BerkeleyLaw
UNIVERSITY OF CALIFORNIA

Berkeley Center for Law, Business and the Economy

University of California, Berkeley
School of Law
2850 Telegraph Ave, Suite 500
Berkeley, CA 94705-7220

Ph: 510.642.0532 – Fax: 510.643.7095
E-mail: BCLBE@law.berkeley.edu
http://www.law.berkeley.edu/bclbe.htm

Shake Shack's IPO: Eating the Burger and Keeping it Whole

By Tamir Chagal, LLM Candidate 2015| February 17, 2015

In late January, Shake Shack, the upper tier hamburger chain, went public and "broke" Wall Street: not only was the company able to sell its shares at a price of $21 per share, twice as much as the price-per-share foreseen prior to the IPO, but it also maintained its strict "anti-activism" corporate governance regime without deterring its investors.

Even after the consummation of the IPO, Shake Shack remained a dual class company, with highly deferred voting rights attached to one class of shares, which were not offered to investors under the IPO. Therefore, while the restaurant's new investors have paid $105 million for 44.2% of the company's economic stake (which is mainly the right to enjoy liquidation and asset distribution events upon their occurrence), the purchased shares only granted them with 14.1% of the aggregate voting powers, while the original founders retained 85.9% of the voting rights. Such control structure enables Danny Meyer, the main founder of Shake Shack, to continue to steer the company's management with little voting dilution in lieu of the injected capital, leaving little room for shareholder activism campaigns by minority shareholders, which is a common instrument by activist investors (such as hedge funds, pension funds, mutual funds, etc.) to reshape the company's strategy.

Meyer's control of the successful food chain is further reflected by the control over the board of directors. So long as Meyer and his pre-IPO investors maintain 25% of their stock, they will continue to be entitled to nominate as least four members, a board majority. Adding to that is the fact that Shake Shack maintains a "staggered board" in which shareholders will not be able to replace the entire board at once, even if the shareholders no longer support the board members' nomination. Therefore, even if Meyer and his backers will lose the majority voting interests in the company, the remaining shareholders will still be required to win at least two cycles of proxy wars in order to replace the board and nominate new board members who might be keener on adopting activists' lobbied resolutions.

The high demand for Shake Shack's stock upon going public, together with the high price-per-share, which doubled yet again on the first trading day, may suggest that investors consider the company as a "cash cow" and desire to cash in on its prospective growth, even at the cost of minimizing their ability to influence decision making in the company. This might explain some unexpected names found on the list of new investors, such as the California State Teachers' Retirement System, a notable pension fund. While this form of corporate governance has generally little effect over individuals' investment decisions, implementing strict anti-activism barriers such as deferred voting for different classes of shares and a staggered board usually deters certain institutional investors, as they consider this kind of regime less attractive for activism campaigns.

It seems that the high attractiveness of Shake Shack has enabled it to raise nine figure funds without causing Meyer and his group of investors to actually relinquish control over the company, nor enable a breach for activism campaigns. Time will tell whether Meyer will be able to sus-

University of California, Berkeley
School of Law
2850 Telegraph Ave, Suite 500
Berkeley, CA 94705-7220

Ph: 510.642.0532 – Fax: 510.643.7095
E-mail: BCLBE@law.berkeley.edu
http://www.law.berkeley.edu/bclbe.htm

tain this form of corporate governance in the event of the company becoming less compelling for investors.