

**Robert A.G. Monks Transcribed Speech**

**Claremont University - November 11, 2000  
Peter Drucker Graduate School of Management**

**"Do Stock Options Provide the Right Incentives?"**

Thank you guys very much.

It is a great and single honor to be asked to speak on the day in which Peter Drucker's birthday is recognized. I perhaps come from about as far as you can come in America to be here, as I come here from eastern Maine and the weather is just about the same as it is here. I would like to say that if at any time anything I say stimulates any of you to ask questions or to throw something please do. I have run for public office. I have been insulted by experts. There really is very little that is going to disturb me, and if it would make the dialogue more fruitful please feel free to do it.

I want to say just a few brief words about Peter. His erudition and the range of his intellects and the extent of his sensitivity have long been commented on by many, many people. There is very little that I could add except the sense of awe, humility and gratitude. Perhaps an elements of which most of you are aware of, but I am particularly aware of is something very rare in this world and that is his generosity. How many people do you think in this world have sent papers, have sent manuscripts, have asked questions, have called on the telephone and have heard the wonderful "This is Peter Drucker". Peter has given, given literally to all who asked whatever he had. There has never been a sense but that his learning, his insight has been available to anybody who asks for it. I hold that out to you as being the ultimate model of what is possible for a human being to contribute. Beyond that I want to congratulate the Claremont Graduate School for having had the extraordinary insight to be able to acquire Peter after his first eight careers. You know, academe deservedly has a bad name for being so narrow. If you are a lawyer you teach in law school. If you are an economist you are an economist faculty. If you are a business school person, God forbid you should think of ethics or philosophy. But the magnificent thing that calling this school after Peter Drucker has signaled to the world is that the study of trying to spend your life creating value is a study that spans the entire academic spectrum. It is not simply a way for the greedy to get rich or for the poor to get rich, it is a way for people to spend their lives in expressing the genius within them in a way that creates wealth for all the world and at the same time does so in a way that is congenial to the interests of society. And by having someone of Peter's scope, you have given a signal to the world that this is the way in which we are going to train people for the 21st century. That is how we are going to continue and expand on the present situation that we have in this world of giving people - free people - an opportunity to improve themselves. And having a way of having a way of life and also having standards that are things that you can be proud of.

I have prepared some comments for you, even though I don't like talking from notes, so I will just have to keep pushing buttons to see if anything happens.

I thought Peter would appreciate Mark Twain [slide #2]. It is my effort to show my intellectual debt to Peter Drucker. Rather than having a picture of Alfred Sloan or something that was quite obvious in the context of commerce, I thought Mark Twain. "Well then, says I what's the use of learning to do right when it's troublesome to do right. It aint no trouble to do wrong and the wages is just the same." Now this is what I hold out to you is the sort of mindset of the modern American chief executive officer. The great problem of governance is what's right and how do we articulate what's right and articulate it in such a way that it is an intelligible incentive for the CEO and therefore sets the tone for the corporation.

The idea that how a corporation is governed is a relatively recent one. I believe in 1979 you could look in any dictionary of business terminology and look for the word governance and you wouldn't find anything. It's the notion of the last twenty years. And many people have been confused, they have said, well if you are worried about governance, you really should have been a clergyman. If you really care about these subjects, please go talk to the ethics class. But, if you really want to be a businessman, please come to this corner and here's the abacus.

McKinsey & Company is a very great firm and they are held in high repute by the people who run companies. McKinsey & Company does not make its money by telling CEOs of companies things that are offensive to them. So, when McKinsey & Company comes out in the year June 2000 [slide #3] and says that after surveying virtually all of the institutional investors in the world, I think some \$5 trillion under management, they have discovered that the investing world places a value on good governance. And that value depends on what country you are in. If you are in England it is 17%, if in Columbia it is 37%. It varies across the world. But stop and think for a minute, what can a management do relatively simply in order to increase the value of their company by 20%? How much do you have to increase sales? How many new inventions do you need? How can you achieve that kind of level of increase in value? So the world is saying to us a well-governed company is worth substantially more than a company that isn't well governed. But what is governance? What are you talking about? Well, McKinsey had a fairly straightforward series of questions that they used, but they boiled down to this -- does the board of directors function? Everyone who has ever dealt with the question of corporations and how they are run and how they are governed and how they are managed always comes down and says "a well functioning board things are good, bad functioning board things are bad." What can we as outsiders know about a board? I have been on 15 boards of companies listed on the New York Stock Exchange, and I can tell you that no outsider would ever have an accurate view of what went on in any one of those boards. Indeed, I didn't have too accurate a view of most of them. It took me about 30 years of being on boards to figure out one or two things I actually could do. But that isn't good enough. We need a proxy for whether a board functions well or not. I have studied this for some time and a proxy that has suggested itself to me is this. If a board has in place a system by which they pay the CEO in a way that benefits society and provides an incentive for the corporation to perform in ways that are societally useful, and that rewards the CEO as long as the stock holders are rewarded, that would be a well governed company. If on the other hand, a CEO is paid in a way that ignores societal considerations and in which the CEO gets paid whether or not the shareholders do well, that is a poorly governed corporation. And the difference, as I am saying, is not an insignificant one. It's 20% on the value if that perception is shared. It's also worth knowing that the SEC requires that contracts be filed with the SEC. They are very hard to find. My partner, Nell Minow and I have a page called [www.thecorporatelibrary.com](http://www.thecorporatelibrary.com). We have on file all the top 500 company CEO contracts. I think after two years of begging, borrowing, weeping, Xeroxing - we have about 320 of them. But it's quite interesting. They are now available through our page, and so we have had some learning on the subject.

One of the aspects of governance is what kind of structure do you set up. And the board of directors is the critical first place you look. [slide 4] This is what the board does in terms of compensation. Of course, the board selects the CEO. The board approves his employment contract. The board administers the option program - theoretically the option programs are ratified by the shareholders. And the board creates the compensation committee. I want you to think for a minute of who comprises the typical American board. The typical American board will have the CEO as the only full time company employee on the board. The other people on the board are a variety of people who were selected according to a strange number of processes, all of which I can tell you from my own experience, which isn't vast, but certainly isn't Peter's. I have been working for the last 50 years quite hard. It simply doesn't work. These are part time people. Let me recount to you a conversation I once had with a CEO of Eastman Kodak. A very charming man named Kay Whitmore. I came to call on him because the stock had been doing very, very badly, but he seemed to find that I wasn't just completely a ludite. I wasn't there just to be mean, I was genuinely interested in trying to help get the stock up and to see if he could do something about it. We were talking about his board and he said "I wish you people would get your act

straight" (he was an engineer). I said what do you mean get our act straight. He said "well, look, people came around here and they told me I had to have a board with women, with blacks, with minority groups, with college professors, and that is what I had. Now you are telling me I need to have a board that contributes to the corporation." That is a fairly graphic example of the confusion that has existed about whether boards are for appearance purposes in order to make it appear as if there is a level of accountability, when really there is very little. Or whether boards are actually going to be a responsible dynamic force. In this context of setting pay, I set this out for you explicitly so you could see the steps. They select the CEO, maybe they do, but does the GE board select Jack Welch's successor? Anybody who thinks yes? They improve the employment contract. I suppose. Have you ever read one of these employment contracts? I have read a lot of them. Everyone in life should read one. Two you can possibly be excused for, after that you really are indeed into masochism. They are incomprehensible. If you think of a part time person being on the board and having the complexity of material served up to him on behalf of someone, who, if they didn't pick them to be on the board, at least had to say their being on the board was congenial to them. That is the sort of structure in which we start, which is not promising.

I would like you to consider another element of compensation in the world today. Virtually all of the television networks are a part of huge communications conglomerates. It is very difficult to have information volunteered on subjects that are offensive to people who control advertising money. The New Yorker magazine is I suppose part of a conglomerate, but it is part of a privately owned conglomerate. This [slide 5] "appeared" recently there about why the program 20-20 would not communicate a piece about executive compensation because they were concerned the CEO of a parent company who has a controversial compensation arrangement would be upset. I take this as being fairly accurate of circumstances today. So it is quite hard to get a sense of public involvement in the question of compensation.

I have two slides [slides 6 & 7], which I put together in order to give you a way of dealing with one of the most difficult problems in talking about performance and pay. I just want you to look at these various lines. I am trying in one slide to show you the different perspectives - you have always heard about short term and long term - that doesn't mean very much. What I am trying to show you here is a variety of people whose involvement in our dialogue this afternoon will be important. What their framework is. A stock trader is instant. You desire to buy or sell, the transactions are immediately available. On compensation for executives and directors, I take cash being 10% of the total, bonus being a bit more and options being about 80%. Options are probably a 5-year framework. No one has yet been able to give me a situation where someone exercised their options and held the stock. The exercise of options is immediately followed by sale of the stock. So that is about a 5-year framework. Then here I introduce another category. You will see later in my comments why. Pension funds basically are invested in order to collateralize a promise for retirement income to people who, on average, will retire about 18 years from now. The framework for pension funds is about 18 years. Increasing investment by institutions, pension funds, preeminent among them, are index funds. Index funds are forever. Index funds own everything and they own it forever. It's important to keep those in your mind. Here I have just a couple of relatively simple concepts that most of the traditional standards of performance, like earnings, cash flow, EVA, or whatever your patented word is for that, market value of the stock, they are all sort of in that time frame. Then, the concept of sustainability - pollution, "contumacy", which is a word I love - what it means is the company is trying to buy the country through campaign contributions and things of that nature, or trying to get the Congress to appropriate more money for corporations than for individuals, which is the current situation. The time period for sustainable concepts is vastly longer than the time period for conventional concepts. Now we will move on.

You thought I would never get to the title of the speech!

Options, when I am talking about options [slides 8], I want to be very clear. I am talking about options in the context of very large publicly held companies. I believe that there is a real use for options in start up companies and in small companies. When I am talking about options, I am

talking about options as they exist for the CEOs of the Fortune 500 or the Fortune 1000 or what have you. I am not talking about it in a venture capital context. As you know, options are the miracle compensation. If at the end of the year your CEO has added \$100 million by whatever calculation you make to the market value of the company, and you think he should have some it, like for example, a local company here thought that their CEO had done very well and they gave him an airplane. You can do that. But if you give someone an airplane or you give them cash, you have to charge it against revenues. It's an expense. But if you give them \$100 million worth of stock options and the worth is Black Sholles model, which is used to trade options by the trillion all the time, no P&L impact. What is that expression about bad compensation drives out good? Essentially, if you are there and you have two choices - one lowers your earnings and one doesn't - hey, you know.

There is another point, which is very rarely commented on, but as the NASDAQ average comes down you might think about it a little bit. When the executive exercises his option, the company books an expense for tax purposes of the difference between the exercised price and the issue price. Those are some not unfamiliar names. Dell - let's just stop with Dell and Sun. What this slide [slide 9] says is "The impact of the tax benefits from the exercise of employee stock options on operating cash flow." For Dell Computer that little gimmick is 26% of its cash flow or a little over \$1 billion. That's something to keep in mind as the NASDAQ keeps going down. It is just simply part of why options are so popular and possibly is one of the reasons why they are so unwise.

The difficulty with options in the context that I put them is that they really are a one-way street [slide 10]. Everyone says "oh my gracious, the best thing we can do for governance is to align the interests of the executives and the stockholders, so that executives make money when stockholders make money and when stockholders don't make money the executives don't make money." That isn't what options are. We see repeatedly in this time of falling stock prices that when the stock price goes down, options are rewritten. They are our one-way alignment. They align when the stock goes up but not when the stock goes down. It's quite apparent that if you are the CEO of a company and you have an option, that your time frame - remember back to my not as simple as I would have liked charts about timeframe - your time frame is probably about 5 years. So there is in a way a pressure for a shorter-term strategy [slide 11]. It is hard to put your finger on it, but let me give you one company you might think about as having a shorter-term strategy - IBM [slide 12]. IBM the great success story of one of the McKinsey wonder child's. He came back from the dead, he is a veritable Lazarus. He has reissued himself some more options and what does he do? Well, they use cash to buy back their capital, which of course impacts the earnings per share, but then in the last couple of years they have done something else. IBM has always had the reputation, the soul if you will, of being the most employee friendly organization in America -- worth tremendous loyalty. They cancelled the defined benefit pension arrangement for the IBM employees. Now at two Annual Meetings employees have appeared in protests and there have been talk pages and all kinds of things of that kind. To put it mildly, they have lost the good will of their employees who have in many cases been done out of a great deal of their expectation for what their pension might be. Is that because the compensation system for the CEO is something that is relevant within a five-year time frame? Is that the kind of judgment you make if you were CEO and you were going to be compensated on what the company was worth 20 years from now? So here is where this question of timeframe is important. I'm not critical of CEOs as a category, I'm simply saying the incentive system that they are presently under, particularly with options, inclines them to think of the five year picture. Where as if you were thinking of IBM in the long term, I don't think you would want to adopt policies that alienated your most critical category, which is the morale of your employees.

Here I just did a slide [slide 13] so that you would have a fairly graphic sense of the kind of questions that the compensation committee has. On the left hand side, I say restricted stock and on the right hand side is option plans. I was on the compensation committee of a company that has now become very large called Tyco International. I think it is the 27th largest company in the world now. It wasn't when I was there. We had the policy of very low pay, and we gave restricted

stock to the executives, a lot of restricted stock. Indeed, the CEO of Tyco last year earned \$187 million. When we issued the restricted stock, it was a taxable event. We took a hit to our P&L for it, and the executive, as his restrictions lapsed and he vested, realized income. We loaned him money to pay his taxes. Now what did that mean? That meant that at the end of the day he has one asset, Tyco stock, and a lot of debt. We have his attention. I can well recall the board meeting of that company in a year when our stock had gone down and the directors took all of their pay in stock. I looked around the room and I started to laugh. People said, why are you laughing. I said well you know, I look around the room and here are a bunch of otherwise very intelligent people and guess what - we all worked for nothing last year. They said what do you mean? I said, well the value of stock that we owned is less than the amount that we got paid last year. It didn't happen again. That is the difference between restricted stock and option plans and that is the difference between having directors who have a very substantial economic interest in the venture and ones who don't.

In terms of thinking of a policy for compensation, I am going to be talking with you about two concepts [slide 14]. One is the current fair market value. The other is the idea of future sustainability. I am going to suggest to you that a proper compensation policy, a properly functioning corporate board - a properly functioning compensation committee - will attempt to identify for that company those elements that permit future sustainability. That means that the impact of that corporation on society must be something that gives one every reason we can imagine to believe that that company can continue to operate in the same way in the foreseeable future. This is the most difficult concept that I am going to try to explain this afternoon, so I will leave it up for a minute [slide 15]. I will read it for you: "Are long term elements essential to sustainability incorporated in the current stock price?" As you might have heard James Baker say on the television recently about the Florida vote count, you can start on a slippery slide here. The slippery slide is that if you don't accept the market as value, then you are accepting something human beings have said from their best intelligence they think is true, which may or may not be true. I am raising for you the question: is the market the only test for what is an appropriate compensation system? I quote here from a letter written to me in 1993 [slide 16] by a local resident, indeed he is sitting in the front row. It is one of our several conversations in which Peter did me the very great favor, with utter civility, pointing out that I didn't really understand what I was doing, a process that I expect to continue this afternoon, for which I am most grateful. But without reading all of it, what Peter says - which I think it ought to be inscribed in every place of study of business - is that the stock market is surely the least reliable judge or at best only one judge, and one that is subject to so many other influences as practically impossible to disentangle. What of the stock market appraisal reflects the company's performance, what reflects caprice, affects the whims of security analysts, short-term fashions in the general level of the economy and of the market itself rather than the performance of the company? It has never been better said. That is the problem. People like to believe - there are a lot of myths we live by - I have already mentioned one, the board of directors. Another myth is the market. The reason why people want to do it is because humankind doesn't like uncertainty. We don't like living with ambiguity, particularly in terms of compensation. We love to have a formula. Give me a formula. If I have a formula it may be good, it may be bad but somebody's not going to be mad at me the day after Christmas because they knew what they were going to get. I'm not going to lose somebody because I made a mistake, because they knew what they were going to get. Everybody wants certainty. I am sorry; you are living in the wrong universe. You don't get certainty. Corporations are too important to try to have refuge behind the notion that the market is an acceptable criteria for the direction of your corporation. We have to do more than that. The market is like the jury system. Everybody knows that 13 or 14 good men and true haven't got the slightest idea what the evidence suggests about the anti competitive aspects in an anti trust case, or perhaps in a murder case. But it is less bad than any other way of trying to do justice. The market has been accepted because it has been thought of as being the less bad way of doing it. I am going to suggest to you that I think we can do better than that. The market itself is really unacceptable.

Just to give you an idea, that the market is not blind utterly, I'm putting up for your consideration two very well known universal companies. Coca-Cola and Philip-Morris [slide 17]. They are very common; they have all the money in the world. They can hire anybody they want to, they are brand names that are known in every continent of the world. They sell mildly addicting or very addicting products and they are susceptible of being purchased by caprice. You don't have to worry if you are going to buy a pack of cigarettes or coke. While cigarettes may kill you, Coca-Cola will ruin your teeth. The market in its wisdom has said that Philip-Morris is valued at 8 times earnings. Coca-Cola is valued at 36 times earnings. They are virtually the same kind of company, and yet the market - the "e" factor - is the one that was always studied, but the multiple that the market puts on it is vastly different and I suggest the reason is (and this is an extreme case) is that the market has said that we do not believe Philip-Morris has the ability to repeat these earnings at this level for the foreseeable future. We believe it is very finite. We believe that they have offended the public sensitivity to such an extent that they will be susceptible of taxation, regulation and other value diminishing reactions from society. Whereas the market says Coke is a good company, people like it, it is sweet. There isn't too much of a constituency for teeth.

Having explained to you sort of generically how there is a subjective factor that goes into value, which is the Coke Philip-Morris factor. I now want to go to a very, very tangible measure and this is a company called Innovest [slide 18], which is a company that does the best work I know of now that has analyzed major industry classifications and the companies that comprise them from the point of view of how well they organize their impact on the environment. They have done it for all of the companies in the S&P 500, they have done it for the FTSE 100 in England and they have concluded there is about a 25% gap between the half of the companies with the best environmental attitude and the half with the worst environmental attitude. So you are beginning to get a sense that value can be related to a company's attitude -- that the earnings are the same, the cash flow is the same, but one company has an environmentally sensitive posture and the other not. This is the beginning of this work. It is available for several of the major industries. This happens to be a recent one on the oil industry.

By way of illustration [slide 19], and this is something you can take away with you. Watch over the next several years the major oil companies. Exxon, a notably insensitive company, said relatively recently that here are our numbers, we are the best company in the industry. We have heard about all of these guys flapping their wings about the environment and all that kind of stuff, but that's just - look go to church if you want that stuff. For us it is cash flow and earnings and we are the best. We are not going to invest just because it is the thing to do, says Lee Raymond. So they now are the biggest, and, they say, the best and in contrast, we have Shell. Royal Dutch Shell is a very proud enterprise. It is a little hard to call it a business because it is almost a social institution in the sense that maybe big Japanese companies are. But Royal Dutch was very, very stung three years ago when they provoked a consumer revolt of the Greens in Germany on the occasion of their Brett Spar drilling rig disposition and their alliance with the major political party in Nigeria at a time they were hanging the minority. Shell is very conscious of this. They are the first people to have literally devoted their principal corporate energies to try to define what are the values by which the venture will be guided. This chart [slides 20-24] - I am going to spend a minute going through it, the base of the chart is governance and values. You can read the captions - I am showing them to you here not because they are the final word, but because of what a very major enterprise has tried to do in breaking down the categories and the way in which the process by which they will identify sustainable values. So they think it starts with integrity. It has to do with the stakeholder's perception of quality of engagement. It then moves to three areas in a second level, the economic, the environmental and the social. In the environmental area I showed you the Innovest slide that began to show how they are beginning to quantify that. Now the difficulty is that at the end of the day you get to the top of the Shell pyramid, which is SD (Sustainable Development) Performance. You see the whole glorious panoply unfolds. What they are trying to do over time is to develop matrices for each of these, and that is what KPI is (key performance indicator) with the orange boxes - squares. They are trying to attach numbers to those even though it is extremely difficult to take the written language, reduce that to a number that is anything more than just a guess and then try to integrate that in with the conventional

numbers that accountants produce. So probably where Shell is now is they have two columns. One column will be their conventional earnings and the other will be some form of matrix that represents a valuation here, and I suggested to you, at least in the environmental side, it is possible to begin to get some fairly hard numbers.

This is where I have been leading [slide 25]. When integrated numbers are achieved, stock values alone will be suitable. Remember Peter's letter? The worst criteria in the world is the stock. He is right. What I am saying is that if you can do what Shell is trying to do and classify the ways in which the corporation adversely affects the world around them, and put numbers on it, you will then have the possibility for true cost. To put it by way of hyperbole, if every time you smoked one cigarette, it cost \$10, there probably would be a lot less smoking. And yet you might have something more nearly approximating the true cost. When integrated numbers are achieved, and I say that in the context of those Shell slides, because it will take a great deal of work and a transition from words to numbers in order to achieve anything like an integrated standard. I have asked Shell about this, I have talked with Mark Moody Stuart very recently, who is the CEO and he says - "Look I'm not sure we are going to be able to produce a single number." People talk now about the triple bottom line. You saw the three pieces there that I had in the Shell chart. What I am saying is that we possibly get to the single bottom line, because that then means that the largest single problem with using the market is solved. The largest problem with using the market is that the market only has the information that people provide it. If you say that people have to provide the information that is in the Shell taxonomy, you then at least have an informed market to produce a value which you could then use as a basis for compensation.

By way of contrast, this is British Petroleum [slide 26], which is a very interesting company now. The CEO is a man by the name of Sir John Browne who is a very distinguished chemist. It was never thought that Browne would get out of the laboratory, but when he did, he has staggered the world. Browne is the first energy company executive to say there is such a thing as global warming, there are particulate emissions. We are responsible in part for both of those phenomena. We consider, in running our company that we have to take steps to stop that. That is in absolute contrast to Raymond's attitude as the CEO of Exxon. That is why I mentioned to you a minute ago you have a battle going on here and you can watch it. You can see how does the market value the short term view of Exxon and how does the market value the long term view of BP. Sir John Browne has committed BP to reducing the particulate emissions by a specific amount by the year 2010. The year 2010 is not the year John Browne is going to retire. It has nothing to do with his options. It is his determination as the responsible executive of this venture with its huge impact on humanity, that this is what they should do in order to be a sustainable enterprise. One has to hope, and it is a hope. Intuitively you think it is true, but you have to say it is a hope. You have to hope that the market will reward BP because if the market doesn't reward BP, they are going to create a lot of problems.

I have mentioned Shell to you, but I put Ford Motor Company up there for another reason [slide 27], I think the company committee should articulate standards. The Ford Motor company, as far as I know, is the only company now in the world that bases the bonuses of its top 30,000 executives - one half on their achievement of a criteria that is not linearly related to current earnings. They have made the effort to try to define what is customer satisfaction. As they say, look, we are as a company nothing if we don't have satisfied customers and therefore customer satisfaction must be the informing energy of the executives of this enterprise. They have made the effort to try to break this down into a matrix that has three components which basically are (i) how did you feel when you bought the car, (ii) how do you feel a year later, (iii) how do you feel three years later? The Vice President in charge of the program, I talked to and the chairman of the compensation committee say "look, we know people can be self serving here. We don't expect that this is going to be totally accurate. What we are trying to do is to create an organizing sensitivity for the executives of this company and hence for the company. The company and whatever people in this company do, that it be sensitive to the needs of customers." And that is how they do it. And that is a model in my view of how a compensation system ought to be achieved.

The Ford Motor Company, as is pointed out to me repeatedly, had been either the beneficiary or the victim - depending on how you look at it - of having a controlling shareholder who is now represented as the Chairman of the board. You may remember that Bill Ford very recently had said - I think in April - that the company really was considering their recreational vehicles and the impact that they have. They both emit too much particulate, they consume too much gas and they are rather too dangerous to other cars on the road. And even though they are the principal source of profit for the Ford Motor Company, he said we are going to try to do something about this. So you begin to get the introduction now of standards that are not short term, that are identified with the concepts of sustainability and that may or may not be congruent with what the market recognizes.

If I have achieved anything graphically this is it [slide 28]. It has taken me a long time to learn what I have tried to tell you and I hope I got most of it right. What I am trying to do is to say, and this was the bottom of Peter's letter to me 10 years ago, Peter is the person who said never, never, never talk about value maximization. He used the felicitous term value optimization. I should have a footnote; indeed this entire field of corporate governance should have a footnote. And you know what the footnote says? "Derived from the life and work of Peter Drucker."

Optimize value - a Druckerism. This is market value as informed by true cost accounting. True cost accounting was my effort in three words to summarize the previous ten slides. This has to do with the market value with, if you can imagine, all of the Shell matrix worked out so that it is an informed market value. Then I say above - "elements supplemental to market value." This is, I want to remind you, that in trying to be a responsible corporate citizen, what is essential is that you take the trouble to identify - God knows in this world you have got to have humility, you may be wrong, but you've got to try to identify what is it that we have to provide by way of specific guidance for how this corporation functions in society so as to ensure that it can continue its profitability and that society can continue on a sustainable basis. So you end up with informed market value plus the obligation to identify those particular characteristics for each company and its impact on society.

At the end of the day, I go back to my slide [slide 29] about timeframe. Who in the corporate equation has the motivation, the ability, and the power to make the determination of long-term values? The CEO probably is only going to see five years out - eight years out. The directors are only going to see eight years out - five years out. Only the long-term shareholders have a concern with long-term value.

I like this chart [slide 30]. I put it together and I said I like it. You see, everybody's always said that the law says that the board of directors should run the corporation for the benefit of the shareholders. I finally figured it out after all of these years. No one has ever told you what a shareholder is. Now is a shareholder some arbitrageur who owns it for a nano second? Is a shareholder a program manager who has a wonderful computer program that buys and sells the whole portfolio three times in the morning? Is it an active manager who goes up and down depending on whether he whispered in somebody's ear? Are they mutual funds who are buying and selling stock because of the tax characteristics of their impact on people? Is it a bank trustee who doesn't do anything because it's cheaper and easier? Is it an insurance company? Is it a pension fund or is it the index funds who we know hold forever? And in my view, the pension funds provide the perfect proxy for the shareholder. The reason being is first, that they are long term, the average period of time of holding will be 18 years until there is retirement. The second thing is that they have beneficiaries whose interests you can determine. You can't tell who is the beneficiary of a mutual fund, they are everybody. I mean, they are long term, they are short term, they are rich, and they are poor. A pension fund beneficiary has the following characteristics: they want enough money to be able to live decently on retirement. They want to retire into a safe world. They want to retire into a clean world. They want to retire into a civil world. So when you understand that, when you say shareholder, you mean pension fund beneficiary, you then have gone a long ways toward articulating a series of standards that are susceptible of being enforced.

So when you say to a director, are you running it for the benefit of the shareholders, you mean are you running it for the benefit of the pensioners. And that gives you a set of standards, which we have never had before. So, in trying to figure out how to put together a well governed company, a company worth the full 20% premium and maybe more, you have to think of having a management structure and I have suggested here [slide 31] a rather strange suggestions, that the compensation committee needs to be expanded with additions of long term shareholding trustees. Now my view is that you probably don't ever want to put institutions on boards of directors, but that doesn't mean you can't put them on the compensation committee. And in my view, if you really want to take a large step toward running an enterprise in a way that is congenial to the interests of society, that has sustainable values, you need to put on in the place where the critical decision is made, somebody with a long term viewpoint to create the compensation system that will reward conduct that is congenial to society, which I suggested Sir John Browne and British Petroleum, in contrast to a rather mindless formula that simply pays people in stock that doesn't really reflect adequately any values. At the end of the day, I think that the best governed enterprise will be an enterprise that has long term shareholders as members of the compensation committee.

Thank you very much.