The Managerial Mistakes that a CEO Must Avoid

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Abstract

The purpose of this study is to identify the managerial mistakes that CEO's must avoid in order not to bring ruin to themselves and to their corporations. The article analyzes the case histories of recent CEO's whose mistakes in leading their corporations cost them their jobs and resulted in great financial loss to their shareholders. The mistakes made by the CEO's whose cases were analyzed can be classified according to causative factors. These causative factors can be incorporated into a guide for avoiding the unethical behavior that is associated with the factors and their ruinous consequences.

Keywords: Corporate Leadership Mistakes

Introduction

The United States and much of the world's economically developed and developing nations are in a period economic ruin (The G20 and the World Economy, 2009). The cause of this period of economic disaster is human error, human moral and ethical failings, and an appalling lack of corporate leadership knowledge. The purpose of this paper is to offer an analysis of corporate leadership behavior—moral, ethical, and legal—that results in ruin to the chief executive, his/her corporation, the employees of the corporation, the shareholders, creditors, and the public.

Method

The paper relies entirely on articles printed in periodicals and newspaper accounts of corporate executives (CEO's) who made conscience decisions on how to lead their corporations that resulted in legal charges being brought against them and their corporations for violations of various regulatory laws. Based on these published accounts, the author attempts to group the acts of the CEO's into types of bad leadership behavior or leadership style.

How a CEO May Cause Harm to Himself and to His Corporation

Despite all the time and effort a CEO may spend studying management and leadership he may still fail to provide adequate leadership to his corporation. This paper is focused on understanding why CEO's failed in their efforts to lead their corporations. It is unlikely that a CEO deliberately sets out to do harm to himself and to his corporation anymore than a man sets out to make himself ill. True, he may know that certain things such as excessive drinking or smoking may adversely affect his health; but, his intended actions are not to make himself ill. No, his actions are directed toward gratifying his desire for the pleasurable effect of smoking and drinking. So also is the case of the CEO who, for example, spends the resources of the corporation in a lavish and exorbitant fashion (Safer, 2004). Another example is that of the CEO who influences the board of directors to pay him an exorbitant salary package that dilutes shareholder's equity and creates a poor image of the corporation (Adelphia founder John Rigas found guilty, 2004). The CEO looks only at his personal gain and satisfaction and ignores the impact of his actions on how he is perceived by the shareholders, and how this unfavorable perception will affect his ability to lead the corporation. Even though the harm was not deliberately intended—that does not exculpate him from blame, nor does it spare him from the consequences of his actions which can lead to the loss of his position and reputation.

In writing this article, the author makes the assumption that a person can learn to be an effective and successful leader. This is no trivial assumption because there are many people who hold the belief that leaders have some special quality that endows them with the leadership skills of a born leader. Or they may believe that a person either has the ability to be a leader or they do not—and if he does not have this natural ability he will never be a good leader. This belief is utterly false and nothing is further from the truth (Yukl, 1994). The truth of the matter is that leadership like any skill is something that is learned through study, observation, and perfected through practice and trial and effort (Bass and Stodgill, 1990). It is not easily mastered, however. It requires the willingness to dedicate time and effort and the intelligence to learn from the successes and mistakes of others as well as one's own mistakes and successes. One of the reasons it is so difficult to learn the art of leadership is because it requires a thorough understanding of the people one wants to lead—and people are difficult to understand and are constantly changing according to the circumstances in which they find themselves. Furthermore, there are so many different leadership styles to learn to use and apply to any given situation. A leadership style may be effective and successful in one corporate situation, and the same leadership style in another corporate situation may be unsuccessful—even disastrous.

The theoretical work done by Fred Fiedler (1997) provides an excellent insight into how various leadership styles may be used in different corporate situations. Dr. Fiedler's premise is that there is no leadership style that is the best one to use in all situations. That is to say, there is no universal best leadership style that will work successfully across all corporate situations. The most effective leadership style is the one that is the most appropriate based on situational factors prevalent in the corporation at that time. The importance of Dr. Fiedler's work to a CEO is that it supports the premise that leadership can be learned. His Contingency Model can be used to analyze why a CEO using a leadership style in one particular corporate situation was successful, while a CEO using the same or a similar leadership style in a different corporate situation was unsuccessful. By the use of the case analysis technique the author of this article examines the mistakes made in corporate leadership situations with the intent of offering an explanation of what went wrong and what could have been done to have avoided the failure.

Power implies authority over others. Without power there is no base for authority. If employees can at their will choose to obey and comply with directives, or not to obey and comply, then the CEO is not in control and he is impotent in his position. The more power and authority a CEO has over his subordinates the more secure should be his position. What is true of power and authority is also true of force and coercion. There is nothing inherently evil in the use of force and coercion. Force and coercion can be brought to bear to achieve good outcomes. Indeed, sometime nothing less than force and coercion will suffice to achieve a good and necessary outcome. Would anyone argue against the use of force to subdue a violent criminal or the use of severe penalties to coerce people into compliance with social legislation? Would labor unions and management negotiate and resolve differences without resorting to violence were it not for the knowledge that if they did not comply with the terms of the National Labor Relations Act they would face heavy legal penalties (Twomey, 2010)? Of course it is not. It is the misuse of force and coercion that is evil and ineffective and must be avoided by a CEO in controlling his corporation. The misuse of force and coercion is one of the reasons that CEO's fail and lose their positions. For this reason it is more instructive for a CEO to understand why Kenneth (Ken) Lay's career ended so badly at Enron than it is to understand why Jack Welch was considered to be successful at General Electric.

The Misuse of Force Coupled With the Appearance of Arrogance - The Case of Al Dunlap

There is an old adage that says: "Pride goes before the fall." As the first example of a CEO whose career was ended by the misuse of force and authority consider the case of Albert Dunlap to whom the press gave the tag name *Chainsaw Al.* With reference to Mr. Dunlap, an apt quote from the Bible would be: "… for all those who take the sword will perish by the sword." (Matthew, 26:52). Among the personal character flaws that will cause a CEO to lose his position of leadership is a callous and ruthless disregard for the employees who he causes to lose their jobs. It is worthwhile to devote some time to understanding the background and career of Mr.

Dunlap to see what he did to lose his position as a CEO, and what, in retrospect; he could have done to avoid being terminated.

Albert John Dunlap was born on July 26, 1937, in Hoboken, New Jersey to a middle class family. He secured an appointment to West Point and was graduated 537th out of a class of 550. Upon graduation he was commissioned a second lieutenant and served only the mandatory three-year term. One of his early positions was as a manager at Lily-Tulip, the paper cup manufacturer. From the start of his career he showed a callous disregard for his fellow employees. At Lily-Tulip, as part of a restructuring project he was responsible for a layoff of 20 percent of the workforce. Management at Lily-Tulip considered the layoffs necessary and Mr. Dunlap received favorable recognition for the restructuring project. He followed the same pattern of cost-cutting by reducing the number of employee positions through restructuring the corporation at Crown-Zellerbach.

Later at the Scott Paper Corporation he would again follow the same pattern of cutting expenses by eliminating jobs and employees through a restructuring of the production operations. He instituted massive layoffs. During his term as the CEO at Scott he terminated eleven thousand employees, including other executives. However, the restructuring served the shareholders well. Scott Paper's stock raised from $38.00 a share to $120.00 a share. He negotiated a merger with Kimberly-Clark that enhanced shareholder's equity by $6 billion. By every measure he accomplished a successful turnaround for Scott Paper. He also increased his own fortune by earning $100 million for his efforts. Mr. Dunlap apparently took delight in being regarded as a tough manager—so much so that he wrote a self-aggrandizing book titled: *How I Save Bad Companies and Make Good Companies Great* (1997).

With such extraordinary success at Scott it is easy to see why the Sunbeam-Oster Corporation, a $1.2 billion maker of electric blankets, outdoor grills, coffee makers and other household products, was so eager to get him as their CEO. In July of 1996, following his spectacular success at Scott Paper, he was appointed CEO of Sunbeam. Proof of Mr. Dunlap's appeal as a corporate reorganizer/turnaround executive was evident when Sunbeam announced his appointment as their CEO—and the company's stock went up by almost 50 percent. There were a lot of happy shareholders at that moment. But their happiness would prove to be short lived. Sunbeam's stock that jumped 50 percent earlier would continue to go up in value until later when it would drop like a hanged man through a trap door. On July 22, 1998, Sunbeam's stock closed at under $9.00 after hitting a high of $52.00 in March of the same year (Byrne, 1999). What went wrong?

During his term as CEO at Sunbeam, Mr. Dunlap shut down or sold off 6 out of 18 plants and terminated 12,000 employees—a massive restructuring of the corporation. He seemed to dolt on his reputation as a callous manager. The traits of arrogance and ruthless indifference toward his subordinates would eventually suck him into a vortex drawing him inexorable towards the destruction of his career. At least this is how some of the media would describe what was to happen to Mr. Donlap. But, if it was not the trait of arrogant, callous indifference toward the employees he terminated that brought him down, then what was it?

Perhaps a factor that caused his failure at Sunbeam was—ironically—his success at Scott Paper. He built his corporate reputation on restructuring companies and laying off employees. Not just a few employees, but thousands of employees including senior officers and closing down plants. He had every reason to believe that based on his previous experience this approach was workable. In trying to understand how a CEO can have a successful reign in one corporation and then have a disastrous term in another corporation, it is helpful to bear in mind that corporations differ in significant ways. What worked well in one corporate setting may not work as well within a different corporate setting. More significantly, a CEO changes over the period of his tenure in that position. Some CEO's grow more efficient and their success is more lasting. Other CEO's, those with character flaws, make the mistake of believing that circumstances that came about by chance were not due to chance, but because of something they did that was right. This may have been the case with Mr. Dunlap. He thought that his callous style of leadership was the reason that Scott Paper was able to reduce its operating costs and to be merged with Kimberly-Clark to the benefit of their shareholders. But there may have been other factors beyond what Mr. Dunlap did that contributed to the favorable outcome. So, perhaps being callous in one's leadership style and reducing costs by massive layoffs might not have been the reason that Scott Paper's stock appreciated. Further analysis is needed before jumping to conclusions as to why the very same tactics that Mr. Dunlap used successfully at Scott Paper did not work as well at Sunbeam. Could it be that there was an outrage at Sunbeam over his callous elimination of people's jobs that did not occur at Scott Paper? Or could his arrogant self-aggrandizement and self-enrichment at the expense of other employees have contributed to his downfall?

No, the personal flaws in Mr. Dunlap's character of arrogance, self-aggrandizement, and indifference towards other employees were only contributing factors. In order to understand what caused Mr. Dunlap to be relieved of his responsibilities, it is necessary to look further into the corporate situation at Sunbeam. The answer is that he used a financial maneuver that proved to be fatal to his career and ruinous to the corporation. The financial maneuver is called *bill and hold*. Sunbeam, at Mr. Dunlap's direction, entered into deals with its retailers where Sunbeam's products would be sold at large discounts to its dealers and held in third-party warehouses for later delivery. According to Sunbeam's auditors this was not an illegal transaction, however the volume was excessive. By this maneuver, Mr. Dunlap overstated revenue by a significant amount. In 1997, Sunbeam had booked an 18 percent increase in sales that actually had not been delivered.

On March 19, 1997, Sunbeam acknowledged that its first-quarter earnings would be below Wall Street analysts' estimates. At that point things began to unravel quickly. By April 3, 1998, Sunbeam's stock had fallen 25 percent to a little over $34.00. Mr. Dunlap tried to make corrections admitting that some bad deals were made with excessive discounts to dealers. But matters did not improve. On June 9, 1998, he made a final fatal error—he lost control of his composure at a board meeting—an unforgivable error. He accused a major shareholder, billionaire Ronald Perelman of a conspiracy to drive the price of Sunbeam's stock down so that he (Perelman) could buy out the company. Mr. Dunlap then uttered the fatal words: "Either we get the support we should have or [Chief Financial Officer] Russ and I are prepared to go…. Just pay us" (Byrne, 1998). The impression that Mr. Dunlap made on the directors was devastating. Their leader, Mr. Dunlap, had become undone—he no longer held their confidence. A few days later the board reconvened and placed a conference call to Mr. Dunlap. Their message was brief, as it always is: "All the directors have considered the options presented to us last Tuesday, and we have decided that your departure from the company is necessary." That marked the end of Mr. Dunlap's term of CEO at Sunbeam and most probably his career as a CEO.

The lesson to CEO's is simply this: A CEO must never lose control of his emotions in the presence of anyone in the corporation, and most certainly never at a meeting where either senior officers or board members are present. A CEO must always appear to be in control of every situation and to have a plan for addressing whatever problems may be present at that time.

Consider the disastrous effect on an operating room staff of nurses and other surgeons if the operating surgeon appeared to be impaired by emotion at the onset of an operation. Would it not seem obvious that those in attendance would immediately take steps to stop the surgeon from beginning the operation? There is certainly a reasonable probability that if Mr. Dunlap, instead of appearing emotionally upset and making a statement indicating that he was ready to abdicate his responsibilities, had offered a plan for addressing the problem of declining share price because of the overstatement of sales, he would not have created the impression that he was no longer to be trusted to lead the corporation. In essence, Mr. Dunlap resigned. That was a fatal and irreversible mistake. Perhaps his arrogant nature led him to behave as he did—to his detriment. In his case the Bible quote was realized: "…for all those who take the sword will perish by the sword."

Question: Were there signs or markers that Mr. Dunlap's way of dealing with people would ultimately result in major problems to the corporation? If you were a member of the board of directors of the corporation and you observed those signs what action could you have taken?

Corruption and Fraud: The Twin Charges Fatal to a CEO's Care

There have been several CEO's who have suffered the destruction of their careers in the last ten years. The corporate world has changed significantly in the past ten years, especially since the adoption of the Sarbanes-Oxley Act that imposes strict regulations on corporations. In addition to stricter regulation by regulatory agencies, there is more attention focused on corporate dealings by the news media than ever before. This closer scrutiny and wide-spread coverage of corporate activities has made it more important than ever for CEO's to be on guard and to be aware of their corporate leadership practices. What may have slipped by the attention of regulators and the news media a few decades ago is much more likely to be discovered and brought to light in today's corporate environment.

The Case of Ken Lay and the Enron Corporation

Perhaps the most heavily publicized case of corporate fraud and corruption since the start of the year 2000 was that of Kenneth (Ken) Lay, the CEO of the Enron Corporation. Ken Lay was the CEO and Chairman of Enron from 1986 until his resignation on January 23, 2002, (Achman, 2002). He was born in Tyrone, Missouri, attended the University of Missouri, where he majored in economics, and earned a Ph.D. in economics at the University of Houston in 1970. He started his career with the Exxon Mobil Corporation. He also worked as a federal energy regulator and moved up to undersecretary for the Department of the Interior in the 1970's.

In 1985 he bought the Houston Natural Gas Company and changed the name to Enron. He became one of the highest paid executives in the United States with a compensation package of over $42 million a year. He was very well connected with people at the highest levels of government. From this high pinnacle of corporate success, he was to fall to ruin taking with him other members of the Enron corporate leadership team, the corporation itself, and thousands of Enron employees who would lose much of their retirement savings held in Enron stock. What went dreadfully wrong?

On July 7, 2004, Ken Lay was indicted and charged with 11 counts of securities fraud, and making false and misleading statements pertaining to the collapse of the Enron Corporation. Earlier, in December 2001, Enron filed for bankruptcy, the largest company to file for bankruptcy in the United States at that time. Investors lost billions of dollars and 20,000 employees lost their jobs—and many lost their retirement savings, a catastrophe of record proportion in all respects. During his trial, Mr. Lay claimed that almost all his wealth, approximately $40 million was invested in Enron stock, and that he also had suffered severe financial losses. He claimed during his trial that Enron's collapse was caused by a conspiracy among short sellers, fellow executives, and the news media. The jury, however, did not believe Mr. Lay's account of the events that led up to the collapse of the Enron Corporation. On May 25, 2006, Mr. Lay was found guilty of conspiracy and making false statements. Before he was scheduled to be sentenced, he suffered a fatal heart attack, (Crawford, 2004).

It is interesting to note that unlike Albert (Al) Dunlap, Ken Lay was not universally held in contempt. True, the employees who lost their jobs and savings felt no remorse over his death, but many others felt that he had been singled out by overzealous federal prosecutors to showcase their drive against corporate corruption. They accused the news media of vilifying him and of character assassination. Clearly, the collapse of Enron was a catastrophic tragedy with its impact on all those people associated with it. What can be learned from an analysis of the events leading up to its filing for bankruptcy in December 2001 and Mr. Lay's indictment in July of 2004?

To begin with, Mr. Lay had no apparent character flaws that made him detested or despised. There is no evidence that he was cruel or insensitive toward his employees. Certainly, there was clear evidence that he mislead employees and others regarding the true financial condition of the corporation. But his motive could have been, as he claimed, to avoid panicking investors into a sell off of Enron's stock. Trying to determine a person's motivation is always difficult and the results are at best inconclusive. This having been stated, what is known is that Mr. Lay had an impressive list of accomplishments that indicate he saw the importance of demonstrating a commitment to social and civil service. Some of his awards and honors include: The Torch of Liberty Award of the Anti-Defamation League, the Super Hero Honoree Award for Child Advocates, Award of Distinction from the March of Dimes, and the Brotherhood Award from the National Conference of Christians and Jews. He was also remembered for his support of projects in the Houston black community. The awards, honors and civic project work are mentioned because it is important for a CEO to be noted for his support of social, civil, and community projects. Often this helps sway the balance in favor of a CEO who is getting a lot of negative press coverage. One can only speculate as whether his good works might have led to a favorable outcome during a prolonged appeal of his conviction had he not died before sentencing.

The problems with Enron were caused by it taking on too much debt. That was the root of the problem—Enron over extended its financial resources. It had used a web of partnerships and other corporate entities to borrow and conceal more than a billion dollars in debt. Additionally, it misrepresented its true profitability by recording inflated profit figures. Its balance sheets, income statements, and other documents were deliberately misrepresenting the corporation's financial condition. The U.S. Justice Department in its investigation charged that Enron's management manipulated Enron's books. Furthermore, that Enron's management including Andrew Fastow, Chief Financial Officer and ex-CEO, Jeffrey Skilling lied about Enron's finances to government regulators, the financial community (including Bank of America), its employees, and the public including its investors. During the period from August through October 2001, Mr. Lay sold 918,000 shares of Enron stock. During this period he told 28,000 employees that the corporation's liquidity was fine. Additionally, Mr. Lay was accused of defrauding three banks including the Bank of America to obtain its lines of credit, (Peters, 2006). He claimed that the sale of his Enron stock was done to meet margin calls. In essence, an analysis of the cause of Enron filing for bankruptcy was that it had taken on too much debt, had hidden the extent of its debt through fraudulent accounting practices, and other misrepresentations. When Enron was unable to obtain any further credit and it was unable to meet its debt obligations, it had no alternative but to file for bankruptcy.

Regarding the fatal mistakes made by Mr. Lay they seem to be related to his attempt to cover up the fraudulent accounting practices and to mislead everyone concerning the true condition of the corporation. He tried to protect his corporation when its condition was such that it was beyond saving. What could he have done to have saved the corporation before it got into such dire straits? Of course, in retrospect anything said as to what he could have done must seem like an exercise in 20/20 hind sight. But, most financial analysts would agree that the conditions leading to Enron's debt situation could have been caught earlier than they were, and remedial plans could have been set in motion. Perhaps a lesson, in retrospect, is that it is best to be open with one's creditors sooner than later, and not to try to deceive them in extending more credit than can be repaid.

But his more serious mistake was in permitting his chief financial officer to produce fraudulent accounting statements, and then lying to everyone about the true condition of the corporation. The loss of one's corporation is difficult to bear—but to face the prospect of prison is even more unbearable. Mr. Lay paid dearly for his mistake as did the employees and the shareholders. That is proof that the penalty for fraud is dear and not worth the risk of a prison sentence. As William Powers, dean of the University Of Texas School Of Law put it: "A fundamental default of leadership and management [begins] at the top, with the CEO." (Ackman, 2002).

Question: Do you think that when a corporation's financial position has reached the point where it faces a high probability that it may not be able to recover, that the CEO should make this clear to the board of directors? As a member of the board of directors, what signs or markers in Mr. Lay's actions offered clues that he was acting imprudently? What approach would you take to protect the corporation?

Crimes That CEO's Commit That Lead to Disaster for Themselves and for Their Corporations - The Case of John Rigas and the Adelphia Communications Corporation

It is a regrettable failing in the nature and character of some CEOs that cause them to succumb to the temptation to use their positions to enrich themselves by illegal means.

An example of a CEO who made this fatal error is John Rigas, the founder of the Adelphia Communications Corporation. An analysis of the facts and the events leading to the conviction of Mr. Rigas for conspiracy, bank fraud and securities fraud will provide a valuable lesson on the danger of resorting to the misappropriation of corporate funds and the attempt to hide the misdeed.

Perhaps a clue as to why some CEOs have the regrettable proclivity toward the misappropriation of corporate funds is that they regard the corporation's assets and resources as their own assets and resources. They seem to think that since they have control over the corporation's assets and funds they can access and use them as though they had every legal right to use them as they please.

This proclivity seems to be more prevalent where the CEO's were the founders of the corporations they built up to become major corporations. Did Mr. Rigas, who founded and built up the Adelphia Communications Corporation, feel he was entitled to use the corporation's assets and funds as though they were his own and not the property of the shareholders? Do CEOs who were accustomed to the free use of their corporation's resources when they were the sole corporation owner as well as the leaders of their corporations believe that after they went public and sold shares to the public they could still behave as though the corporation's assets were still solely their own, and that they were not accountable to the shareholders who were now the new owners? To use an analogy, does someone who sells his house to a buyer believe that he can still have access to the house and to its contents? Why of course not.

Continuing with the analysis of Mr. Rigas' failed leadership of the Adelphia Communications Corporation, it is helpful to understand something about him, his career, and how he came to be the head of one of the largest cable companies in the United States. Mr. Rigas was born in 1924 in Wellsville, New York. He served with the U.S. Army during the Second World War and saw combat in France (Bull, 2004). He earned a BS in Management Engineering from Rensselaer Polytechnic Institution. He started the Rigas Cable Television Company that had the TV cable franchise for his hometown in Caldersport, Pennsylvania. He then formed a partnership with his brother Gus to form the Adelphia Corporation. He started to borrow heavily to buy suburban cable companies and Adelphia became one of the largest suburban cable providers with 5.6 million customers in 30 states. Adelphia also provided long-distance telephone service to 110,000 customers in 27 states and high-speed cable Internet service. Mr. Rigas was regarded as a successful entrepreneur and received many honorary degrees. Where did Mr. Rigas go from rags to riches to ruin, and what can be learned from his misfortune?

Mr. Rigas lived the life of a successful, wealthy corporate executive. Indeed, evidence introduced at his trial painted the picture of a man who spent money lavishly. He built a palatial $30 million Adelphia headquarters building in Caldersport Pennsylvania. He purchased 3600 acres of timberland outside his home in Caldersport at a cost of $26 million. Other examples of excessive spending were also introduced in the court's records. According to the court's record, Mr. Rigas' son Timothy was so concerned with his father spending of corporate funds that he put a limit on his father's withdraws of corporate funds at $1 million a month. The pattern was clear; Mr. Rigas was spending corporate funds with total disregard for the interests of the shareholders, a serious mistake for a CEO.

The more serious mistake, however, was resorting to a complex scheme to lie on financial filings and to attempt to hide massive corporate debt in the magnitude of $2.3 billion. Mr. Rigas and his son Timothy would end up being convicted of conspiracy, bank fraud, and securities fraud. They deceived investors, financial institutions, and stole the funds of the corporation to enrich themselves—the most serious and fatal mistake of all. And for this mistake John Rigas was sentenced to 15 years in prison and his son Timothy was sentenced to 20 years in prison.

The Adelphia Communications Corporation was placed in bankruptcy and its assets sold off. Philadelphia-based Comcast Corporation and The Time Warner Corporation agreed to acquire Adelphia's cable assets and some liabilities for $12.7 billion in cash and 17 percent of the common stock of Time Warner's corporate subsidiary, Time Warner Cable, Inc. Adelphia's long-distance business was sold to Pioneer Television for $1.2 million, (Shore, 2005). The mistake of the father, John Rigas, sadly caused the end of the Adelphia Communications Corporation, and the loss of both his freedom and that of his son—a crushing blow.

What is the lesson to be learned? Perhaps, the lesson to CEOs is best expressed in the words of Epictitus as expressed in the *Enchiridion(a Manual)*: " So remember [if you treat] what is others' [as] your own, you will be hindered, you will mourn, you will be disturbed, and you will blame both gods and humans, but if you think only yours is yours, and another's, just as it is another's, no one will ever compel you, no one will hinder you, you will not blame anyone, nor accuse someone, not one thing will you do unwillingly, no one will harm you, you will have no enemy, for you will suffer no harm from anyone" (Epictitus, 2003). Perhaps, if Mr. Rigas and his son had read and learn from Epictitus they would not be serving their sentences in prison.

The Rigas case has two factors that could be of concern to members of the board of directors, creditors, and shareholders. The first is that John Rigas was the founder of the Corporation and was still in a position to spend large sums of the corporation's money. The second factor was that his son was running the corporation. What signs or indicators were there in this case that the two factors would be the underlying causes of the corporation's financial problems?

The Case of Bernard (Bernie) Ebbers and the World Com Corporation

Bernard John (Bernie) Ebbers was born on August 27, 1941, in Edmonton, Alberta, Canada. He attended the University of Alberta, but later transferred to Mississippi College where he earned a BS in Physical Education. He began his business career by operating a chain of motels in Mississippi. In 1983, he joined several other investors in the newly formed Long Distance Discount Services, Inc. In 1985, he took over as CEO of the corporation. The company acquired over 60 other independent telecommunication companies. In 1995, the company changed its name to World Com. In 1996, World Com acquired MFS Communications, Inc., which at that time owned UU Net, for $12 billion. In September 1998, World Com merged with the MCI Corporation for a reported $37 billion. It was one of the largest corporate mergers in US history. In 1999, MCI World Com attempted to acquire Sprint Communications for over $115 billion. However, the attempted acquisition was blocked by US and European antitrust regulators. At this time a general downturn was beginning to take place in the telecom market and World Com stock price began to decline. In the first quarter of 1999, World Com stock peaked. Mr. Ebber's personal holdings were estimated to be about $1.4 billion. He was listed by *Forbes* magazine to be 174th in its list of the 400 richest people. He was honored by Mississippi College with an Honorary Doctorate of Laws. The merger of World Com and MCI Communications brought fame and fortune to Mr. Ebbers. MCI World Com was the number four communications company in the US. *Forbes, Business Week, Financial World, Fortune,* and other magazines praised Mr. Ebbers for his stellar performance in pushing MCI World Com to number 80 in the *Fortune* 500 *List of Best Corporations.* The *Wall Street Journal's Shareholders Scoreboard* ranked MCI World Com number one among telecommunication companies in return to shareholder investment in 1997, 1998, and 1999. He was among 16 outstanding CEO's recommended by *Financial World,* and *Business Week* ranked him as one of the top managers in 1997. Mr. Ebbers was inducted into the Mississippi Business Hall of Fame. He served as chairman of the board of directors of the Competitive Telecommunications Association from 1993 to 1995. On July 16, 2001, President Bush announced that he intended to appoint Mr. Ebbers to the President's National Security Telecommunications Committee (NSTAC). The NSTAC is composed of up to 30 presidential appointees. In its advisory role the NSTAC provides industry-based analyses and recommendations on policy and technical issues related to telecommunications, information systems infrastructure protection, and other national security and emergency concerns (O'Donnell, 2002). From this extraordinary pinnacle of success, Mr. Ebbers began his descent into the lowest depths of personal ruin, dragging down with him the World Com Corporation and its shareholders. Again, what can CEO's learn from an analysis of Mr. Ebber's leadership of the World Com Corporation? It appears that much can be learned.

Mr. Ebbers start on the road to ruin began when he and members of his management team began to make false and misleading entries on Enron's corporate statements. The magnitude of the accounting misstatements was in the range of $3.85 billion to $11 billion. On July 8, 2002, Mr. Ebbers was subpoenaed to appear before the U.S. House Committee on Financial Services. Mr. Ebbers stated he had nothing to hide. He denied engaging in any criminal or fraudulent conduct. After making the statement he asserted his Fifth Amendment right against self-incrimination. He was threatened with contempt of Congress charges, but the charges were never brought. After nine hours of attempting to get information from Mr. Ebbers and other witnesses, the committee members still had not gotten any sort of information concerning the accounting practices used to hide debt and expenses, and to inflate earnings by nearly $3.9 billion (Schoenberger, 2002). During the hearing some of the witnesses attempted to blame World Com Chief Financial Officer, Scott Sullivan. John Sedgmore, who replaced Mr. Ebbers as CEO of World Com, tried to defend the company by saying that he and others had investigated the matter to uncover any wrong doings and had cooperated with authorities. Mr. Sedgmore also blamed the company's external auditors, Arthur Anderson, for failing to catch the accounting problems. Related to the questioning of members of the World Com Corporation and the Arthur Anderson auditor, Melvyn Dick, was the questioning of Jack Grubman, an analyst with Solomon Smith Barney in New York. Mr. Grubman was questioned because he recommended World Com stock to his firm's investors—even when it appeared he suspected that the corporation was in serious financial trouble. Mr. Grubman's involvement in the World Com affair and his role in touting its stock to his firm's investors were viewed by the financial industry as a scandal in its own right.

The road to ruin for Mr. Ebbers and World Com went into a steeper descent when on August 27, 2003, the Oklahoma Attorney General, Drew Edmondson, filed a 15-count indictment against Mr. Ebbers (Moritz, 2003). The charges were dropped with the right to refile retained on November 20, 2003. Even though the charges were dropped, it is interesting and instructive to see exactly what it was that the Oklahoma Attorney General charged Mr. Ebbers with doing that constituted a crime.

The following statements are taken from the Oklahoma Attorney General's indictment against Mr. Ebbers (Ebbers, 2003): Count 1: Violation of the Oklahoma Securities Act 71 O.S. Section 101 (1). On or about…March of 2001, in connection with the offer, purchase, or sale of defendant World Com, Inc.'s securities…Bernard J. Ebbers…caused, directed, or allowed certain major operating expenses to be capitalized…and allowed said expenses to be materially understated and income to be materially overstated for the fiscal year ended December 31, 2000, in defendant World Com Inc.'s publicly available 10-K statement filed with the SEC…. Further, the Defendants were well aware that…the results of the entries would be reflected in the 10-K…and the information contained in the 10-K would be used by investors…during the course of the offer, purchase or sale of Defendant World Com Inc.'s securities, and…investors…would be defrauded by the information contained in the 10-K [Statement]. The remaining counts in the indictment alleged that Mr. Ebbers instructed Scott Sullivan, the CFO, to make journal entries into World Com Inc.'s general ledger corresponding to expense accounts that were materially understated and to make entries that materially overstated income. Furthermore, Mr. Ebbers…[The] defendant did not provide…any supporting documentation or any proper business rationale for the entries. There was no justification in fact or under General Accepted Accounting

Principles (GAAP) for the entries. In essence, Mr. Ebbers was charged with directing his CFO, Scott Sullivan to enter false and misleading information on the corporation's financial statements including the K-10 Statement filed with the SEC with the intent to mislead and defraud investors and financial institutions

On March 2, 2004, federal authorities indicted Mr. Ebbers on charges of securities fraud and conspiracy. He was found guilty of all charges and sentenced to 25 years in federal prison. The toughest sentence ever handed down in a corporate accounting case (Frieden, 2004). On July 28, 2006, a federal appeals court upheld the conviction and 25-year prison sentence of former World Com CEO Bernard Ebbers on charges related to a multi-billion dollar accounting fraud. The ruling by the three-judge panel cleared the way for him to begin serving the 25-year prison sentence. The opinion of the court written by Judge Winter is especially telling of how the federal courts view corporate crime. Referring to Mr. Ebbers' crime, he stated that Mr. Ebbers' actions to hide World Com's financial problems were substantial and had cost investors dearly. He went on to say, "The methods used [by Mr. Ebbers] were specifically intended to create a false picture of profitability even for professional analysts [and] that in Ebbers' case was motivated by his personal financial circumstances. Given Congress' policy decisions on sentences for fraud, the sentence is harsh but not unreasonable" (*Money*, 2008). The message delivered by the federal courts is painfully clear—if a CEO is convicted of defrauding investors and financial institutions, he will be punished harshly. The World Com Corporation and its investors also paid a dear price. The amount of the accounting fraud was estimated to be in the range of $11 billion which caused the collapse of the World Com Corporation which was then declared bankrupt.

What final remarks can be made on such a sad ending for the man and the corporation? According to reporters Jayne O'Donnell and Andrew Backover, of the *USA Today* magazine, Mr. Ebbers' high-risk act came crashing down on him, (2002). Their fix on the story of Mr. Ebbers is that he built up World Com with reckless bold deals and big gambles that ultimately crashed. Again, according to their article published December 11, 2002, in *USA Today* in the Money section, Mr. Ebbers spent money, his own and that of the corporation lavishly. For example, he bought Canada's biggest ranch and two farms. The ranch manager, Joe Gardner, was said to have boasted that after Ebbers bought the ranch in British Columbia in 1998, that, "We have all the money in the world." Additionally, he invested in a minor league hockey team, a trucking company, an all-terrain vehicle dealership, a lumber yard, enough timberland to cover half the state of Rhode Island, and a yacht company. He financed these purchases with $408 million in loans from World Com. It seems he and Mr. Rigas of Adelphia both believed that they could use the corporation's assets for their personal financial transactions.

Mr. Ebbers built World Com into one of the largest corporations in the telecom industry. In 1999, his personal fortune was estimated at $1.4 billion and *Forbes* listed him as one of the richest men in the U.S. But his investments showed a lack of good judgment. He paid a huge premium for the companies he acquired. He overpaid for the ranch, the timberland, the yacht yard, minor league hockey business, and seemingly everything else he invested in. According to the bankruptcy court record, World Com's many acquisitions were poorly integrated and lacked strategic planning. Mr. Ebbers' plan was to grow by acquisitioning. But the strategic plan was seriously flawed. The acquisitions were not well integrated into the corporate structure. In all, World Com made about 60 acquisitions, with its acquisition of MCI in 1998, costing $40 billion. These acquisitions caused big financial problems. Debt mounted on debt. Mr. Ebbers was alleged to have used World Com shares to secure $1 billion in personal loans. [Actual estimates of the amount of the loans differ.] When World Com stock did rise, he used the increase in stock value to make more acquisitions. But as stock prices dropped it became increasingly difficult to meet the debt obligation for both his debt and that of World Com. When World Com became increasing unable to manage its excessive debt, Mr. Ebbers made the fatal mistake of directing his CFO to hide the true condition of the corporation by entering false data on its books, and even worst, to enter false data on its K-10 Statement. At that point he reached the end of the road—federal prison.

The cases of Ken Lay (Enron) and Bernie Ebbers (World Com) have some interesting similarities. Both men were skilled and experienced executives. Both men were successful in increasing the size and scope of their corporations. Both men made decisions and exercised judgment that brought an end to their careers and financial ruin to their corporations. How were the decisions each man made similar and how were they dissimilar? As a board member what signs were there that each man was embarked on a course that would end in financial ruin for the corporation, its employees, and shareholders?

Conclusion

As is often the problem with case studies, it is not easy to formulate a conclusion that flows smoothly and flawlessly from the analysis. This is also true of this author's attempt to identify behavioral flaws that can serve as markers associated with financial ruin resulting from faulted executive leadership. However, there does seem to be value in identifying, studying and classifying flawed executive behavior that if detected in the formative stages, can be halted before it progresses to the terminal stage where a corporation, its shareholders, and the general public suffer serious losses. This then is what the author offers as the value of this study—the identification of flawed corporate executive behavior patterns that have the proclivity for doing irreparable harm to the corporation. As all corporations have a board of directors, it seems reasonable that board members should be vigilant in monitoring CEO behavior to preclude CEO's from engaging in the types of behavior presented in this study.

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