

GOVERNING FOR GENUINE PROFIT

Corporate Governance and Peace Conference

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Business corporations seek **profit**. That is, after subtracting cost, they **maximize net revenue**. **Spillovers** (both costs and benefits) involve **trade-offs governing boards should make**. Spillovers, especially when coupled with clumsy applications of **discounted present value**, distort a business' perception of profit. Today, businesses are buffeted by the old risks of recession and the **new risks** of terrorism. If modern society is to survive, then the **seeds of terrorism** and their fruit of tremendous loss must be contained. Accordingly, governing boards must propel businesses towards a **paradigm of genuine profit**. Governing boards must insist that their businesses prospect for **positive feedback loops** and implement a **sustainable profit stream**. In short, **governing boards must insist that business be entrepreneurial**.

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Business corporations seek profit.

Society encourages investment via limited liability.

Shareholders place their wealth at risk.

The Board of Directors and the Officers are fiduciaries.

The fiduciaries pursue shareholder wealth maximization.

Long run, not short run, maximization is pursued.

Profit is a net, but net of what?

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That is, after subtracting cost, they maximize net revenue.

revenue

Business is biased towards revenue.

Often, this bias is appropriate.

A sustainable firm must capture value.

However, the true goal is wealth, not revenue.

cost

Business is biased against cost.

Cost bias is greatest against internal costs.

External costs all too often are ignored.

An additional bias is of today over tomorrow.

All too often business eats its seed corn.

Cash profit is net revenue: total revenue minus total cost.

Cash profit is but one measure of value and of wealth.

Spillovers (both costs and benefits) involve trade-offs governing boards should make.

Markets reflect transactions of the willing AND able.

Spillovers (i.e., externalities) are involuntary transactions.

AT THEIR ESSENCE:

Board oversight is prioritization of the long run.

Prioritization is choosing between known options.

Choosing is accepting trade offs.

The realm of management is the near term.

The realm of the Board is the long term.

As certainty diminishes the role of the Board increases.

The Board must choose which externalities to internalize.

Spillovers, especially when coupled with clumsy applications of discounted present value, distort a business' perception of profit.

A dollar paid tomorrow is worth less than a dollar paid today.

When is \$1,000,000 tomorrow only worth \$1 today?

At 20% interest rate in 72 years.

At 10% interest rate in 144 years.

At 5% interest rate in 288 years.

Venture Capitalists strive for a return of 100% , or 14 years.

Iroquois management for the seventh generation is 134 years (or is it 210 years?).

The KEY QUESTION is:

"Will that \$1 be dedicated today for tomorrow's use?"

Today, businesses are buffeted by
the old risks of recession and the new risks of terrorism.

typical management of old risks

Minimize costs located internally,
in part,
by ignoring the magnitude of costs located externally.

new management of new risks

Strive to avoid the **tragedy of the commons**.
Seek out and prosper via **synchronicity**.
Business must anticipate more.
Because it is profitable, I am my brother's keeper.

If modern society is to survive,
then the seeds of terrorism and
their fruit of tremendous loss must be contained.

Risk can not be zero.
Containment is the maximum feasible success.

Contained terrorism might fail completely.
terrorism's maximum feasible consequences
versus
ability to bear and spread the losses

Terrorism's great and shared risks
increase the probability of **shirking** and, thus,
suffering the tragedy of the commons.

The seeds of terrorism are in our human condition.
a minimal price of life

poverty
illiteracy
ideological intensity
e.g., perversion of religion

the lesser angels of our nature

The fruits of tremendous loss are technological.

"minor" losses
specific physical assets
human casualties: whether few or many
major losses
network effects: whole > sum of parts
social psychological paradigms

Accordingly, governing boards must propel businesses towards a paradigm of genuine profit.

It is the duty of a corporate board to take ownership of the project to create the shift towards a paradigm of genuine profit.

The genuine profit paradigm shift can be irrelevant if:
too small,
too infrequent, and/or
too late.

Our gathering here helps belie predictions that the speed of diffusion of terrorist technology will render irrelevant the transformation of corporate governance.

Governing boards must insist that their businesses prospect for positive feedback loops and implement a sustainable profit stream.

All business opportunities requires prospecting.
grabbing low hanging fruit
versus

planting and tending the vineyard

A feedback loop is an expansive source of causality.

positive

freedom

negative

terrorism

Episodic profit stream often is falsely profitable.

Sustainable profit stream is truly profitable.

Life is reinforced and enhanced by sustainability.

In short, governing boards must insist that business be entrepreneurial.

Risk management is the primary task of any entity.
Legally limited liability does not limit ethical responsibility.

Legal and ethical risk management call for intelligence of design and operation as measured by the quantity and quality of the outputs relative to the inputs as well as the cherished values.

We all will fail
if governing boards maximize shareholder wealth based on their knowledge of the price of everything and the value of nothing.
