



JACKSON LEADERSHIP
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WALL STREET WEEK WITH FORTUNE



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GEOFF COLVIN: He's accused of looting Tyco when he was CEO; now the trial of Dennis Kozlowski is underway. Frank Quattrone, once the star investment banker of the tech stock bubble, is now spending his days in a courtroom. And plaintiffs demanded more documents from Ken Lay, Enron's former chief, this week. Suddenly these former high-fliers are deep in the justice system, and our next guest says the details of how they went wrong can help protect us from making bad investments.

Whenever a company or career turns up dead, Sydney Finkelstein performs the autopsy, and his fascinating findings are the largest research project ever devoted to leadership failure. He's a professor at the Tuck School of Business at Dartmouth.

Professor Finkelstein, Ken Lay of Enron, Bernie Ebbers of WorldCom, Dennis Kozlowski of Tyco, all very smart guys. They worked very hard. They really wanted to succeed, and of course three of the most spectacular CEO failures in history. Besides all that, what did they have in common?

SYDNEY FINKELSTEIN: Well, they were tremendously talented, and that's very much one of the themes that I found all the way through in the research that I did: tremendous track records. In fact, you don't get to run a billion-dollar company unless a lot of people selected you in front of a lot of other people.

What they really had in common in addition to that type of track record was falling into a series of traps, you can call them, or habits of behavior that really turned them in the wrong direction.

COLVIN: Well, in your book based on this research, which is called *Why Smart Executives Fail* you identify what you call the Seven Habits of Spectacularly Unsuccessful People. Now, what's interesting to me is that a lot of them sound like good things. For example, they identify so completely with the company that there is no clear boundary between their personal interests and corporate interests. Well, a lot of governance experts will say the problem comes when the CEO's interests are allowed to diverge from the corporate interests. So, say he can pay himself a huge bonus while the shareholders get poorer.

FINKELSTEIN: I think that's a perfect example of how in small doses a lot of these themes, a lot of these behaviors are really, they're really sensible. The problem comes up when they go out of control. And that's true, you mentioned Dennis Kozlowski. One of the habits that I talk about is the company is mine, the belief that you, that you own the company, the belief that the company is almost an appendage to yourself as opposed to you being an employee, an executive, or even the CEO of the company. And when that happens, it's really a slippery slope down to getting closer to some allegedly illegal activities.

COLVIN: Well, that was certainly the case in his case and many others. Since it's my place, in effect, anything I do is by definition okay.

FINKELSTEIN: I think that's ImClone, I think that's Martha Stewart, I think that's definitely Adelphia. There are a lot of companies that fall into that boat.

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CEO WARNING SIGNS

UNNECESSARY COMPLEXITY
SPEEDING OUT OF CONTROL
THE DISTRACTED CEO
EXCESSIVE HYPE
A QUESTION OF CHARACTER

COLVIN: Another one of the habits of unsuccessful people, they seem to have all the answers, often dazzling people with the speed and decisiveness with which they can deal with challenging matters. But we praise people, we train them, we reward leaders for being fast and decisive. So what's the danger?

FINKELSTEIN: The danger is when you come up and say, "I've got all the answers." Number one, you shut out other people. You make it difficult to get the team that's around you to be able to contribute. And number two, who is it to say that you really do have all the answers? In fact, many of the executives that I interviewed and that I talk about in the book had answers, but they weren't the right answers at all. But there was no one there who was able to challenge and question them, because they have this mindset that said they have to have all the answers.

COLVIN: And so their attitude intimidates everybody else.

FINKELSTEIN: Absolutely.

COLVIN: Well, it's one thing to explain what went wrong after the fact. What we all really want is some way to forecast or foresee failures before they happen. And you have come up with exactly that, a list of warning signs. Unnecessary complexity is the first one, meaning what? Unnecessarily complex answers to simple questions?

FINKELSTEIN: Sometimes it's unnecessary to complex strategies, like Webvan when they created dozens of warehouses around the country to sell online groceries, and it cost them over a \$1 billion, when we all know you can hire a kid after school to deliver groceries at a slightly lower price point than that.

COLVIN: Speeding out of control. What's that all about?

FINKELSTEIN: That's a warning sign that says you're moving so quickly that you're not able to really manage what's going on. You're getting ahead of yourself. A lot of startups of course fall into that trap.

COLVIN: Yeah, they did. The distracted CEO.

FINKELSTEIN: The CEO is more interested in seeing himself on television, who is interested in having stadiums named after him or her. That's someone who is distracted.

COLVIN: So when the CEO becomes a celebrity, that may in itself be a sign of trouble.

FINKELSTEIN: I think that's right.

COLVIN: Excessive hype.

FINKELSTEIN: You see excessive hype both about products and about actual companies. And I think there were several companies that I looked at where the hype was just going on and on and on. Whether it's Mattel with the Barbie brand, which became the core of the whole company, even though they ended up making a series of acquisitions that weren't quite so successful, or it's a startup company like a General Magic, which is the old Apple spin off where they hyped the product.

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COLVIN: Right. Finally, a question of character.

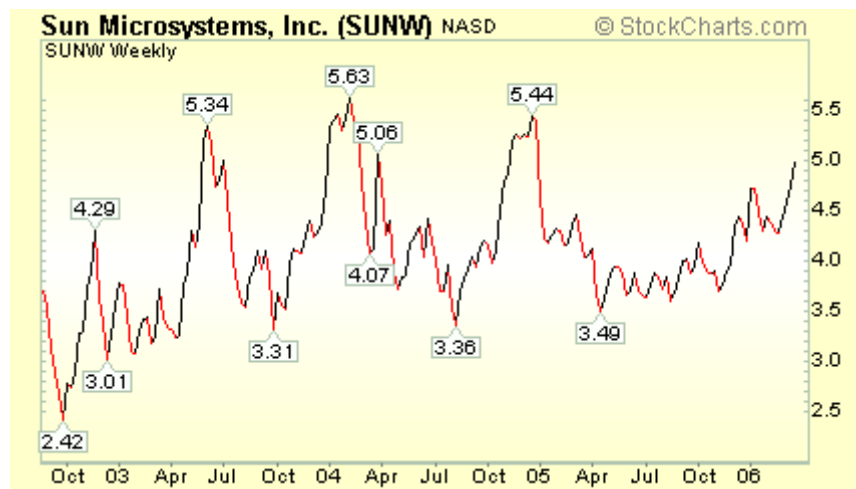
FINKELSTEIN: In the final analysis, I think that's the most important thing, and it's the hardest to get your hands around of course. I try to develop some ways in which the average investor, or employee of a company for that matter, can try to get a sense of what to do, and there are a few things that we can talk about along those lines.

COLVIN: So how can employees or shareholders figure out if there are character problems in a particular CEO or in a company?

FINKELSTEIN: The first place to look is the annual report and the letter to shareholders that the CEO writes. It is one of the most vetted of all documents that any company has. There are lawyers that go through it, other top managers. And if there are still some warning signs that you see there, where maybe the CEO is talking about "I" rather than "we" a little too much, talking about, or rather not acknowledging, any of the mistakes that the whole world knows happened, those are things to look out for.

I think another one is to spend some time listening to conference calls with research analysts. They're now always available on the Internet, often in real time. And listen carefully to how the CEO, and for that matter the CFO, respond to questions that probably they didn't expect or maybe didn't want. How open are they? What type of reaction are they giving you? And you can learn a lot I think from kind of having that type of insight.

COLVIN: Let me ask you, with that as background, about a couple of companies that have been in trouble lately. Sun Microsystems, very high profile CEO, Scott McNealy. Merrill Lynch analyst Steve Milunovich said just this week, "the company has gone from being pure in vision and predictable in financial performance to an underachieving, bloated, unfocused reflection of its former self." In light of your research, how's it look?



FINKELSTEIN: I'll tell you something about Sun. There's a pattern that emerged over a year ago, which was -- and it's a classic warning sign -- of significant turnover of senior executives. And they were all in the same type of time period of two, three, four months apart, and every single one of them by themselves, they sound reasonable, whether there's other opportunities or some other reasons. But when you start to see that pattern begin to snowball, and now, I mean if you go up and down the ranks of Sun, you'd find that probably two dozen senior executives have left, and why is that?

COLVIN: Gateway, another high profile company with a high profile CEO, Ted Waitt. That was at \$80 a share a couple of years ago. Now it's \$6 a share. How's it look to you?

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FINKELSTEIN: I think Gateway is a story of what I call desperation management. It's a company that keeps on changing their strategy, has no clear sense of how to win. For example, Ted Waitt was the founder of the company, steps to the side. He's back in. He changes his whole top management team. They decide that they can't beat Dell at PCs, so let's go and try to beat Samsung and Sony with plasma TVs. That constant change is really not the right thing to do, always looking for something to hang your hat on.

COLVIN: Well, if you look at the opposite of all these traits we're talking about, presumably you'd come up with a list of pretty good bets for the future. So with that in mind, who do you like?

FINKELSTEIN: Well, I think there are a few companies that I've seen where if you see the strategy, in particular what the leaders are doing, they're doing the opposite to what I describe in the book. Accenture, the consulting firm, is a good example. Joe Forehand is the CEO, and he had the incredibly challenging job of following George Shaheen, who as you may recall, left to go to Webvan.

COLVIN: To Webvan, right.

FINKELSTEIN: Kind of created a circle for us. And what he had to do is, number one, go through the IPO process. Number two, rebrand Accenture, which was the old Andersen Consulting. And we know the partner of Andersen Consulting was Arthur Andersen.

COLVIN: Arthur Andersen.

FINKELSTEIN: And he managed to go through all of those different stages and pretty challenging situations, expand the level of responsibility for people throughout the organization, and try to create a more open-minded organization.

COLVIN: One more.

FINKELSTEIN: I think I would take the New York Times Company as another example, and they're a particularly interesting one because of the Jayson Blair scandal and how they got so much bad press around that. In fact, if you go look at their corporate management, in particular the CEO, Russell Lewis, he in my mind is a standout for someone who is creating a very open-minded organization, a place where they are challenging and asking the tough questions. And the Jayson Blair story is a good one, because it was Russell Lewis and his top management team that were willing to take the rather challenging step of having the two top editors in the news division resign in response to the Jayson Blair scandal. And I think that was a tough call to make and the right call to make.

COLVIN: Sydney Finkelstein, this is a really fascinating perspective on things. Thanks for your views.

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