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SALARY AND SCAM

FINSHOTS COLLEGE WEEKLY

Finshots College Weekly - Salary and Scam

In this week's newsletter, we talk about Elon Musk's $45 billion pay package, the biggest crypto scam in history, KitKat's tax troubles and more.

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Elon Musk is overpaid. But who cares?

In 2018, Tesla's Board of Directors and most shareholders approved a sparkling pay package for the company's CEO, Elon Musk. And despite none of this pay hike being in cash, it was corporate America's largest by far. Musk would gradually get 12% more shares in the company, over the next few years depending on whether he'd achieve goals the Board had set for him.

To put things in perspective, these goals were split into multiple milestones. Say, pushing up Tesla's market capitalisation, increasing revenues or earnings before tax. And for every milestone Musk fulfilled, he'd receive 1% more shares than he already held. The final aim though, was to make Tesla a $650 billion company or simply multiply its market value (from the levels of 2018) by nearly 11 times over the next few years.

Yup, sounds like an audacious target, we know. But Musk was able to accomplish most of them by 2022. So, he was obviously entitled to receive the pay he was promised.

But Richard Tornetta, one of the shareholders, didn't think so. He took Musk straight to court because he felt that Musk didn't deserve such a mammoth payout. And he may have had some substance to his allegation because the court actually sided with him. It declared Musk's pay at Tesla excessive and cancelled it.

Why, you ask?

Well, for starters, Musk apparently controlled Tesla to the extent that other employees even considered him a tyrant. He not just occupied the most powerful roles of the Chair, Founder and CEO at Tesla, but also had his way with most things.

For instance, he made up positions and titles for himself without even consulting the Board. In 2021, Musk appointed himself "Technoking". In Musk's defence, it was a Chief Technology Officer that had more confidence and "great dance moves and sick beats". His antics even extended to pausing Tesla's acceptance of Bitcoin despite the Board's approval. Or even deploying 50 Tesla engineers to help him evaluate Twitter's engineering team. Again, without taking the Board's permission.

You could blame this behaviour on the Board's relationship with Musk. Musk and his brother Kimbal made up 25% of the entire board of directors. And the rest of them weren't really independent because many of them were friends who he was going off to vacations with.

So, this level of comfort with his so-called Board may have made him feel like he could always inform them of his decisions later. They could be Tesla's governing body just on paper but for Musk they were friends after all! And that meant that Musk decided how things would be done at the company.

He could use this control to prevent the Board from negotiating his pay by comparing it with packages offered to other high level executives of his calibre in the past. It was 250 times greater than the median peer CEO compensation in 2017. In fact, the plan's closest comparison, as you can imagine, was Musk's earlier compensation plan as of 2012. They'd even have to go chop-chop on his pay approval because it was Musk who dictated how much time or rather how unreasonably less time they'd get to review it.

Now, shareholders obviously didn't know of his dealings with the Board or the kind of power he exercised on them simply because they weren't informed of it earlier.

That’s what must have probably got them to sign off on his pay. They’d assume that an independent Board, unrelated to Musk and unbiased by his influence, approved Musk’s pay.

And all of this put together convinced the court that Musk had extreme influence over the whole process. Control was Musk’s quick fix to get the pay he imagined for himself.

After all, his personal ambitions of colonising other planets like Mars, were just as expensive. So he had to find a way to fund it.

But here’s the thing. A few days ago, Tesla’s shareholders sort of reinstated Musk’s package by approving it in a meeting all over again. Yeah, we’re talking about the same set of shareholders that the court felt had approved his pay nearly 6 years ago on the basis of misinformation and deceit.

So, why did they do it, you ask?

You could say “Hey, that’s probably what shareholders really want. Maybe their votes aren’t influenced by Musk’s control. Maybe he’s just a Superstar CEO who’s earning every penny of his pay but came across as intimidating to the court.”

Well, some shareholders may have thought in that direction, no doubt. But the real reason they redeemed his pay all over again may have simply been "control" itself.

Let's explain.

Look, Musk has his fingers in many pies. There's SpaceX, The Boring Company, Neuralink and now X (formerly Twitter). And not approving Musk's pay would simply mean that he could make surprising decisions like quitting from Tesla itself. And this isn't something we're making up. That's a threat that Musk himself had issued through a post on X. If he didn't get a total of 25% of Tesla, he'd simply leave.

Knowing Musk, this is something that shareholders thought could surely pan out if they'd disagree with his pay. And that would drive down Tesla's share prices, leaving them sandwiched in a court fight between Richard Tornetta and Musk himself.

Their best bet? Keep Musk happy.

And who knows? Maybe this will just motivate him to deliver even more value to shareholders. Maybe they really don't want to bet against Elon Musk.

The biggest crypto scam in history?

In 2016, Ruja Ignatova, a Bulgarian-born German businesswoman addressed a cheerful crowd at Wembley Football Arena in the United Kingdom.

She passionately exclaimed, “OneCoin is on course to becoming the world's biggest cryptocurrency so everyone can make payments everywhere!” She swore that it would be a "Bitcoin Killer", and that nobody would ever speak of Bitcoin in the years to come.

By then, the British had already spent almost €30 million on OneCoin. And extravaganzas like the one at Wembley only helped increase the rate at which these folks poured money into this strange opportunity

They'd seen how the renowned success of Bitcoin, a groundbreaking decentralised digital currency, reaped substantial profits for its early backers. And many of them who could not capitalise on this trend, did not want to miss the bus again.

Between 2014 and 2017 investors from Hong Kong to Pakistan to Canada ... and even Palestine invested over €4 billion in OneCoin.

But in 2017, OneCoin's anxious investors, who failed while desperately trying to convert their coins into cash, attended a gathering at Lisbon, Portugal. They wanted answers and waited for explanations from Ignatova. And guess what?

She never showed up.

Ever since, many international agencies including the FBI (Federal Bureau of Investigation) have been investigating her whereabouts.

But who is this mysterious woman? And how did she even manage to pull off such a legit looking cryptocurrency scam?

Well, let's take it from the top.

In 2014, Ignatova partnered with Karl Sebastian Greenwood to start a cryptocurrency. They called it OneCoin.

Now you'd think that it would work just like any other cryptocurrency. It would probably have to be mined on a decentralised network of sorts called a blockchain. For context, a blockchain is a ledger where every cryptocurrency transaction gets recorded and validated. And it's decentralised because it can run without any oversight or control from a single person, a central authority or even a government.

But with OneCoin things were different. Investors would just have to enrol for a OneCoin membership. These packages cost anything between €140 to €118,000. The bigger the package, the wealthier you'd become because the scheme was simple. OneCoin would sell educational course material with every package their investors bought. These courses covered stuff like cryptocurrencies, trading and investing. And this was considered OneCoin's main business.

Another thing that also came with these memberships was tokens to buy OneCoins. These OneCoins could be converted into cash on an exchange that the company built. So investors could buy expensive Guccis, Lamborghinis, villas or anything else they wanted. And since their coins would determine their value from the demand and supply on a blockchain it operated over, more people would mean a stronger OneCoin and richer investors.

It was quite a sparkling get rich quick scheme. And people were getting rich for real too. Because here's what we didn't tell you.

OneCoin's packages also lured its investors to sell OneCoins to their friends, family and acquaintances, so that it would eventually build a network and rake in more money.

To put things into perspective, imagine that you pay €1000 and buy a OneCoin package. You get access to courses, and tokens to more OneCoins. You then tell two of your friends to buy it. You tell them how amazing OneCoin's content is and that they can actually buy expensive stuff a few years later with the OneCoins they have. If you successfully convince them, you earn a cut for hiring new people. They carry forward this chain and the more people all of you have working under you, the more money you make.

If your friends don't want to join the scheme, that works perfectly too. You can still make money by just selling OneCoins.

And for it to seem genuine, OneCoin started off with large multi level marketing agencies that already had established networks of people. These agencies would obviously be able to quickly sell more OneCoins and memberships. So it would create the perfect mirage of huge earnings.

One successful multi level marketer based out of the Netherlands for instance, was able to make a whopping €90,000 in his first month itself! And many marketers like these would be invited to expensive parties and events like the one Ignatova hosted at Wembley. That's how tactfully OneCoin expanded its network. It was an apt pyramid scheme.

But for OneCoin's investors it was a flawless money minting machine backed by an Oxford alumnus, a PhD holder from Konstanz and an ex-employee of McKinsey and Company, a respected management consultancy firm. Yeah, Ignatova had quite an impressive background.

All of it seemed to be working just fine until one phone call changed everything. A few months after the Wembley's event, Bjorn Bjercke, a blockchain expert got a rather shocking job offer. The recruitment agent who contacted him offered him a hefty pay package and perks.

His role? — Create a blockchain for OneCoin!

Now, you can imagine what a whammy that would be. A cryptocurrency company had been operating for nearly 3 years without a blockchain!

And that tip off was enough to bring everything down like a house of cards. Bjercke blew the whistle on OneCoin and soon enough cryptocurrency enthusiasts discovered the truth. They found out that Ignatova and her partners in crime were manually assigning values to OneCoin. That's how its value really exploded. The course material they sold was mostly plagiarised as well.

These folks tried to alert OneCoin investors too. But the trust Ignatova had built was hard to break. Several global governments like Bulgaria, Finland and Norway even began cracking down on OneCoin's shenanigans. And in 2016, the Hungarian Central Bank warned that 'OneCoin' was a pyramid scheme. But despite these red flags, investors refused to believe that their 'Cryptoqueen' could be a scamster.

They only began to smell something fishy when OneCoin's exchange began to fall apart. See, investors who owned coins could convert their coins to cash whenever they wanted, on a private exchange called xcoinx dot com. OneCoin obviously paid them from a pool of wealth they'd created. It was like paying old investors with new investors' money. That's how pyramid schemes work.

And since this exchange set daily limits on how much of their OneCoin balance investors could sell, there wasn't a risk of investors withdrawing their money all at once.

But at the beginning of 2017, OneCoin abruptly shut down its exchange on the pretext of being under maintenance. Investors couldn't cash out. And weirdly, it never reopened.

The only way for investors to know what was really happening was to attend the OneCoin event at Lisbon where Ignatova would make an appearance. That unfortunately, never happened and it all began to make sense. Ignatova vanished into thin air, leaving her accomplices in trouble. Greenwood was sentenced to 20 years in prison and was ordered to pay up $300 million last year.

As for Ignatova, chatter around her plausible death has been doing the rounds since the last few days. Investigations suspect that a Bulgarian drug lord who she hired to protect her may have actually killed her

But without real proof the FBI won't strike her name off their top 10 most wanted fugitives list. Could that mean that Ignatova is still alive?

Well, we can't really tell. For all you know, she could be smartly faking her death to divert the attention of investigators, while living her best life on a yacht with the billions she swindled.

Today's Discussion 💡: When KitKat wasn't chocolate

Is KitKat a 'wafer with a chocolate coating' or a 'chocolate with a wafer inside'?

This exact problem troubled Nestle and tax authorities back in 1999.

Nestle had argued for long that KitKat was a 'wafer with a chocolate coating'' and ought to have attracted a tax rate of 10%. Plain and simple.

The tax authorities disagreed. They believed the product was a "chocolate with a wafer inside", liable to be taxed at 20%. They wanted to tax Nestle and they wanted it bad.

And finally, the matter was brought before the Mumbai Customs, Excise and Gold Tribunal

The tax authorities started with a bang. They noted—

“The product is a composite product consisting of chocolate, wafer and praline. It, therefore, cannot be classified as a wafer... It would also not be correct to say that wafer contains chocolate since it is completely covered by it. The predominant product in terms of value and weight is milk chocolate, comprising 68 to 72% by weight of chocolate and also value.

It is also considered by the manufacturer to be chocolate and treated as chocolate for purposes of storage and transport. It is perceived by the dealers of the product as well as its ultimate customers as chocolate and no person in common trade parlance refers to it as a wafer.”

Ipso facto, KitKat must be chocolate.

But the tribunal disagreed. Milk chocolate does in fact contain cocoa butter and cocoa powder. However, the mere presence of cocoa does not mean the preparation ought to be classified as chocolate. As they noted—‘While all chocolate must necessarily contain cocoa, it is not every cocoa product or preparation that is chocolate’.

As they noted—‘While all chocolate must necessarily contain cocoa, it is not every cocoa product or preparation that is chocolate’. They also observed that there was nothing to indicate that the product was being sold as chocolate. Their contention was that people were buying KitKat under the tacit assumption that it was a combination of chocolate and biscuit. They did not have any reason to believe otherwise. And as such, they agreed with Nestle’s classification.

KitKat was finally declared a “wafer” and that was that.

#AskFinshots 🙋

This week's question is from Tina from Delhi University. Tina asked, "Hi team Finshots. How did you raise your first seed round?"

Thanks for the great question Tina. Here's what Bhanu, our CEO had to say—

"Right out of college, our plan was to launch a stock broking platform. But we needed about 3-4 crores in capital just to set up the business. So our fundraising plan kicked into gear the moment we decided to start up.

We first met a businessman in Mumbai — a man who had made millions in the scaffolding industry. He was very enthusiastic about meeting us but then ghosted us after our first meeting. Fail.

We then approached VCs who were all equally eager to talk to us. But then never followed it up with a firm offer. After all, we were three rookies with 0 experience/know-how about the broking industry.

So we moved away from fundraising and started doing content, in the hopes of building a community. A community that we hoped to leverage in the future.

To compensate for the lack of funds, Shrehith started teaching on the side and Lokesh built a proprietary trading algorithm for a stockbroker in Ahmedabad, so that we could keep running the business.

In the meantime, we kept doing content. One year later, we got a call from someone in Zerodha saying that they liked our content. They asked us to fly down to Bangalore to meet Nithin and after a 40-minute meeting, we had finally raised our seed round.

Key Learnings:

1. It can be hard to raise money when you're building businesses that don't scale.
2. You may have to approach non-traditional VCs. For instance, Zerodha invested in us, not because they wanted a certain IRR (Internal Rate of Return) on their investment. But because they believed we'd add value to their users.
3. You can always try to run a tight ship with limited resources until you attract investor attention

P.S.: In the process we also ditched the idea of building a stockbroking platform and instead, we now run Ditto Insurance, an insurance advisory platform."

Hope this answers your question Tina!

Have a question for Team Finshots & Ditto? Write to us at colleges@joinditto.in and we'd see if we can get you an answer!

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