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Alibaba post-IPO structure gives insiders control

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In this Aug. 27, 2014 file photo, a chef walks in the headquarter campus of Alibaba Group in Hangzhou in eastern China's Zhejiang province. Control over Alibaba Group will stay in the hands of founder Jack Ma and other company veterans after the Chinese e-commerce giant goes public on the New York Stock Exchange in a record busting share sale. (AP Photo/File)

Control over Alibaba Group will stay in the hands of founder Jack Ma and other company veterans after the Chinese e-commerce giant goes public on the New York Stock Exchange in a record busting share sale.

A group of 27 managers dubbed the "Alibaba Partnership" will have the power to nominate a majority of board members, a structure that was unpalatable to Hong Kong's stock market and resulted in Alibaba deciding to list in New York.

Alibaba says the arrangement will preserve its innovative culture in a fast-developing industry and reduce distractions from financial market fluctuations. The plan echoes tech founders in China and abroad who say they need to retain control to keep alive the creative energy of their startup days and launch new initiatives, even if that lowers short-term profits.

Other companies including Google Inc. and Facebook Inc. also have tried to preserve control for their founders, often by awarding them a different class of stock with more voting rights. But research suggests such arrangements enrich insiders at the expense of other shareholders and in Alibaba's setup, some see a reflection of China's authoritarian politics.

"The Alibaba governance structure is probably inspired by the Chinese political structure," said David Webb, a former banker who operates the website webb-site.com about government and corporate affairs.

"The 'Partnership' is equivalent to the Politburo of the Communist Party," said Webb in an email. "The shareholders are equivalent to the People, who have no say in how their country is run."

Alibaba says its goal isn't to lock in control for its founders, who will receive the same stock as other shareholders. Instead, the company says it wants to create a collegial leadership group that can make long-term decisions. It says new partners will be picked from time to time by an inner circle of five members, including Ma and vice chairman Joe Tsai.

"This structure is our solution for preserving the culture shaped by our founders while at the same time accounting for the fact that founders will inevitably retire from the company," said Alibaba in documents filed with the U.S. Securities and Exchange Commission.

The arrangement allows Ma to retain control even though his and Tsai's shareholdings are outweighed by the 34.1 percent held by Japan's SoftBank Corp. and Yahoo Inc.'s 22.4 percent, said Zhang Tingyu, a specialist in corporate governance at the Chinese University of Hong Kong. Ma has 8.8 percent and Tsai 3.6 percent.

"Jack Ma worries about this situation: If the performance of the company gets really bad, can he continue to run it?" said Zhang. "That is why he set this up."

Ma, a former English teacher who founded Alibaba in 1999 in his apartment in Hangzhou, has stressed the importance of keeping the business flexible even as it grew to 22,000 employees.

Alibaba says more goods are sold on its online platforms than by Amazon and eBay combined. The company has spent billions of dollars over the past two years to diversify into mapping, taxi hailing, online finance and other businesses.

Ma, 49, stepped down as chief executive last year, saying it was time for younger leadership, but stayed on as chairman.

In his last major act as CEO, Ma launched an initiative to break up Alibaba's seven business units into 25 smaller divisions to respond more effectively to changes in the market. He called that the hardest "cultural transformation" in the company's history.

Alibaba's insistence on its partnership structure helped to sink plans for a possible stock market listing in Hong Kong last year.

The company turned to U.S. markets after Hong Kong regulators insisted all shareholders receive a voice in corporate decisions equal to the number of share they held.

By contrast, American regulators allow multiple share classes and other tactics to give some shareholders more voting power.

A 2009 study by Ronald W. Masulis of Vanderbilt University, Cong Wang of the Chinese University of Hong Kong and Fei Xie of George Mason University found dual-class companies tend to pay CEOs and managers more and deliver less value to shareholders.

To address that, Alibaba says partners must own stock to "align the interests of partners with the interests of our shareholders."

Candidates to become new partners will have to have worked for Alibaba for at least five years. Other requirements include integrity, a "track record of contribution" to Alibaba and being a "culture warrior" committed to company values.

Analysts say the initial public offering could value Alibaba at $150 billion to $200 billion, making each 1 percent holding worth up to $2 billion.

That could bring a windfall to an opaque group of outsiders who were allowed to buy shares in advance that could soar in value after the IPO. Alibaba's shares are expected to begin trading later this week.

Alibaba has released no details but Hong Kong news reports say the investors include a fund run by Jiang Zhicheng, a Harvard-educated grandson of former President Jiang Zemin, and other princelings, or relatives of Chinese leaders. Other reported pre-IPO investors include China's sovereign wealth fund, the China Investment Corp., and state-owned China Development Bank.

They bought a total of 5.6 percent of Alibaba, according to the Hong Kong magazine Asia Weekly.

Those links should help Alibaba obtain licenses required to enter finance and other fields, said Zhang, the governance expert in Hong Kong.

"That's another potential value for Jack Ma," said Zhang. "He has good government connections."