PERMANENT
EQUITY

# Rule #1: Do No Harm

*TL;DR: Keeping "Do No Harm" Rule #1 is difficult, aspirational…and essential.*
*For us, not doing harm to a business stems from a core principle of humility. This focus allows us to:*

1. *Build relationships and trust*
2. *Ask questions and understand processes*
3. *Follow problems to the root*
4. *Determine where we can add value and unlock capacity*
5. *Augment and enhance what's already working*
6. *Create long-term outcomes in which everyone wins*

## What's the Harm?

At Permanent Equity, "Do No Harm" is a primary cornerstone of our approach, defined within the context of our values and priorities. "Do No Harm" sounds simple. But what counts as harm?

The ethics of defining harm have always been challenging. Even Hippocrates, commonly credited with penning primum, non nocere (first, do no harm) didn't actually include it in the Hippocratic Oath. If a doctor were actually going to do no harm, active surgical intervention would never happen, and the ongoing harm of a tumor would be allowed to fester and spread.

In any type of decision-making, from healthcare to investing, the possibility for harm is everywhere, and Do No Harm is not a neutral statement.

By approaching our partnerships with humility and curiosity, by prioritizing outcomes in which everyone wins, by building trust in our relationships with operations teams, and by understanding the value we can provide, we've figured out what harm means to us. And we work like hell not to do it.

## Stay Humble

Our commitment to Do No Harm stems from a foundational principle: humility. (It's also facilitated by our extremely long time horizon, but more on that later.)

Focusing on humility as an aspirational posture to guide our actions gives us a way to set priorities. In looking toward humility, we're not concerned with looking important, being the cleverest or fastest, or seeking solutions that are the most personally enriching or lucrative to the exclusion of all else.

Instead, humility requires that we take the time to understand the intricacies of a particular company, build relationships with current leadership and employees, ask questions motivated by curiosity and enthusiasm while genuinely listening to the answers, and actively seek out open and honest feedback.

When we enter into a partnership, we do not come to the table thinking that we know more than the leadership team does about their industry, customers, suppliers, production, or service. What's more, we're not trying to be better than they are at those things. If we start getting too big for our britches in areas that aren't our expertise, that's harm. Full stop.

## Remember Chesterton's Fence

In G.K. Chesterton's 1929 book The Thing (bear with us), two reformers come across a fence in the middle of a field. The first leaps into action, proclaiming "I don't see the use of this; let us clear it away." The second quickly replies "If you don't see the use of it, I certainly won't let you clear it away. Go away and think. Then, when you can come back and tell me that you do see the use of it, I may allow you to destroy it."

We like to think we're the second kind of reformer, even if we tend to think in terms of strategic changes to small business operations instead of fences and fields (although if you've got a fencing company you're interested in selling, by all means get in touch).

Every process, procedure, and position a small business has was initially created (and probably with some pain and suffering); it had a purpose, even if that purpose isn't clear to someone new coming in the door. Just as Chesterson's fence wasn't beamed down by aliens, a small business's invoicing system wasn't cooked up in a fever dream.

One of the basic tenets of Do No Harm is that everything in a small business was put in place because somebody thought it would be good for something. If we can't figure out what that something is, we've likely missed some other thing and misplaced our humility. And if we start making changes from a place where we've decided things are meaningless and mysterious, chances are that harm will follow–whether that be alienating existing leadership or employees, gumming up processes we thought could run smoother, shifting customer profiles to a market that doesn't exist, deleting some operationally critical Excel sheet that looked like it was outdated lunch orders, or some other harm we can't even think of because potential harms are innumerable–and specific to company and context.

Whatever the "fence," we prioritize studying it and talking to the people who built it. Only once we know fully why it's there, what it's supposed to do, and whether it is or isn't doing that, then we collectively can decide whether to keep it, replace it, repair it, double down on it, or practice our hurdle sprints over it.

## Let Great Be Great

When thinking about what counts as harm, it's easy to get caught up in the negative outcomes and become hyper-focused on how to avoid them. With that too, is the potential to fixate on opportunities lost.

There's another side to the Do No Harm imperative, though, that actually opens up new opportunities, at least when practiced with humility and patience. What's missed if we keep our understanding of harm limited to malfeasance and disaster? The opportunity to let great be great.

Part of our investment approach is that we don't partner with businesses because they're broken; quite the opposite. We partner with a given business because of its capabilities and successful track record. Any value built in partnership is meant to augment current success and supercharge the management team's expertise.

These twin posts of Chesterton's fence and let great be great solidify the idea of humility as the backbone of Do No Harm: We know enough to get out of our own way, and also not to get in the way of profitable excellence.

## Get to the Root

If Do No Harm is going to be practiced meaningfully, it needs time. We operate on an extremely long time horizon (~30 years). That not only means that we have more breathing room to establish trust and understand the company before considering any changes, it also lets us see what's going right–what built the business and stabilized its success.

We typically get to know our companies for 18 months to two years before making meaningful changes–and we're almost never the ones to initiate those changes. The operating team at a given company has the first-hand knowledge and deep insight into the inner workings of a company. If there's a problem or an opportunity that would benefit from change, it bubbles up naturally, as would hopefully occur with or without our involvement.

Time also affords us the opportunity to trace challenges and problems to their roots, rather than attacking the most visible, surface level issues. Even if it's not always harmful, per se, this type of quick action is, at best, pulling off the dandelion's head.

Finally, that extended time horizon aligns incentives; because we're in it for the long haul with our portfolio companies, their harm is our harm.

## Set theTable Right

Cultivating a Do No Harm ethos is hard, particularly in the context of investing. There are any number of incentives driven by an "only so much pie" mindset. It sets the table poorly and incentivizes bad actions.

Do No Harm is sometimes misinterpreted as not being involved, rarely-if-ever intervening, or being unwilling to take action or change leadership. In a context that seems dedicated to the questionable wisdom of "move fast and break things," non nocere seems pretty antiquated (not least because of the Latin). Some might even take this as an indication that we're only enforcing the status quo or even paralyzed into inaction. But it's worth noting that the full phrase, straight from Hippocrates' pen, is really **Primum** non nocere: **First** do no harm.

We've always been committed to this idea of "first" as critical, because it reminds us that there will inevitably be a second, a third, a thirty-fourth–but each subsequent step taken with and alongside a portfolio company will be better, more informed, and more effective if we build patience into that "first." It also means we aren't playing from behind, remedying whatever harm we did in the need to seem busy and important.

While we don't get involved in businesses that are structurally broken, sometimes we find elements that are. Just as a doctor reacts to an injury with immediate intervention and care, so must we respond. Operating by this idea of Do No Harm as Rule #1 requires decision-making rooted in clearly understood and deeply felt priorities and values.

To our minds, there wouldn't be much point in investing in a business that's running along at a good clip with no need for improvement (there's always a reason small businesses remain small). But coming into a good, sturdy, durable business and shaking things up because of some sense that that's what private equity does…well, it's easy to see how a boatload of harm could be done in no time.

Even if we're doing things we think should be done–issues that come up in due diligence, situations that look like something we've seen before at another business–it's always worth taking a step back and remembering that we don't know this business yet. So, first, we build trust and company-specific knowledge.

## Start with No Harm, End with No Harm

Let's also be clear that harm to a company can start well before investment boots hit the ground and reverberate after exit. In many cases, harm–or at least the potential for harm–is baked into the system from the get-go.

Do No Harm, scaffolded by our commitment to humility, extends to the price we pay, our aversion to transactional debt, our default to asking questions, and our unwillingness to let non-business-related events like a change in ownership drive changes in the business.

A business operates with certain economic pressures (e.g., payroll) consistently over time. When an equity transaction happens, depending on the way that transaction is structured, the magnitude and source of those pressures can shift enormously, very quickly. For example, traditional private equity's model frequently hinges on debt and complicated fee structures. In this case, it's possible for a business to go from having total autonomy over its cash flows to having 60% or more of cash flows earmarked for debt payments.

Whether such a structure inflicts direct financial harm is specific to that business, but it changes the very rules of the game. That business must now shift their decision-making to prioritizing repaying debts first. Debt is not a productive operating priority. This change to the operating core, prompted by an investment system based in debt, has the potential to do significant harm.

In practicing the principle of let great be great, we go back to Rule #1 and typically employ no debt. We have no transaction fees or other "gotchas." In principle, we aim to design deals that do not put financial and operating priorities at odds–and therefore enable operators to focus on operating to build durable value.

The leveraged buyout incentive system also ramps up the potential for harm post-close. When the primary objective is to provide investors a return in three to five years, decision-making is made in that context. Dramatic increases in EBITDA are inevitably the aim because that's the most straightforward path to a higher valuation exit. But if you're moving fast enough, you can keep adding to a leaky bucket and have it feel full. But someone at some point will be left with a mess.

It's hard to square these foundational choices with a principle of Do No Harm; when we say "Do No Harm," we're not just talking about not making major changes before we've forged relationships and gotten a genuine read on the landscape–it means, from the very beginning, we aim to make rational investments that acknowledge embedded risks in reality–without introducing new forms of harm.

## Be a Work in Progress

Harm is complicated, and sometimes not doing it requires looking like you're not doing anything. That can be an uncomfortable place to be, especially when it feels like you have something to prove, or when you're facing uncertainty, or when it looks like things are going south.

Every rule has an exception, and for us the exception to the Do No Harm principle is when there is already obvious harm being done to the business or the employees. We will intervene to protect, even if it means temporarily harming the profitability of the firm or the company.

We are also, inevitably, making decisions, with imperfect knowledge and between imperfect people. Our firm, our portfolio companies, our operating teams are all doing the best we can to plan and prepare to insulate against obstacles in a world full of educated guesses and calculated risk. We strive to define success in which everyone–from Permanent Equity to the brand to the operations team to the customer–wins.

What we have going for us in pursuing a philosophy of Do No Harm is that it helps us build shared trust (we're not out to strip your company for parts) and align ambition (continuous improvement and sturdy growth). Trust allows for transparency and authenticity. It affords us the privilege to be wrong and admit it and strive for better.

Ultimately, Do No Harm is aspirational–for better knowledge, stronger relationships, more trust, sounder actions, and more value.