What's a Business For?

My thanks to Charles Handy for asking the right questions at a moment when answers will attract sober action. His "What's a Business For?" (December 2002) is right on the mark. But while Handy's question is brilliant, his answer is misleading.

When he quotes Dave Packard in answer to his question, saying "a group of people get together and exist as...a company [to] make a contribution to society," he puts sole proprietorships out of the bounds of business but puts political parties, churches, terrorist cells, and clubs inbounds. This mistake is not accidental. By defining a business as civic humanists define a community – a group of people freely making their own destiny – Handy forgets the battle we consultants fight against both the civic humanism of Hannah Arendt and the economic liberalism of Milton Friedman.

Who would deny that we experience business at its best when we are, as Handy says, a chosen few joined together to make a significant contribution to society? That's what makes any business worth joining. But a business's social contribution, no matter how infinitely valuable in history's eyes, is always focused on caring for certain necessities of customers and owners. A business is not a community but an establishment (even of one) that forms its own destiny by taking care of needs others will pay for.

Today, consultants spend much time helping managers change course from profit disciplines that have turned stultifying and from company love fests that have produced doomed innovations. Like it or not, business uniquely is about both love and money: two gods, not one.

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Many of those we have come to call "investors," Charles Handy points out in "What's a Business For?," paid their money not to the company itself but to the party that previously owned the shares – an important fact that is too often forgotten. Handy implies that these investors should not then receive dividends.

However, there is still a case to be made for paying a dividend to such an investor. By buying shares on the market, an investor indirectly contributes value to the company. First, the increase in share price due to the demand in the market will raise the company's currency for acquisitions. Second, the stock market demand will increase the company's image value – through, for example, the reinforced media coverage.

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Expensing Options Solves Nothing

We at Towers Perrin read William Sahlman's recent article, "Expensing Options Solves Nothing" (December 2002), with great interest. We agree, but for different reasons, that expensing stock options is not a panacea for the current problems with executive compensation and corporate governance. In fact, a recent Towers Perrin study indicates that investors have already considered the effect of options on companies' performance.

We tracked investor response to more than 100 companies that had announced since July 2002 that they would expense options on their income statements. We examined the companies' share prices for the 60 trading days before and after their declarations. Their share price performance was the same, on average, as the S&P 500. The accounting advantages of stock options are apparently not valued by the stock market any more than favorable accounting for inventories or mergers was in past studies.

We also agree that the real issue with current accounting treatment for stock options is that fixed-price stock options are not treated in the same way as other forms of equity compensation. The favorable treatment of fixed-price options has contributed to a bias toward this compensation method despite its relatively weak connection to the day-to-day operating decisions most managers are responsible for.

That bias may be removed in the future as more and more companies reexamine the true costs and benefits of their current compensation programs. We expect that future compensation programs will continue to include fixed-price options but in lesser proportion to other equity- and cash-based designs. We also expect that most companies will focus more strongly on rewards tied to long-term operating results (decoupled from share price fluctuations), and that they will place a greater emphasis on business unit incentives. Such enhancements will help bring executive compensation back to its original purpose of providing strong incentives for managers to maximize value for investors at a reasonable economic cost.

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How to Stay Stuck in the Wrong Career

Herminia Ibarra's thoughtful article on changing careers, "How to Stay Stuck in the Wrong Career" (December 2002), makes a valuable contribution to a complex subject. I particularly like the analogy of the journey following a crooked path. However, to suggest that people have to be willing to abandon everything they have ever been taught about making career decisions is, I believe, unhelpful. Counseling people not to listen to the usual advice is not a good starting point in any journey. People moving through significant transitions deserve the opportunity to access a wide range of advice, some of it conflicting.

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