Opinion **On Wall Street**

Robinhood push to democratise finance falters with own shares

IPO gives greater voting rights to founders of upstart brokerage

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Robinhood co-founders Vladimir Tenev and Baiju Bhatt celebrate in New York following the company's IPO © AP

Madison Darbyshire JULY 30 2021

Robinhood has had a pretty clear pitch as it has taken on Wall Street's traditional brokerages with its trading app — democratise finance for all.

That slogan hearkens back to the origins of the company in 2013 in the wake of the Occupy Wall Street protest movement, which railed against wealth inequality and the power of big banks.

Robinhood's co-founders said they saw a need to disrupt the established, elitist financial system and make equity markets more accessible to everyday investors.

That pitch — reinforced with branding that played on the original Robin Hood ideal of stealing from the rich to give back to the poor — helped make the company the brokerage of choice for many new, young investors piling into equity markets since the start of the pandemic.

But in making its $32bn initial public offering this week, corporate governance activists believe the upstart company has not lived up to the democratic ideals of its mission statement.

Robinhood offered up to 35 per cent of its shares to its own customers, offering access for retail investors to a part of the market traditionally reserved for large investment institutions. It allocated the shares itself, bypassing traditional Wall Street banks by using the new IPO access feature on its app.

However, it has eschewed what corporate governance experts believe is the gold standard for shareholder structures of one share, one vote.

Not all Robinhood shares are created equal. Its co-founders will retain an extraordinary level of control over their company after it goes public. Robinhood's dual class structure means the shares sold to retail investors and institutions carry one vote, while the shares held by its co-founders Vlad Tenev and Baiju Bhatt carry 10 votes per share.

The former high-frequency traders will own approximately 16 per cent of the company's shares (7.9 per cent each), yet control 65 per cent of the votes, with Tenev holding 26.2 per cent and Bhatt holding 39 per cent, according to the company's prospectus.

Dennis Kelleher, the chief executive of Better Markets, a financial reform advocacy group, said it was not clear that retail investors understand that "the owners of Robinhood are rigging share ownership in their favour".

"Robinhood should tell retail traders that its shares available to them are in fact impaired shares that are always going to be less valuable than the shares of people running Robinhood for their own benefit," he said.

Some 85 per cent of companies in America that went public in 2020 used one share one vote structures according to data from the Council of Institutional Investors, a corporate governance advocacy body. However, many higher profile companies — particularly in the tech sector — have more power over their investors to push through dual-class structures.

When ride-hailing service Lyft went public, for example, its co-founders owned just 5 per cent of the stock but held on to 49 per cent of the votes using a 20 to 1 dual share structure. In some companies, the extra voting rights even extend to the afterlife. Pinterest founder Ben Silbermann was also issued shares that gave him 20 times the number of votes of common stock shareholders, a privilege that gave him voting rights for up to 540 days after his death.

If the company actually succeeds, the shareholder power imbalance will widen. Tenev and Bhatt's voting share rises if the share price hits certain price targets. If they receive their maximum agreed compensation including shares, the co-founders' voting rights would represent more than 75 per cent of total shareholder votes in the company, according to the company's prospectus.

IPO investors raised concerns about the dual class structure, and the unusual amount of power it gave both Tenev and his increasingly silent partner Bhatt. Both have been dealing with numerous regulatory interventions as a result of their "move fast and break things" approach to Robinhood's early growth.

One large money manager who declined to invest in the IPO said: "You have no power over the management team if you want to get rid of them, and that is something to worry about."

Premium valuations placed on hot companies with dual voting class structures in IPOs also tend to dissipate in subsequent years, according to research from the European Corporate Governance Institute on US companies from 1980-2017.

David Erickson, a lecturer at the University of Pennsylvania's Wharton business school and former IPO banker, said it was not uncommon in recent years for tech companies over the last few years to have a dual-class voting structure. But he said it was odd to have one if a company was claiming to democratise investing.

"One share one vote is how you democratise investing," he said.

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