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Understanding true risk

A number of years ago, the father of a good friend of mine died. By most accounts my friend's father was rich, basically a good Christian family man, and generally considered a benefactor of a local Christian University.

This man was a Korean War veteran who returned from the war, sold his interest in the family Eastern Washington farm and used the proceeds to move to the coast and purchase a dairy. Over time he enlarged the dairy and expanded into manufacturing and distributing of a full range of dairy products. From there he built a small chain of supermarkets and invested in real estate.

My problem with this individual was that he considered his wealth to be his own and should have known better. He was quite happy to be considered a university benefactor, even though his contributions were quite modest, compared to his overall wealth.

When you actually looked at what he was able to do, his success wasn't really due to his business acumen. His success was brought about, by being in the right place at the right time, with a sufficient capital stake, and really not taking any risks. He raised his family, spent way too much time putting all the pieces together, and didn't do foolish things with the money that came his way. So on reflection I suppose it was his money.

In contrast in my early entrepreneurial days, I had two mentors of that same vintage. These two mentors combined probably had processed twenty times the wealth of the benefactor. They looked at their wealth as an opportunity to invest and contribute to the greater community, and essentially looked at their money as a scorecard for what they were doing, not who they really were.

In Moses' admonition to the children of Israel in

Deuteronomy 8, he makes it clear that the author of all wealth is the LORD. In other words, wealth is a gift, and how you use your wealth will one day be judged along with other acts you have been associated, some good, but most evil. One evil is to consider any wealth you may have obtained, to be yours, something personally sacred, that you truly earned in response to your labors.

The New Testament application to this specific revelation of Law is found in a parable presented by Jesus in Luke 12:16 28:

Then He spoke a parable to them, saying: "The ground of a certain rich man yielded plentifully. And he thought within himself, saying, "What shall I do, since I have no room to store my crops?' So he said, "I will do this: I will pull down my barns and build greater, and there I will store all my crops and my goods. And I will say to my soul, "Soul, you have many goods laid up for many years; take your ease; eat, drink, and be merry."' But God said to him, "Fool! This night your soul will be required of you; then whose will those things be which you have provided?'

"So is he who lays up treasure for himself, and is not rich toward God."

Then He said to His disciples, "Therefore I say to you, do not worry about your life, what you will eat; nor about the body, what you will put on. Life is more than food, and the body is more than clothing. Consider the ravens, for they neither sow nor reap, which have neither storehouse nor barn; and God feeds them. Of how much more value are you than the birds? And which of you by worrying can add one cubit to his stature? If you then are not able to do the least, why are you anxious for the rest? Consider the lilies, how they grow: they neither toil nor spin; and yet I say to you, even Solomon in all his glory was not arrayed like one of these. If then God so clothes the grass, which today is in the field and tomorrow is thrown into the oven, how much more will He clothe you, O you of little faith?

If I had ten percent of the riches of Christians I have run across over the years, who believe it is they who have made themselves rich, I could have a mansion in Medina along with Bill Gates.

"O you of little faith." There are some religious teachers that make a great deal of money telling you that faith is a force, and if you too want to have a lot of money you must get into the force, and the faith force flow will make you rich. How you do that is essentially follow the religious leader by contributing significantly to his faith force ministry.

If you look at the context of the Bible however, you find out that faith is really a complex gift, created by God, to do His will, in you, and in the world generally. As a gift you are to manage the substance of what is given to you. I teach, as many others I have known over the years, the opposite of faith is not unbelief, but fear.

Fear, overcoming it, or falling victim of its doubts, is the greatest operating principle at work in the world. That fear is rooted essentially in the fear of God, but people can invent or create almost an infinite number of schemes to prove otherwise. If mankind truly had created the infinite subterfuge, then he would have achieved the goal, described by the serpent in the garden in Eden, we would have become as God.

What has happened as I write these words is one of these complex programs of fear of God and His judgment has begun to unwind or fall apart. We can call this the subprime mortgage crisis, or blatant energy speculation, or a credit crisis, or we could go on, and on. The real problem that no one will admit is that atheistic evolutionary materialism is really just a fear Ponzi scheme, and average investors, or taxpayers around the world, have been left holding all the liabilities.

You were taken in by all of this, essentially by never looking seriously at the risk you were denying, by placing the majority of your wealth in either real estate, or publicly traded stocks, or even a more risky get rich quick Ponzi game. You got into the game in either the 80's or 90's led by someone similar to my friends father, who really had never taken any risk, exercised any faith in their lives, and still had benefited greatly, well beyond their wildest dreams.

To be honest however, you find these people not only in church and the secular world, but also on the libertarian right, many which, did take some risk. However this all took place in a historically unreal world of generally increasing wealth, until the end of time, or the Rapture. That end of time economic model is now broken, the Rapture remains, still

emphasizing a less than 200 year theological history.

So how do you overcome fear with faith? As with anything else, practice, practice, and more practice. Duh! Perhaps a better question is how do you begin, slowly and gently?

Since we have been talking money and wealth and the real problem is lack of confidence in the world's financial systems, perhaps you might be interested in investments more or less risky than putting it to interest in a bank?

As we discussed last week, you can invest in a small publicly traded company in the United States or elsewhere. In reality however, with the financial requirements to list securities in the United States, the real wealth has already been created and distributed to the founders. Just check out Bill Gates, Steve Jobs, and many others.

As an interesting sidelight, most of these new technology companies were created in the time of high marginal tax rates, before the so called Reagan Revolution. Ponder that over your next 5 cup of Starbucks coffee, which at that time was a tiny coffee shop and roaster in the University Village, a small shopping center just east of the University of Washington in Seattle.

You might know a Sarah or a Joe, who has a good idea, good business acumen, and who, you believe, could build a small company to a level where it really could benefit from a public listing. There and only there, working with the original founders and investors, can you achieve your own small piece of the Bill Gates legacy.

So we have just answered the first step of the process. You know that Sarah and Joe, are straight shooters, and while they may fail, they will do as best as humanly possible to control and harness their, and the companies energy, toward clearly defined enterprise objectives one of which, but maybe not the only one, is the creation of monetary wealth .

There are two others we will look at in this article, but this simply is very complex pun intended and is going to become more complex, basically as government tries to protect you from your own greed, tensioned with your fear of faith.

Perhaps the most difficult problem for a small business, is how do you get your money out, if you need it for some reason?

This is probably the biggest obstacle to the success of an LLC, or limited liability company. The shares individually involve a significant chunk of more than spare change. Furthermore because of that chunky requirement, the total pool of investors is quite small. Hence you are pretty much into the program for the whole life of the company. Then there is the further problem of how you value that initial investment in terms of present value, preferably a positive present value. Can't you just feel the love evaporating?

Now a standard corporation does not have that high per share investment, hence you might be able to simply break up your investment into small lots, thereby being able to sell a portion of your investment to a variety of other investors. However, as we pointed out last week, you are not a sophisiticated investor in the first place, and chances of Sarah and Joe finding enough of those people to make the enterprise work, is really not that great, especially in this market. In the true perspective, if Sarah and Joe had access to all that wealth, they really would not need the money you truly may some day need.

Now the question you forgot to ask last week might provide the solution to all of this. The question is how did Sarah and Joe qualify to be sophisticated investors in their own company? They have no more money to invest than you do, and just like you, the only time they have seen Bill Gates is on TV, or seen his picture in a magazine or newspaper.

Sarah and Joe are officers in the company, and also serve on the board of directors. The board of directors being the qualifying criteria that allows them to not only invest, but also to run the show. They own founders shares, some of which they paid for with money, but most they did not pay for directly in cash, but in time, effort, and most profoundly the risk associated with getting the enterprise to this point. The point being, with all the investment capital they will need at this level of investment, they remain the majority stockholders period. Furthermore, they might allow you to obtain some of those time, effort, or risk shares also.

Members of the board of directors are supposed to have access to the inside information on the workings of the enterprise. However, this can become a do nothing club, where everyone scratches each other's backside, thereby grossly and negligently abandoning all fiduciary responsibilities. So why not make all investors, board members to keep everyone on their best game all the time?

The board of directors of closely held corporations can invest in these closely held corporations regardless of the amount of money they originally invested or their actual outside net worth. That means also that you can buy and sell, to and from one another. The true question only remains, how large is the board of directors?

The only time I have heard this idea utilized came from my securities lawyer in my gold mining days. He stated that there was an entrepreneur in Portland, that needed to raise; let's say a million dollars to start and run his company. He sold shares for 5000 per share, but every share had the accompanied right to be a member of the board of directors. From what I can remember he had about 75 members on his board and had funded the whole company by that means.

The company had basically a well paid professional management team also board members , but if there was really anything that a board of directors needed to do, instead of booking a conference room they, rented a meeting room that would hold the whole board meeting at one time.

This was essentially before the age of the Internet. With email, all you would really need to have a board meeting is the requirement for an email account. If need be, it would be easy to put together a webcast, or even a podcast, to convey the required information to each board member in a timely basis. Once a year you hold a big company picnic and annual meeting where everyone comes together and gets to know one another.

Investors can choose to actively participate in the running of the company or not, but they all have a much better idea on what is going on in the enterprise. While there is not a public market for stock immediately, it is reasonable that you can cash out your investment or buy new stock as opportunities change among all the board members.

It would seem that operating in this way a corporation board could manage a total board of 250 members or more, which would required an average investment of 4000 to raise the 2 million we discussed for Sarah and Joe's company last week. However, the required investment and number of board members should be determined in the process of preparing the original business plan, right along with marketing, finance, and other opportunities, and risks of the enterprise.

These thoughts of course may not be legal in your locality, so consultation with a good securities lawyer would be advised if you would consider such an opportunity.

Washington State is probably one of the most regulatory obtuse states in the union. That means if you ask for guidance before hand, you will simply be told, "You can't do that." Pressing further, the reason is, that reason is, because the regulator didn't think of it first, and if carried forward, it might someday, and someway, cause them some potential headache, before they retire. So it all depends upon your definition of is, is, and where you put the commas. In other words it may be easier and cheaper to ask for forgiveness than permission in the first place.

It probably would be advisable to have some sort of investment community fee to join; therefore members are only trading shares with other members. For example, Wonder Springs could sell virtual lots in the community and allow a community member to own stock, as well as set up a method where stock could be used to purchase goods and services etc. It really relates to whether, the company is really organized just along monetary lines, or has some specified community benefits it seeks to enrich also.

The real way to secure investment in small business is to make all stock issued in these initial offerings free from ever having to pay capital gains as long as they are held by the original investor, their heirs, and that initial investor capitalization pool. Once that stock is sold it becomes just common stock in any subsequent issue.

Hence, there should be some sort of total investment cap for this capital gains exclusion.

Before this financial bailout, the impossible to raise equity money seemed to range from about 200,000 to 2 million. My guess is in this new investment and credit desert that range may need to be extended from 100,000 to 5 million, but that number, should be set my market conditions. This opportunity for savings from capital gains taxes will probably come with some strict governmental oversight.

Perhaps a better way would be to not mess with the government and provide an appropriate capital gains account from founders stock, which accompanies these original monetary investment of say a 20 premium. That way up to a 20 capital gain is incorporated into these initial investments.

There is going to be an increasing emphasis especially in the near future to regulate all levels of business investments. Most of that will focus upon trying to fix a broken economic model that was grossly simplistic and highly focused toward bigness is always superior to anything else.

Some Native Americans have a term for the white man as having a worldview of "arrogance squared." This arrogance of what truly should be discerned as Natural Law, has cost Wall Street and Wall Street investors approximately one third of the wealth it theoretically once controlled. Before it is all over, in this easy money and inflationary fear driven environment, that number will more than likely go down to half that high mark some months ago.

Humpty Dumpty has fallen, he can't be put together again, but human capacity, which understands its true role as a gift from God, can and will make a difference again. Continuing to ignore the consequences of recreating ourselves in our own image of God, is foolishness define in Absolute Truth. A lesson this world now is in the process of learning in daily application.