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Competitive Effects of Differential Voting Rights and Promoter Control in Indian Start-Ups

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Abstract : The definition of 'control' in India is a rapidly evolving concept, owing to varying rights attached to varying securities. Shares with differential voting rights (DVRs) provide the holder with differential rights as to voting, as compared to ordinary equity shareholders of the company. Such DVRs can amount to both superior voting rights and inferior voting rights, where DVRs with superior voting rights amount to providing the holder with golden shares in the company. While DVRs are not a novel concept in India having been recognized since 2000, they were placed on a back burner by the Securities and Exchange Board of India (SEBI) in 2010 after issuance of DVRs with superior voting rights was restricted. In June 2019, the SEBI rekindled the ebbing fire of DVRs, keeping mind the fast-paced nature of the global economy, the government's faith that India's 'new age technology companies' (i.e., Start-Ups) will lead the charge in achieving its goal of India becoming a $5 trillion dollar economy by 2024, and recognizing that the promoters of such Start-Ups seek to raise capital without losing control over their companies. DVRs with superior voting rights guarantee promoters with up to 74% shareholding in Start-Ups for a period of 5 years, meaning that the holder of such DVRs can exercise sole control and material influence over the company for that period. This manner of control has the potential of causing both pro-competitive and anti-competitive effects in the markets where these companies operate. On the one hand, DVRs will allow Start-Up promoters/founders to retain control of their companies and protect its business interests from foreign elements such as private/public investors – in a scenario where such investors have multiple investments in firms engaged in associated lines of business (whether on a horizontal or vertical level) and would seek to influence these firms to enter into potential anti-competitive arrangements with one another, DVRs will enable the promoters to thwart such scenarios. On the other hand, promoters/founders who themselves have multiple investments in Start-Ups, which are in associated lines of business run the risk of influencing these associated Start-Ups to engage in potentially anti-competitive arrangements in the name of profit maximisation. This paper shall be divided into three parts: Part I shall deal with the concept of 'control', as deliberated upon and decided by the SEBI and the Competition Commission of India (CCI) under both company/securities law and competition law; Part II shall review this definition of 'control' through the lens of DVRs, and Part III shall discuss the aforementioned potential pro-competitive and anti-competitive effects caused by the DVRs by examining the current Indian Start-Up scenario. The paper shall conclude by providing suggestions for the CCI to incorporate a clearer and more progressive concept of 'control'.

Keywords : competition law, competitive effects, control, differential voting rights, DVRs, investor shareholding, merger control, start-ups
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