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[Public confidence in big business: 22%]

HARD-WIRED MANAGEMENT MORALITY: COALITIONAL CRIME AT ENRON, WORLD COM, TYCO, HEALTHSOUTH

Setting the Scene. The sheer audacity and scale of the corporate corruption uncovered at century's end left the general public—as well as the business community itself—overwhelmed and shocked. Large numbers of executives and companies at the very pinnacle of American (and foreign) enterprise were charged with crimes and civil misdeeds. Public distrust of business plunged to new lows. New laws sought to curb these excesses. Many voices of protest were heard, many explanations offered. This chapter offers yet another, drawing upon network theory, complexity science, neuroscience, and evolutionary psychology.

Corporate corruption is typically a group activity. Beyond secrecy, it requires the cooperation and active collaboration of an initiator and confederates. The lone embezzler who siphons off illicit gains and the entrepreneurial investment advisor who hoodwinks trusting clients, though numerous, are exceptions to the rule. Corporate misdeeds of the kind discussed here tend to be carried out by corrupt alliances.

This view is at odds with various popular explanations of the great flood of corruption that washed over the U. S. corporate landscape at the turn of the century. Flawed personal character, lax corporate governance systems, executive pay tied to stock options, understaffed regulatory agencies, cozy ties between companies and their auditors, collusion between stock analysts and the companies whose stock they analyze and report on, a market-induced profits-before-people attitude, the “irrational exuberance” of stock market investors, an unprincipled focus on greed and personal gain—all have been advanced as key flaws that need to be “fixed” if

business is to recapture the confidence and trust of investors and the general public. While there is something to be said for each, taken together they are little more than folk explanations, lacking a theoretical base grounded in empirically derived data.

This chapter takes a different tack, arguing that corporate corruption is a function of (1) managerial hierarchy, (2) environmental opportunity, (3) dominant values of corporate culture, and (4) executive minds hard-wired for the pursuit of power. The presence of these four conceptual components is demonstrated by interpretive data derived from published sources. The goal is to describe networks of intrigue and corruption that emerged in four of the most prominent corporations involved in the corporate scandals of the late 1990s and the early 2000s: Enron, WorldCom, Tyco, and Health-South.

What the Companies Did

Fraudulent, corrupt actions varied from company to company, but a common pattern can be discerned. These might conveniently be called generic types of corporate wrongdoing that appeared in each of the four companies.

- Lax, compliant oversight by the board of directors, including audit and compensation committees
- Flexible interpretation and use of generally accepted accounting principles
- Issuing reports falsifying the company's financial condition by understating costs and inflating revenues, income, and profits
- Executives receiving and paying unauthorized bonuses and other non-job-related personal benefits from company funds
- Collusion with audit firms to conceal the company's financial condition from, and thereby to mislead, investors, creditors, government regulators, stock exchange commissions, and tax authorities
- Collusive cooperation with stock analysts, brokerage firms, and investment banks to boost the reputed value of the company's stock

These generic forms of fraud and corruption were then multiplied and varied from company to company:

- Manipulation and restriction of energy supplies to boost prices and company profits at **Enron**

- Off-book transfer of assets, costs, and revenues through special purpose entities, for personal profit of insider executives at **Enron**
- Salaries and bonuses unjustified by economic performance at **Enron Broadband Services** and at **Tyco**
- Over-claiming on Medicare payments at **HealthSouth**
- Conflict-of-interest contracts between the company, directors, and executives at **HealthSouth, Tyco, and WorldCom**
- Payments-in-kind (bonuses, housing loans forgiven, gifts of company cars, condos, private school tuitions) to cooperating managers and staff members at **Tyco**
- Use of family members and friends to funnel company funds for illegitimate purposes at **Enron** and **HealthSouth**.

The consequences of these modern forms of piracy were far ranging, victimizing literally millions of people and affecting some of the economy's major institutions. The plundering:

- Diminished stock values for individual shareholders, creditors, pension funds, brokerage houses, and other investment institutions
- Destroyed jobs, disrupted career paths, and wiped out retirement reserves of employees
- Reduced sales and revenues of dependent supplier companies
- Through market manipulation, created crisis, uncertainty, and exorbitant prices in energy markets, especially in California, thus greatly burdening state budgets with debt loads
- Exacerbated the debt problems of state governments through false reporting of income, use of off-shore and off-book accounting, and questionable classification of revenues, thereby reducing state tax collections
- Caused the bankruptcy of **Enron, WorldCom, and Tyco**, significant financial loss and continuing instability of **HealthSouth**, and dismemberment of the **Arthur Andersen** auditing firm
- Produced a range of new government regulations and stock exchange rules, thereby increasing the complexity and cost of business operations
- Resulted in a massive loss of public trust in corporations and great damage to the image and reputation of business in general.

The Central Propositions

Seven propositions support the central argument that corporate fraud and corruption are group activities initiated by high-ranking executives working collaboratively with company directors, other senior officers, mid-level managers, administrative staff, and various external confederates.

In the four companies reported here, corporate fraud and corruption are proposed as:

P1: *coalitional actions, not individual acts*

P2: *top-down in origin, not bottom-up*

P3: *hierarchically imposed and collaboratively induced, not independently volitional*

P4: *activated by self-aggrandizing executive impulse, not by pursuit of organizational function or purpose*

P5: *habitual, repetitive, and infectious, not a reversible one-time event*

P6: *extra-organizational, not confined within the company*

P7: *opportunistic and episodic, not ubiquitous, and triggered by environmental challenges and energized by aggressive, high-velocity, growth-oriented corporate culture.*

Sources Used

Most of the data reported here were derived from news stories and investigative reports published in the business press. The leading journalistic source was *The Wall Street Journal*; others were *The New York Times*, *Business Week*, wire service stories, and various on-line newspaper and magazine data banks.

No claim is made for completeness or comprehensiveness of the reported data, especially since investigations and legal ramifications can continue indefinitely. Press reports of unproved charges, legal indictments, court-approved plea agreements, guilty pleas, convictions, and prison sentences have been used to identify and describe the alleged initiators, collaborators, and corruption networks. Unless clearly stated otherwise by legal authority, all such reported charges and legal actions are treated as allegations only. In spite of these qualifications necessitated by fairness to the parties involved, the published data give a reasonably accurate impression of the organizational skeins tying corporate actors together into networks of intrigue, corruption, and personal enrichment.

The focus of this inquiry and report is on actions that can be construed as *unethical*, not whether an individual, group, or firm is found guilty or innocent of a crime or of fraudulent and corrupt behavior that is judged to

be *illegal*. Reported unethical actions tend to be far more numerous than prosecuted unlawful acts for the simple reason that the legal process allows, and often encourages, a winnowing down of charges by prosecutorial strategies as a way of securing convictions on those that can be proved in court. Negotiating plea agreements often, perhaps usually, reduces the number of legal grounds on which a final agreement will be based. An example is **Enron's** Chief Financial Officer (CFO) indicted on nearly 100 counts who was allowed to plead guilty to only 2 of the charges to induce his cooperation in naming others. Hung juries, retrials, and mid-trial changes of strategy by prosecutor or defendant can result in abandonment of one or more charges of illegal action. Therefore, news media reports of corporate activities that may eventually produce indictments, trials, convictions, and sentences tend to give fuller accounts of what can be construed as unethical or socially irresponsible behavior than the court record itself.

Webs of Intrigue

Figures 1–4 depict the organizational networks sustaining the corrupt and fraudulent activities at **Enron, WorldCom, Tyco, and HealthSouth**. These might usefully be called webs of intrigue and deceit. As the internal auditor who uncovered the fraudulent scheme at WorldCom said, “It was a spider web of transactions, and it was not easy to trace.” Corruption in each company was made possible and carried out by four kinds of participants. *Schemers/Drivers* are the originators and the primary source of organizational authority for corrupt actions—the spiders sitting at the web’s center, so to speak. In each figure, they are located in the circle. *Functional Enablers*, shown on the left, use their organizational function and authority to advance or reinforce the corrupt scheme. *Staff Cooperators* (on right) “go along” with the scheme, either willingly or reluctantly, by following orders from superiors. *External Confederates* (bottom), though not directly part of the company, provide indispensable aid that both sustains and extends the corrupt scheme’s influence well beyond the company’s borders.

Knowledge of the corrupt scheme is unevenly distributed throughout the web, so that any of the four—Schemers/Drivers, Functional Enablers, Staff Cooperators, and External Confederates—may or may not be aware of the full extent of the scheme. This would be especially true in any very large corporate structure where operations are far-flung, authority is divisionalized, or board oversight is technically difficult.

Figure 1

THE ENRON WEB

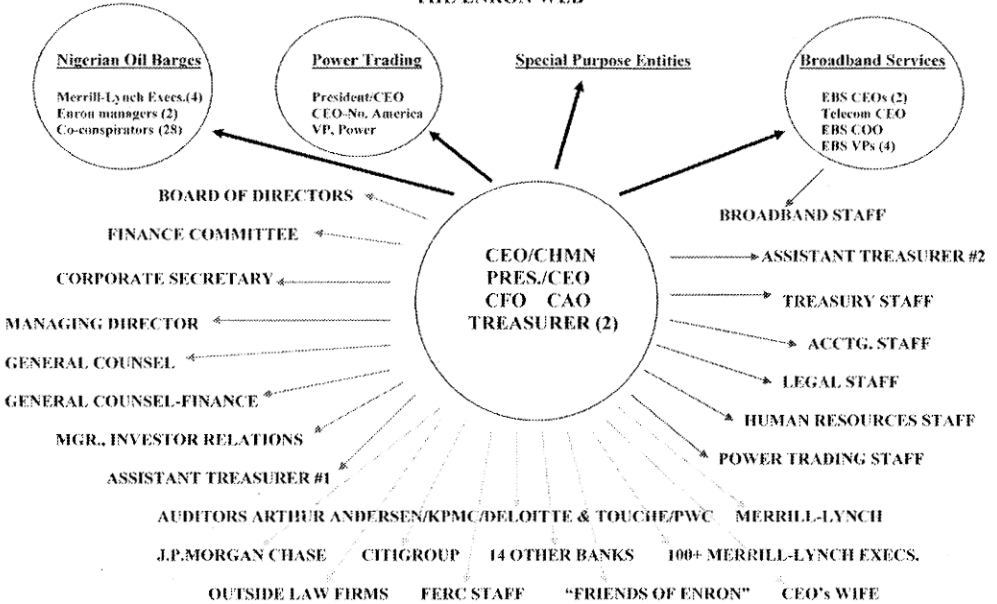


Figure 2

THE WORLDCOM WEB

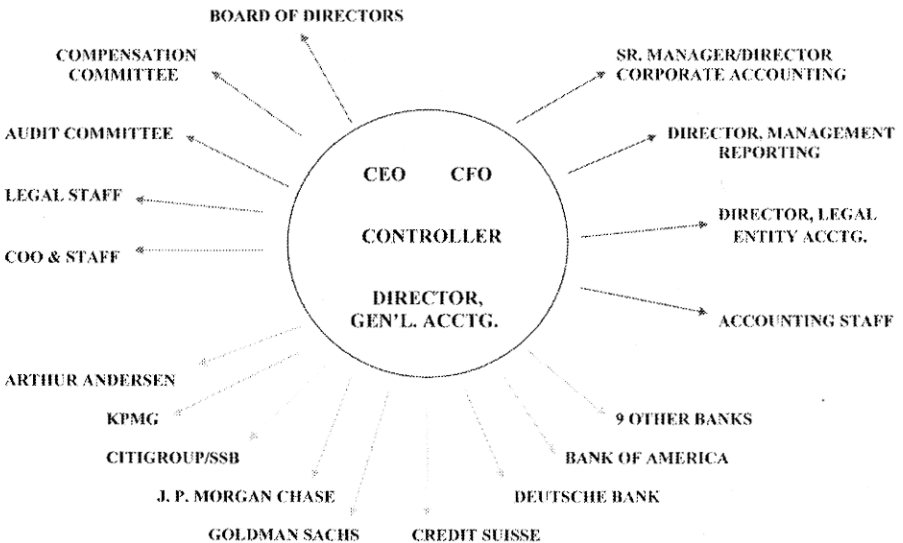


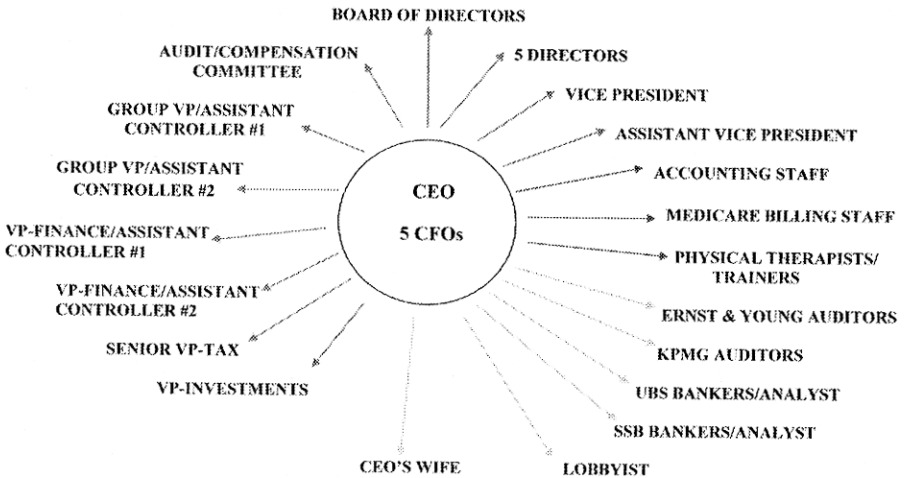
Figure 3

THE TYCO WEB



Figure 4

THE HEALTHSOUTH WEB



Support for the Propositions

Proposition 1: *Corporate fraud and corruption are coalitional actions, not individual acts.*

Enron. News reports identify more than 50 people by name said to be involved in corrupt, illegal activities of one kind or another, but this figure does not include a large number of others, including unnamed members of the board of directors; in-house lawyers; miscellaneous staff members in accounting, law, broadband services, treasury, and energy trading; several outside law firms; staff of the Federal Energy Regulatory Commission (FERC); 16+ banks; four auditing firms; close friends of Enron's CFO, as well as family members. Enron's president, as part of his legal defense strategy, asked permission of a federal judge to release the names of 114 co-conspirators, but even that count falls short of the total numbers involved.

Enron's networks of corruption were very extensive, requiring the collaboration and active involvement of many corporate functionaries at many different levels and in many different offices. Fraud was centered in four different areas of company operations: special purpose entities, broadband services, energy trading, and an operation in Nigeria. If one were to picture Enron corruption as a cancer centered in company headquarters, then these four "daughter cells" had metastasized to other locales and organs in Enron's far-flung corporate body.

WorldCom (now MCI). At WorldCom, 14 persons were named as active participants. Others included 12 directors, members of the board's compensation committee, 3 accounting managers, in-house lawyers, 7 miscellaneous executives and their spouses, miscellaneous staff in accounting and law, 15 banks, 2 brokerage firms, and 2 auditing firms. Bankruptcy court examiner Dick Thornburgh reported that at least 40 WorldCom employees knew about the fraud but were afraid to speak out. A former WorldCom CEO stated that the wrongdoing was confined to "fewer than 100" employees.

Tyco. The numbers at Tyco also reveal the presence of a coalitional network. Eighteen persons have been identified by name or position, while others include members of the board's compensation committee; board members identified as "cheerleaders" of the fraudulent operations; in-house lawyers; 51 employees who received unauthorized bonuses; lower-level managers who manipulated accounting rules; miscellaneous staff in accounting and regulatory law; 1 auditing firm; and 1 brokerage firm's vice president and stock analyst. The total number involved probably reached 70 or more.

HealthSouth. Thirty-three persons were identified by name. Others unnamed but involved were the board of directors; members of the board's audit-compensation committee; miscellaneous staff in accounting and Medicare billing; physical therapists and trainers; 2 auditing firms; 2 bankers; stock analysts at 2 brokerage firms; a director's wife; and the CEO's wife. An estimate of 50 or more employees is not unreasonable.

These reported coalition numbers for the four companies are undercounts of the actual numbers of network participants. In no case was the fraud carried out by a single individual or a duo of schemers. Like wolves, corporate crooks conspire and hunt in packs, not as loners.

Proposition 2: *Corporate fraud and corruption are top-down in origin, not bottom-up.*

A stereotypical view of crime depicts a kid putting his hand in the cookie jar while Mom isn't looking. That image doesn't compute in the corporate world, at least not in the companies discussed here. In all four companies, the very topmost executives—chief executive officer (CEO) and chief financial officer (CFO)—were the leaders, the initiators, the drivers, and the schemers. It was Mom, not Johnny, who sneaked the cookies while no one was looking.

At **Enron**, CEO and CFO were joined by several other high-ranking executives, including the CEO of North American operations, Energy CEO, and Telecommunications CEO (2 of the latter), the company's chief accounting officer (CAO), 5 vice presidents, and a chief operating officer (COO). Also implicated were members of the board of directors, especially the board's finance committee, general counsel, and general counsel-finance.

The story is essentially the same at **WorldCom** (CEO, CFO, COO, controller, director-general accounting, board members and board committees), **Tyco** (CEO, CFO, general counsel, compliant board of directors, and board compensation committee), and **HealthSouth** (CEO, 5 different CFOs, board members, board audit-compensation committee, and 8 vice presidents).

Clearly, people who occupied these exalted positions were the organizational elite. Corporate fraud is an elitist activity, originated at the pinnacles of power and authority. Thus the corporation's hierarchical organization that cedes dominant power and decision making to the highest ranking officers contributes to, and makes possible, the formation of elitist coalitions bent on personal enrichment through fraudulent and corrupt means.

Proposition 3: *Corporate fraud and corruption are hierarchically imposed and collaboratively induced, not independently volitional.*

To be successful, high-level corporate defrauders and corrupters must enlist others from within the company. These others—they might accurately be called “gang members”—are recruited for their usefulness in authorizing dubious actions, falsifying company records, devising ways around standard operating procedures (such as generally accepted accounting principles), colluding with auditors or deceiving them, jacking up market prices by artificially restricting supply (as **Enron’s** energy traders did), shredding incriminating documents or deleting e-mail files, submitting inflated financial reports, concealing true costs of operations, etc.

Not all gang members sign on willingly or even knowingly. They may be persuaded or ordered to write a financial report they know to be untrue. When a **WorldCom** employee questioned an accounting discrepancy, the company’s director of general accounting told him, “Show those numbers to the damn auditors and I’ll throw you out the f_____ window.” One J. P. Morgan Chase banker told a colleague who knew about **Enron’s** fraudulent trading contracts, “Shut up and delete this e-mail!!!!!!” **Tyco’s** manager of human relations eased the CEO’s questionable loans through or around official channels, while the head of regulatory accounting altered internal documents to conceal results from Arthur Andersen auditors. Three mid-level accountants knowingly counted reserves as current expenses for several consecutive quarters. A combination of physical therapists, trainers, and billing personnel at **HealthSouth** cooperated in making false claims to Medicare. One of the healthcare company’s vice presidents authorized the filing of false federal and state tax returns, while another overvalued company investments to make the company look good to investors. **Health-South’s** assistant controller and four subordinates made false accounting entries and “were afraid to report what was going on,” then later pleaded guilty, saying they believed they wouldn’t be implicated in the fraud because they weren’t actually signing the falsified documents!

The plight and ethical posture of these lesser gang members varies. Some were willing accomplices, amply rewarded for their cooperation by raises, promotions, bonuses, forgiveness of housing and relocation loans, vacation trips, golden parachutes, gifts of company stock and company SUVs, lavish lunches and parties, etc. Others were reluctant to go along but did so anyway, fearing job loss if they did not cooperate. Whether shill or knowing crook, both types were caught up within an organizational system that exerted a powerful influence on their economic well-being: their salary, benefits, health care, and retirement pensions. Many found it easy to “go

along if the boss wants it,” like good organizational soldiers everywhere. They were also subject to all the pressures one feels in a vibrant corporate culture, not wanting to rock the boat and having little incentive to do so.

Enron’s go-go culture was famous for its lavish excesses, employee parties, celebrations, and awards, in one case featuring a baby elephant as party guest. It would have been hard to resist going along with whatever the job called for, even though legally or professionally dubious. Although some employees clearly struggled with their consciences and in some cases openly opposed corrupt actions, most accepted what they believed to be the realities of life in a big organization and became willing accomplices.

Ethical culpability in general is associated with one’s level of organizational authority, starting with top-ranked *Schemers/Drivers*, followed by *Functional Enablers* who use their organizational authority to advance or reinforce the corrupt scheme, and then by lesser-ranked *Staff Cooperators* who, willingly or reluctantly, agree to follow orders.

Proposition 4: *Corporate fraud and corruption are activated by self-aggrandizing executive impulse, not by pursuit of organizational function or purpose.*

However exorbitant the executive salaries, however generous the bonuses, however lavish the company-paid personal expenses, however enriching the special-favor allocations of IPO stocks to favorites, however stratospheric their stock-option awards, however many conflict-of-interest deals with directors, however often false reports were filed with regulatory overseers—in all these instances, it was always claimed by the Schemers/Drivers that such actions benefited the company and helped discharge obligations to shareholders, creditors, employees, and other stakeholders. “I did it for the company” was the accused’s mantra, and later became a part of their legal defense, at **Enron, WorldCom, Tyco, and HealthSouth.**

CEOs at all four companies could point to a phenomenal expansion of corporate assets and markets during their tenure. Stock valuations climbed steadily, boosted by (and boosting) investor confidence. Acquisitions ballooned, creating larger and larger corporate empires with larger and larger revenues. Investment banks poured billions in credit into corporate treasuries. Brokerage analysts touted the companies’ stock as a sure-fire thing. Auditors’ reports reinforced the judgments of outsiders. Company employees were induced, and sometimes required, to put their retirement funds into company stock. Such all-round confidence from so many quarters certainly seemed to testify that top management was guiding each of the four

companies in the best possible way to achieve positive results for all market participants.

The fuller, and more accurate, story is now known. It was not organizational purpose and economic function that drove the key Schemers. Each CEO knew well before anyone else that his company's economic standing, and even its future, was threatened by decisions and actions that profited the Schemers/Drivers, Functional Enablers, and Staff Cooperators, not to say many External Confederates. **Enron, WorldCom, Tyco, and HealthSouth** suffered financially as a direct result of the unethical, corrupt, behind-the-scenes actions initiated by the top-level executives and carried out with the help of others both inside and outside each company.

WorldCom fraud totaled at least \$11 billion, the company lost \$60 billion in asset value and wound up bankrupt. Of **Enron's** three main fraudulent operations—broadband services, energy trading, and off-book special purpose entities—only energy trading brought money into the company but did so illegally by rigging market supplies and prices. Broadband services never made a penny, and the off-book, off-shore special purpose entities lined the CFO's pockets but not **Enron's**. At **HealthSouth**, the total fraud figure was over \$4 billion and, like the other three companies, its stock value plummeted. All four companies turned out to be financial disasters for shareholders, creditors, and employees. None could legitimately claim that their top executives' policies and decisions had produced results beneficial for the company's long-term economic strength.

By contrast, the record shows that executive self-aggrandizement was the central motive at work. Executive Schemers raided company treasuries at will, authorizing out-of-sight salaries for themselves, exorbitant (and in at least one case, extortionate) bonuses, travel allowances, stock options and outright gifts of stock, purchases of artwork, forgiveness of personal loans, gifts of housing and jewelry, multimillion dollar parties (including an infamous one on foreign soil to celebrate a CEO's wife's birthday), sweetheart deals for favored directors, and underwriting executive love affairs with favored staff members.

The chief Schemers' self-magnification quest went beyond mere economic enrichment to include social and political influence. **HealthSouth's** political lobbyist orchestrated political influence at local, state, and federal levels, including friendly relations with Senators Daschle, Harkin, and Hatch, House Speaker Hastert, and President Clinton. Through generous philanthropic gifts, executives at **Enron** and **Tyco** saw their names linked to university halls, sports stadiums, streets, and other public venues. Others were seen and admired as patrons of the arts. An apparent craving for fame fed an endless accelerating cycle of attention-getting activities. As one

post-bankruptcy report said, the CEO at **WorldCom** “was allowed nearly imperial reign over the affairs of the company.” Another source labeled **Tyco’s** CEO as “the captain of corporate piggery,” not a coveted title but a suggestive one.

All the evidence points towards a quest for self-aggrandizing executive glory, which subordinated and sabotaged what might otherwise have been policies intended to strengthen and expand their company’s core economic mission. This observation is consistent with evolutionary psychology’s contention that the modern executive brain reflects the ancestral conditions and challenges of Ice Age hunter-gatherers whose families, clans, and tribal groups were organized hierarchically by dominant alpha males who monopolized sexual access to females and the spoils of hunting. The impulse to acquire and wield power, and to enjoy all of the associated perquisites—financial, social, political, and sexual—appeared to be present in these companies. That the urge might be planted deep within a hard-wired executive brain may explain the persistence with which it appears and reappears in today’s corporate world.

Such behavior also supports a picture of corporate culture dominated by two core value sets—economizing and power-aggrandizement—that shape and drive company decisions. This view was developed in the preceding **Year 2000** chapter in Part III. and more fully in an earlier book, *Values, Nature, and Culture in the American Corporation*.

Proposition 5: *Corporate fraud and corruption are habitual, repetitive, and infectious, not a reversible one-time event.*

Once begun, corporate corruption seems to take on a life of its own, becoming virtually unstoppable. Normal checks and balances are corrupted: internal and external audits, board of directors authorization, arm’s-length relations between stock analysts and client companies, due diligence by creditors. Top-level Schemers find they must draw in larger numbers of Enablers and Cooperators: quarterly reports must be fudged, anticipated revenue is booked as current income, off-book entities become a dump for burying excessive costs or boosting company revenues, tax and government regulatory reports must be fine tuned to conceal lax compliance, compensation and audit committees are induced to bend the rules or look the other way. Gang membership swells as recruits are drawn from all organizational levels. Secretaries, supervisory staff, accounting underlings, financial analysts, professional staff, public relations managers, health care specialists, and legal staff become knowing partners, or in some cases unwitting ones, in the crimes initiated by their superiors.

Accounting fraud began at **HealthSouth** in the mid-1990s and continued quarterly for nearly a decade. **Tyco's** misdeeds may date as far back as the 1980s, while **WorldCom's** accounting irregularities began in 1997 and its CEO-CFO collusion around 2000. **Enron's** several layers of corruption were laid down mainly during the 1990s. In general, the most active fraud paralleled each company's drive for growth, expansion, and market dominance. As stock valuations climbed higher and higher, so likewise did executive rewards, putting a premium on keeping the curve on an upward slope. Fortunes were being made. The slightest hints of trouble—a slippage of quarterly revenue, a negative earnings report, the loss of an important market segment, failure to get regulatory approval of a new product, government cutback of health care allocations, a Wall Street analyst's skeptical assessment—could bring it all crashing down.

The corruption juggernaut bulled ahead, gathering speed and compounding fraud as it went. Nothing was allowed to block its path—not organizational rules, professional standards, laws, company traditions, uncooperative employees, auditor oversight, government regulations, stock exchange guidelines—nothing! Rules were bent, standards disregarded, laws flouted, traditions disregarded, uncooperative employees fired, auditors deceived or co-opted, regulatory agencies lied to, securities exchange guidelines manipulated. What had been epidemic in the executive suite soon was endemic to the entire culture. The cancer, the virus, the infection invaded all levels, broke down governance immune systems, leapt over corporate walls, infected auditors, bankers, brokers, regulators, friends, and family members. A virtual plague had descended on corporate America. It would not be easy to shake off.

Proposition 6: *Corporate fraud and corruption are extra-organizational, not confined within the company.*

An integral part of corruption strategy is the recruitment of External Confederates. Although varying somewhat from company to company, the usual candidates for gang membership are auditors, investment bankers, brokerage houses and their analysts, outside law firms, cooperative government regulators, and close friends and family members of the chief Schemers. Typically, **Enron** led the way among the four companies discussed here, having successfully recruited Arthur Andersen auditors, several of its partners, and one of its in-house lawyers; 3 other auditing firms; Merrill Lynch as a firm entity plus several senior-level individual officers, and staff lawyers; J. P. Morgan Chase and Citigroup as firms plus senior officers; 14 additional investment banks; several outside law firms; com-

pliant Federal Energy Regulatory Commission regulatory staff; and the CFO's friends and family members, including his wife who also was assistant treasurer. **WorldCom's** reach was somewhat less by comparison, involving only two auditing firms, 3 investment banks, and a brokerage house and its star analyst. **Tyco's** crookedness received support from its auditor, PriceWaterhouseCoopers, and the Merrill Lynch brokerage firm. The Schemers and Drivers at **HealthSouth** found help from two auditing firms, two investment banks and their analysts, the CEO's wife, various friends, and a political lobbyist.

The External Confederates' support of crookery took various forms. Auditors signed off on procedures that violated generally accepted accounting principles, thereby misleading investors and creditors. Arthur Andersen's auditing and support staff, on the advice of a home-office lawyer, initiated the destruction of potentially incriminating documents at **Enron**. Brokerage and banking analysts, by issuing over-the-top unjustified estimates of company stock valuations (sometimes encouraged by that company's top Schemers), curried favor as a way of promoting their bank's business with the corrupt firm. Some senior banking officers led the cheering for a company's stock while urging their own staffs to "clean up their e-mail files" to avoid possible government prosecution. Government watchdog agencies permitted regulatory rules to be bent. Outside law firms advised in-house counsel regarding legally dubious actions, and one law firm issued a premature and incomplete internal investigative report clearing one of the companies and its executives who had engaged in illegal activities. Close family friends of corrupt corporate executives, along with the spouses of favored officials, served as channels for funneling illicit corporate funds out of the company and into the wrong hands.

The active cooperation of all types of External Confederates makes it abundantly clear that the web of deceit and corruption centered in the host corporation spread well beyond each company's own home-grown Mafia-like mob.

Proposition 7: *Corporate fraud and corruption are opportunistic and episodic, not ubiquitous, are triggered by environmental challenges, and are energized by aggressive, high-velocity, growth-oriented corporate culture.*

The pervasiveness and persistence, not to say the organizational depth and external reach, of fraud and corruption seen in these four companies raises a question of overriding significance for the modern business corporation: Are such acts ubiquitous, representing a continuum of behavior to be expected of all corporations and their top-level executives? Could it be that

fraud and corruption are somehow inherent to corporate operations? An affirmative answer would surely shake the very foundations of business life as we know it.

The evidence reported here supports a less dramatic conclusion but one that gives pause nevertheless. All four companies were riding a big wave of expansion and growth in their respective markets. **Enron** had set its sights on becoming, not just the “world’s largest energy company” but the “world’s greatest company.” It also swaggered into the rapidly growing telecommunications market by proposing a vast fiber optics network to compete with cable service. Its energy-trading and market-making skills in a range of commodities became its greatest claim to fame on Wall Street, boosting its stock to ever higher levels. Also during the 1990s **Tyco’s** CEO Denis Kozlowski at one point was gobbling up a record 200 companies each year in an expansionist binge started by his predecessor a decade earlier, as Wall Street analysts cheered, investment bankers poured unlimited credit into the company’s treasury, and revenues and earnings ballooned. **HealthSouth** prospered for a decade, its revenues fed by an aggressive acquisitions drive to get greater access to Medicare funds which were growing to match an aging population. Its profits soared each year by double digits, and its stock was bid up by nearly one-third from 1987 to 1997. Founded in 1983, **WorldCom’s** relentless drive to the top was also fueled by a series of acquisitions and mergers, including two whoppers, \$12 billion for MFS Communications (1996) and \$42 billion for MCI (1997), and a failed effort to buy Sprint for \$129 billion in 1999.

The common denominator and sustaining goal of such expansionist drives is an ever increasing valuation of the company’s stock. Stock markets embrace it, creditors extend loans based on it, shareholders covet it, executive stock options soar with it, employee retirement accounts swell along with it. Keeping it spiraling upward becomes key to the fortunes of all involved.

Classic complexity theory says that self-organizing agents interacting with each other and with their environment spontaneously form complex adaptive systems (CAS’s) that support the agents’ needs (see **Year 1998** chapter above). The better and closer a CAS interacts with its environment, the more successful it is. That means a CAS must be good at meeting and taking advantage of adaptive opportunities that arise from its surroundings. Its strategy by necessity is opportunistic. The same applies to the modern corporation, which is a type of CAS operating in a variety of market environments. As new challenges appear—a new competitor, new products, new technology, political changes—they must be matched by suitable responses. Company strategy necessarily becomes opportunistic and

episodic, dependent on both opportunities and threats arising irregularly from the market environment.

For **Enron**, energy markets surged, opening up new marketing vistas, along with fiber optic technology promising new ways of beaming television into millions of homes, plus profit opportunities from market-making commodity trades. Rapid expansion of telecommunications technology paved the way for **WorldCom's** drive for market domination. An aging, health-conscious American public was all **HealthSouth** needed to dream of unending revenues and profits by hooking its economic star to Medicare payments and rehabilitation services. **Tyco**, already an acquisition-built conglomerate, had only to take advantage of a feverish economic expansion cycle during the 1990s to find willing investors and investment bankers to feed its dizzying drive for market domination.

For all four companies, new environments created vast new opportunities for growth, expansion, and profits. They all reacted just as complexity theory predicts: their top-level executives and directors spontaneously self-organized company operations to fit and take advantage of emerging environmental opportunities. The internal excesses of fraud and corruption were spawned by the combined force of external environmental challenges and a corporate culture attuned to power and domination. In that sense, they were episodic and opportunistic, not necessarily a ubiquitous trait of corporate executive decision making.

If not universal, it is possible to conclude that corporate fraud and corruption are ever-present potentialities embedded in the fabric of corporate culture, capable of being activated by hard-wired executive motivational impulses in response to environmental opportunities for personal gain, enrichment, and power enhancement.

Birds of a Feather....

For those who believe that corporate malfeasance and crime are exceptions, or that corporate wrongdoing is normally committed by only a few "rotten apples" or "bad actors," the record and scale of recent corporate scandals will come as a wakeup call. A partial list of only the most well-known cases tells a strikingly different story. All of these companies, their top executives and directors, aided by auditors, law firms, stock analysts, and investment bankers have replicated essentially the same picture of coalitional misdeeds found in **Enron**, **WorldCom**, **Tyco**, and **Health-South**.

Here is a very incomplete roster where the webs of intrigue and plundering are virtually identical to those reported in this chapter: **Xerox**, pho-

tocopy technology; **Parmalat**, the Italian food giant; **Adelphia Communications**, the Pennsylvania-based cable company; **Lucent Technologies**, well-known telecommunications company; **Qwest Communications**, telecommunications firm; **Gemstar-TV Guide**, publications; **Cendant, Inc.**, travel and real estate; **Rite-Aid** pharmacy chain; **Ahold**, Dutch supermarket chain; **K-Mart** discount chain; **Global Crossing** telecommunications; **Office Max**, office-supply firm; **Bristol-Myers Squibb**, pharmaceuticals; **Symbol Technologies**, bar-code technology; **Beacon Hill Asset Management**, investments; **Bankgesellschaft Berlin AG**, banking; **Dynegy**, telecommunications; **McKesson**, drugs; **Banco Santander Central Hispano Americano SA**, banking; **American International Group (AIG)**, insurers.

Managers and analysts working for **Merrill Lynch**, **Credit Suisse First Boston**, **UBS**, and **Citigroup**; other investment banks **J. P. Morgan Chase**, **Goldman Sachs**, **Bank of America**, **Canadian Imperial Bank of Commerce** plus an equal number of others; and audit firms **Arthur Andersen**, **PriceWaterhouseCoopers**, **Ernst & Young**, **KPMG**, and other lesser known ones—all of these firms have supported, condoned, collaborated or colluded with the corrupt, fraudulent actions of companies charged with crimes and civil infractions. Add to this list large parts of the mutual fund industry found cheating investors *en masse* by permitting after-hours trading by a favored few.

Those “few rotten apples” begin to look more and more like an entire orchard.

Whatever Happened to Corporate Social Responsibility?

This paroxysm of corporate dishonesty, thievery, and betrayal of public trust contrasts sharply, even bitterly, with CSR’s origins a half century ago. Then, it was believed (as revealed in **The 1950s** chapter, above) that being socially responsible was the mark of a truly professional corporate leader. Business purpose was *served* by CSR, ennobling the business practitioner and justifying the position of prominence and influence granted to that class by the public.

Are we to conclude that Frank Abrams’ 1950s vision of corporate responsibility has been replaced by the turn-of-century corporate piggery of **Enron’s** Andrew Fastow, **WorldCom’s** Bernie Ebbers, **Tyco’s** Denis Kozlowski, and **HealthSouth’s** Richard Scrushy?

How far down into the corporate institution, and how widely, do corruption’s tentacles reach? Do the genes of greed tug harder at the corporate psyche than the culture of ethical caring? Was Frank Abrams a false

prophet? The CSR Grail an illusion?

These hovering questions haunt the hopes of all who seek goodness within corporate enterprise. Is it possible that some of the answers are to be found within the nation's business schools who are charged to prepare tomorrow's leaders? Have they been complicit in corporate crimes? More hopefully, can they restore Frank Abrams' vision? Those challenges are examined next in **Part IV**.