec. & Exch. Comm'n v. Musk, No. 22-1291, 2023 WL 3451402 (2d Cir. May 15, 2023).

250. Tesla, *Corporate Governance: A Message from Robyn Denholm, Our Board Chair*, https://ir.tesla.com/corporate (last visited Jan. 24, 2024).

251. Rohan Gaswami, *Elon Musk Still Needs 'Twitter Sitter,' Judges Rule*, CNBC (May 15, 2023, 11:37 AM), https://www.cnbc.com/2023/05/15/elon-musk-still-needs-twitter-sitter-judge-rules.html.

252. *See* Robert B. Thompson & Donald V. Langevoort, *Redrawing the Public-Private Boundaries in Entrepreneurial Capital Raising*, 98 CORNELL L. REV. 1573, 1573–74 (2013); Verity Winship, *Private Company Fraud*, 54 U.C. DAVIS L. REV. 663, 671 (2020).

253. Pollman, *supra* note 228, at 370 (quoting Jay Clayton, Chairman, U.S. Sec. & Exch. Comm'n, Remarks to the Economic Club of New York (Sept. 9, 2019), transcript available at https://www.sec.gov/news/speech/speech-clayton-2019-09-09.)

254. Allison Herren Lee, Commissioner, U.S. Sec. & Exch. Comm'n, Remarks at the SEC Speaks in 2021 (Oct. 12, 2021), https://www.sec.gov/news/speech/lee-sec-speaks-2021-10-12.

255. Pollman, *supra* note 228, at 377.

be significant.[256] Some SEC Commissioners have called for further study in this area and a possible extension of Section 12(g) of the Exchange Act to increase oversight and SEC enforcement ability in the private markets, with a particular focus on the "unicorns" that have proliferated in recent years.[257] Whether the SEC has the legal authority to reshape the public-private divide in this way is a matter of debate among scholars,[258] particularly in light of pending cases before the Supreme Court that could both limit the SEC's enforcement ability[259] and sharply reduce the authority of administrative agencies more generally by casting aside the decades-old administrative law principle of *Chevron* deference.[260] There is so much uncertainty in the private markets right now, and so little known about the private markets, that it is hard to say that regulators will have an active role in protecting shareholders of "unicorns" and other startups that are still held privately from the actions of their CEOs.

All of these regulatory efforts, however, are colored by the concern that while the work of regulators may have positive impacts on the market generally, it is ineffective to proactively protect investors in individual companies from the bad acts of corporate officers. First, CEOs can harm shareholders through misfeasance or malfeasance without actually violating the federal securities laws.[261] And second, the speed with which the SEC acted in its 2018 action against Musk is the exception, rather than the rule. In most circumstances, by the time regulators are involved, the harm usually has already been inured to shareholders. For these reasons, while the SEC plays a vital role in maintaining market integrity in the United States, it is limited in its ability to safeguard shareholders from the superstar CEO.

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256. *Id.* at 378–83 (describing three main factors driving securities fraud in the private markets: pressure, opportunity, and rationalization).

257. Lee, *supra* note 48; Caroline A. Crenshaw, Commissioner, U.S. Sec. & Exch. Comm'n, Big "Issues" in the Small Business Safe Harbor: Remarks at the 50th Annual Securities Regulation Institute (Jan. 30, 2023), https://www.sec.gov/news/speech/crenshaw-remarks-securities-regulation-institute-013023.

258. *Compare* Pollman, *supra* note 228 and Winship, *supra* note 252 *with* Alexander I. Platt, *Unicorniphobia*, 13 HARV. BUS. L. REV. 115 (2023). For a longer list of articles arguing for greater oversight in the private markets, see Platt, *supra*, at n. 11.

259. Sec. & Exch. Comm'n v. Jarkesy, No. 20-61007 (U.S. argued Nov. 29, 2023).

260. Loper Bright Enter. V. Raimondo, No. 22-451 (U.S. argued Jan. 17, 2024).

261. Katanga Johnson & Chris Prentice, *How Murky Legal Rules Allow Tesla's Musk to Keep Moving Markets*, REUTERS (May 14, 2021), https://news.yahoo.com/analysis-murky-legal-rules-allow-110204331.html.

V. CONCLUSION

The success that Elon Musk has had at Tesla, SpaceX, and his other ventures has only heightened Silicon Valley's passion for finding the next superstar CEO. Early-stage investors and venture capitalists who make up the boards of many startups are looking for someone with confidence and charisma who can become synonymous with the corporate brand. This often leads them to overlook or eschew good corporate governance practices that ensure the CEO and other officers meet their fiduciary duties to the firm and its shareholders. In the worst of cases, it even tempts them to overlook recklessness with the truth and behavior that is damaging to the firm's culture. In this modern era, when startups are more likely to stay private for a longer period and out of the watchful eye of regulators, it is okay for boards to be founder-friendly, but not to the expense of meeting their duty of oversight. There is a fine line between being the inspirational founder-leader of a successful Fortune 500 company and being the subject of the next *Wall Street Journal* investigation or tell-all biography. Maybe that is why we are so fascinated by Elon Musk—in him, we have both.