FROM GREAT TO GHASTLY: HOW TOXIC ORGANIZATIONAL CULTURES POISON COMPANIES THE RISE AND FALL OF ENRON, WORLDCOM, HEALTHSOUTH, AND TYCO INTERNATIONAL

David R. Lease, Norwich University

Abstract

This paper presents an analytical and comparative study of four recent corporate scandals involving organizations that had previously been recognized as both ethically and organizationally sound. Based on these case studies, the following issues are discussed:

(1) The role of leader behavior and organizational/leadership styles in shaping the corporate organizational culture of an organization, and

(2) The extent to which this culture renders the organization and its members (including the top executives) prone to ethical misbehavior.

The four companies selected for this case analysis are: Enron Corporation, WorldCom, Inc., Tyco International, Ltd., and HealthSouth Corporation. Each case is considered individually. The basic elements in the scandal are outlined and the principal aspects of each organization's corporate culture discussed, with special emphasis on the influence of leadership styles and leadership behavior/practices on organizational culture. The four cases are then compared and contrasted in the light of the existing evidence on the relation between corporate culture and ethical misbehavior.

PRELUDE

"We were doing something special. Magical. It wasn't a job – it was a mission. We were changing the world. We were doing God's work."

– Jeffrey Skilling, former Enron COO, President and CEO in the immediate aftermath of Enron's bankruptcy filing*

"I don't want to just be rich. I want to be World Class rich!"

– Kenneth Lay, former Chair & CEO, Enron Corporation**

"I've thought about this a lot, and all that matters is money."

– Jeffrey Skilling, explaining his theory of motivation to another Enron manager***[1]

INTRODUCTION

In the mid-1990s, when Chief Executive Officer (CEO) Bernard Ebbers used rigorous cost control and an aggressive acquisition strategy to turn his small long-distance telephone company into a global telecommunications giant named WorldCom, Wall Street quickly fell in love (Jeter, 2003). Wall Street analysts were particularly enamored of WorldCom Chief Financial Officer (CFO) Scott Sullivan, the man who engineered the WorldCom--MCI takeover and who was widely viewed as "the key to WorldCom Inc.'s financial credibility" (Young & Perez, 2002, p. B1). In 2002, four years after brokering the historic WorldCom/MCI deal, Sullivan was fired from WorldCom and named by prosecutors as the chief architect in what was ultimately revealed to be a $11 billion accounting fraud (the world's largest), leading to the biggest Chapter 11 bankruptcy filing in U.S. history (Young, 2005, p. C3).

Before it collapsed in fraud, scandal and bankruptcy in late 2001, Enron had been named "America's most innovative company" six times in a row (McLean & Elkind, 2003, p. xxiv). Enron's CEO, Kenneth Lay, was regularly lionized in the business press. Although it would eventually be learned that the company's 1,000% return to investors was little more than the accounting fraud, only few firms were as much adored by Wall Street as Enron was in the late 1990s (Sridharan, Dickes, & Caines, 2002).

Lambasted in the press in 2003 – 2004 for spending $2 million of his company's money on a lavish birthday party for his wife, former Tyco CEO, Dennis Kozlowski, was once appreciatively dubbed "The Most Aggressive CEO" and talked about "as a second Jack Welch" (Kellerman, 2004, p. 45). Before he was fired in 2003 for leading a massive accounting fraud, HealthSouth's CEO and Chairman, Richard Scrushy, was hailed as an innovator who reinvented healthcare delivery and, like Kozlowski, was widely admired for his aggressiveness (Haddad, Weintraub, & Grow, 2003; Helyar, 2003).

Adelphia, Arthur Andersen, Enron, FINOVA Group, Global Crossing, HealthSouth, Tyco, WorldCom, and a number of other companies felled by corporate scandals over the past few years have in common the fact that they were all widely admired. In many cases, the business press and Wall Street hailed these companies as exemplars of corporate excellence and exalted their CEOs as visionary leaders (Callahan, 2004). Ironically, these examples of public figures following unethical business practices had previously been lauded as excellent corporate citizens and role models of ethical businessmen. For example, Enron's Code of Ethics, with its Vision and Values platform encompassing its RICE (Respect, Integrity, Communication, and Excellence) values statement, was often cited as a model corporate code of ethics (Barth, 2003; McLean & Elkind, 2003). Likewise, some of the same CEOs who later became infamous for their rapacious greed and willingness to loot their companies in order to line their own pockets had previously built up reputations as conscientious Christians and generous philanthropists. Such was the case with both WorldCom's Bernie Ebbers and Enron's Ken Lay.

Post-mortem analyses of the recent corporate ethical scandals have offered a number of theories about why these once highly regarded organizations went bad. Much of the research has pointed to the effect of an organization's culture in shaping and supporting the shared "norms, beliefs, attitudes, and values" that characterize the style or way of doing things in the organization (Luthans & Hodgetts, 1992, p. 205). An organization's culture, in turn, is shaped by the company's founder and maintained by the executives and managers who run the company. Organizational cultures are strengthened and preserved by the tendency of the management to hire people with similar values and beliefs (Hill & Jones, 1995). Consequently, the ethical failings of top leadership can often inadvertently be supported by, for example, an organizational culture that advocates winning at any cost (Carson, 2003; Jenkins, 2002; Jennings, 2004; Prentice, 2003; Seeger & Ullmer, 2003).

In focusing on leaders, researchers have considered not only the leaders' personal ethical failings, but also – and perhaps most critically – the impact of the leaders' behavior and leadership style on the organization. In particular, a number of analysts have suggested that the CEOs and other top leaders involved in corporate scandals may have created or fostered the development of an organizational culture and structure that was antithetical to ethical business behavior (Callahan, 2004; Carson, 2003; Jennings, 2004; Raghavan, Kranhold, & Barrionuevo, 2002; Sims & Brinkmann, 2003; Stanford, 2004; Stephenson, 2004).

PURPOSE AND SCOPE

Based on an analytical and comparative study of four recent corporate scandals involving organizations that had previously been recognized as both ethically and organizationally sound, this paper considers the contribution that leaders' behavior and organizational/leadership styles make to organizational culture and the extent to which the resulting organizational culture renders the organization and its members (including the top executives) prone to ethical misbehavior. The four companies selected for this case analysis are Enron Corporation, WorldCom, Inc., Tyco International, Ltd., and HealthSouth Corporation. First, each case is considered individually. The basic elements in the scandal are outlined and the principal aspects of each organization's corporate culture discussed, with special emphasis on the influence of leadership styles and leadership behavior/practices on organizational culture. The four cases are then compared and contrasted, in the light of the existing evidence on the relation between corporate culture and ethical misbehavior. The role of leadership style and behavior in the development of this culture is also discussed.

NOTE ON THE SELECTION OF CASES

Enron, WorldCom, Tyco, and HealthSouth were selected for analysis because of the availability of information on their organizational culture and of the specific details of the companies' ethical lapses. While there is now a large and growing literature on the Enron debacle and, to a much lesser extent, the meltdown at WorldCom, information on the scandal and the organizational culture evident at the corporation at the time of the scandal is much more difficult to obtain from them than it is to get from most other firms. Much information has been and is still being withheld pending the outcome of civil and criminal litigation related to four companies studied. Because of the availability of information and the applicability of the case to the scandals at the other firms, this analysis places a particular emphasis on the Enron scandal.

There were other reasons for the final selection besides the availability of information. Enron was selected because it was the first in a series of major corporate scandals, because of the extensive publicity of the case, and because Enron has become synonymous with corporate malfeasance. As the biggest accounting fraud in world history, it seemed necessary to select WorldCom for analysis. Tyco and HealthSouth were selected to expand and complement the analytical material available in the WorldCom and Enron cases. All four organizations are U.S.-based corporations with international operations. Three of the four firms represent distinct (and different) industries – energy (Enron), healthcare (HealthSouth), and telecommunications (WorldCom) – while the fourth, Tyco, is a conglomerate with interests in a range of industries from healthcare to plastics to fire to security. The scandals at all four firms involved questionable or fraudulent accounting practices as well as a range of unethical and/or illegal activities carried out by top managers and executives. In all four cases, the actions of unscrupulous executives hurt their companies and their stakeholders. Enron and WorldCom were driven to bankruptcy, while HealthSouth was de-listed from the New York Stock Exchange. The Tyco scandal caused a near-mortal wound to the conglomerate's reputation. HealthSouth was chosen for analysis because former CEO Richard Scrushy was the first CEO of a major company to be indicted on charges of knowingly filing false financial statements under the Sarbanes-Oxley Act, which was enacted in the wake of the Enron crisis (Abelson & Freudenheim, 2004). The Tyco case was chosen because of its difference from the other three cases. Enron, WorldCom, and HealthSouth were all founded in the 1980s and the recent corporate scandals at each company involved executives (Lay, Ebbers, Scrushy) who were part of the companies' founding. Tyco, on the other hand, was founded in the early 1960s and former CEO Dennis Kozlowski – the man at the center of the scandal – had led the company only since 1992 (Hoover's, 2004b).

CASE STUDY 1: ENRON CORPORATION

> *"We treat others as we would like to be treated ourselves. We do not tolerate abusive or disrespectful treatment. Ruthlessness, callousness and arrogance don't belong here."*
>
> – Enron Code of Ethics, July 2000; value of "respect"

> *"When you misrepresent the nature of the company, artificially inflate earnings, hide losses, when you do things like that to cause your stock price to rise, that is stealing. We stole."*
>
> – Andrew S. Fastow, testifying at the trial of former bosses Kenneth Lay and Jeffery Skilling (Washington Post, March 12, 2006)

> *"Skilling was known to himself and others as the smartest human being ever to walk the face of the earth. He never lost, and he never failed. He was arrogant and ultracompetitive."*
>
> – Brian Cruver, former senior manager at Enron (cited in Callahan, 2004, p. 128)

"You know what the difference is between the state of California and the Titanic? At least the lights were on when the Titanic went down."

> – Jeff Skilling, then Enron's CEO, amusing himself at a conference in June 2001 by telling a joke about the California energy crisis (cited in McLean & Elkind, 2003, p. 281)

"We create optionality. Enron is so much more valuable – hence our stock price – because we have so much more optionality embedded in our network than anyone else."

> – Andy Fastow, Enron's Chief Financial Officer, explaining Enron's business model to three *Fortune* magazine journalists in February of 2001 (McLean & Elkind, 2003, p. 323)

"Well, Dave, in the final analysis it doesn't matter what you crazy people in California do. I've got smart guys out there who can always figure out how to make money."

> – Ken Lay, Enron's CEO, in a late 2000 conversation with David Freeman, head of the Los Angeles Department of Water and Power. Lay had argued that price caps weren't necessary; Freeman maintained that they were (in McLean & Elkind, 2003, p. 281)

"The numbers, the earnings show that the company is just in excellent shape right now ... this is an entirely personal decision."

> – Jeff Skilling, August 13, 2001, reassuring investors following his abrupt resignation as CEO (in McLean & Elkind, 2003, p. 347)

"If anything, there seems to be even a little acceleration in the company's both financial performance and operational performance ...There are no accounting issues, no trading issues, no reserve issues, no previously unknown problem issues. I think I can honestly say that the company is probably in the strongest and best shape that it has probably ever been in."

> – Ken Lay, August 13, 2001, reassuring investors following Skilling's resignation and Lay's announcement that he would be returning as CEO (in McLean & Elkind, 2003, p. 347)

"I think we slipped a little bit on this recently, and we've got to restore it. Values are incredibly important to the fiber of this company."

> – Ken Lay, August 15, 2001, addressing Enron employees as the returning CEO and noting the one area where the company might need to make some minor changes (in

McLean & Elkind, 2003, p. 353)

"Has Enron become a risky place to work? Skilling's abrupt departure will raise suspicions of accounting improprieties and valuation issues ...I am incredibly nervous that we will implode in a wave of accounting scandals ..."

– Sharon Watkins, an internal auditor at Enron, in an August 14, 2001 letter to CEO Ken Lay (cited in McLean & Elkind, 2003, p. 355)

BACKGROUND

Unfolding in the shadow of the September 11, 2001 terrorist attacks, the collapse of Enron in 2001 – 2002 stunned the business community, outraged the public, and stupefied the politicians who had come to view Enron as representing the best of corporate America. Founded in 1985, Houston-based Enron Corporation was once the world's largest energy company. In April 2001, just eight months before the company declared bankruptcy, Enron was ranked number seven in market capitalization on *Fortune* magazine's list of the 500 largest corporations in the United States (Sridharan, Dickes, & Caines, 2002). From the perspective of Enron's top managers, seventh wasn't good enough. In January of 2001, Enron Chairman Kenneth Lay, CEO Jeff Skilling, and the other members of Enron's management committee met to fine-tune Enron's annual vision statement. They decided that the title of "World's Leading Energy Company" – no longer fully conveyed the grandeur of Enron. They decided that Enron should aim at becoming the "World's Leading Company" as defined by market capitalization (McLean & Elkind, 2003).

Enron enjoyed a long, favorable run among both Wall Street analysts and the business press, but in late 2000 and early 2001, analysts and investigative journalists who looked hard enough were beginning to see signs that all was not well at the would-be "world's leading company". A run-up in Enron's stock and the company's reliance on mark-to-market accounting led a few analysts to wonder if Enron was overvalued. Closer examination of Enron's financial statements only led to further questions. No answers were forthcoming.

When asked about Enron's accounting in early February 2001, one Bear Stearns analyst commented, "You don't have a clue, I don't have a clue, and I'm not sure they have a clue. Enron is a big black box" (McLean & Elkind, 2003, p. 321). Trouble in some of Enron's businesses, more questions about its accounting, concerns over insider sales (Lay, Skilling, and other executives were selling significant blocks of Enron stock), rising corporate debt, the general downturn in the stock market, and the fallout from the California energy crisis sent Enron's stock on a downward spiral in the first half of 2001. By June 2001, Enron's stock price had fallen to around $50 a share, down 45% from its August 2000 peak of $90. On August 13, 2001, Enron CEO Jeff Skilling, who had assumed this position, after long serving as Chief Operating Officer, only in January 2001, abruptly resigned for personal reasons and was replaced by the former CEO and company founder, Kenneth Lay. After Skilling's resignation, Enron's stock dropped to $38 a share and then continued its skid into the fall, first on rumors and later on evidence of massive malfeasance and possible fraud in some of Enron's SPEs or special purpose entities, particularly those under the direct control of CFO Andrew Fastow (Sridharan, Dickes, & Caines, 2002). On October 24, 2001, as Enron's stock hovered at around $19 a share, Enron CFO Andy Fastow was fired. About the same time, Arthur Andersen, Enron's auditing company, implemented a new document retention policy. Thousands of documents pertaining to Enron were shredded before the Securities and Exchange Commission notified Arthur Andersen of an investigation of Enron and demanded a cessation of all shredding (McLean & Elkind, 2003). On December 2, 2001, in the wake of a last-ditch and ultimately failed effort at a rescue merger with Dynegy Direct, Enron filed for the largest Chapter 11 bankruptcy in U.S. history (Sridharan, Dickes, & Caines, 2002). A little more than a year later, in January 2002, Kenneth Lay was finally forced to resign as Enron's chairman and CEO (McLean & Elkind, 2003).

The stunning scope of the Enron debacle gradually emerged in 2002 and 2003 as a result of Congressional hearings, journalistic investigations, courtroom testimony, and the statements of internal whistleblowers. At the Congressional hearings on Enron's collapse, all the top executives called to testify refused to answer key questions and, with the exception of Jeff Skilling, exercised their Fifth Amendment right against self-incrimination. Skilling testified without taking the Fifth but denied any direct culpability. In fact, he maintained that he was not aware that *anything* was wrong with the company. Fastow eventually pled guilty in exchange for a reduced sentence (Sanford, 2004). Lay's strategy has been to blame his subordinates – notably Fastow, Skilling, and Chief Accountant Richard Causey – for the problems, denying all the while that he had any personal knowledge of the accounting fraud (Behr, 2004; Ken Lay's lame excuse, 2004).

The information that has been made public since Enron filed for bankruptcy in December 2001 has revealed that most of Enron's supposed financial success over the previous several years was nothing more than a sham, courtesy of end-of-quarter accounting adjustments. The entire operation was rife with conflicts of interest. CFO Fastow appeared to have engineered a massive fraud for the purpose of enriching himself (Callahan, 2004; Jenkins, 2002; Raghavan, Kranhold, & Barrionuevo, 2002). All the top executives engaged in questionable practices of insider stock sales as the company's stock was tanking. Lay, for his part, took what one board member labeled the "ATM approach" – repeatedly drawing down a $4 million line of credit he had with his company, using it to pay off his own creditors, and then selling vast amounts of Enron stock to pay back the loans. McLean & Elkind (2003) reported that in the six months from November 2000 to June 2001, Lay was able to sell $52 million worth of Enron stock using this strategy.

It wasn't just the company loans, stock sales, and questionable accounting practices that characterized the Enron scandal. Even by U.S. corporate standards, Enron executives were paid lavishly, enjoying not only above-market salaries, but also freewheeling expense accounts and staggeringly large bonuses. The Enron parking lot was full of Porsches and Ferraris. While lavishly compensated, executives did not shy away from taking advantage of every opportunity to steal more from the company through phony partnerships and special purpose entities (Prentice, 2003; Raghavan, Kranhold, & Barrionuevo, 2002; Seeger, 2003). CEO and Chairman Lay, a self-described devout Christian, was particularly notorious for his love of the Enron-funded extravagant life. According to numerous reports, he used the Enron corporate jets as personal transportation not only for himself, but also for his family and friends. He managed to find jobs – and more often, whole companies – to occupy his family members, including his son (Behr, 2004b; Callahan, 2004; McLean & Elkind, 2003).

The scope of the Enron scandal was such that it seemed to demand an unprecedented response. The Justice Department filed hundreds of charges against Enron executives (finally indicting Lay in July 2004) for fraud and conspiracy. Meanwhile, shareholders and former employees filed civil lawsuits against the former energy giant. Although Enron and Lay, in particular, had long ties to the Bush Administration, they had "donated millions of dollars to Republicans and Democrats alike" (Enron and Andersen, n.d., n.p.), and "had enjoyed much closer ties with Clinton Administration regulators than was generally known" (Weisskopf, 2002, n.p.), a unified Congress and Administration were quick to refuse a bailout and to press for meaningful sanctions. The most significant government reaction to the scandal was the July 2002 passage of the Sarbanes-Oxley Act. This law requires companies to have a special code of ethics for financial officers, makes it a crime for corporate officers to lie about financial statements, and includes other legal impediments against corporate misconduct (Peppas, 2003).

The magnitude of the consequences of the Enron debacle is as dramatic as the scope of the scandal. As a direct result of the accounting fraud, over 20,000 Enron employees lost hundreds of millions of dollars in retirement and savings accounts (Behr, 2004b). During the Congressional hearings, many former Enron employees testified that they had retired with $700,000 to $2 million in Enron stock that had become worthless (Sridharan, Dickes, & Caines, 2002). While Enron executives were frantically dumping their Enron stock as the price started to tumble, the majority of Enron employees were prohibited from selling their stock (Sims & Brinkmann, 2003; Sridharan, Dickes, & Caines, 2002). The debacle put thousands of employees (both at Enron and in related companies such as Arthur Andersen) out of work. It is now known that the misconduct at Enron contributed materially to the California energy crisis. Seeger (2003) sums up some of the other costs and consequences of the unethical conduct at Enron:

> The Enron case cost investors billions of dollars in equity, dealt a fatal blow to the accounting giant Arthur Andersen, generated a dizzying array of lawsuits, and prompted serious rethinking of SEC regulations. Enron and the distrust in corporate governance it generated also helped fuel a sharp downturn in major stock markets. (p. 65)

The Enron case and the publicity surrounding it did much to undermine the public opinion of corporations in America. A Harris Interactive/Reputation Institute study of consumer attitudes towards U.S. corporations in the wake of the corporate scandals found that among consumers, Enron ranked 60th out of 60 companies identified on measures of consumer trust, the same dead-last position it has held since the survey began in 2002 (Alsop, 2004). Enron has become the quintessential symbol of unethical conduct. Former CEO Kenneth Lay, a mild mannered son of a Baptist minister with the physical appearance of Elmer Fudd, has become one of the most hated men in America (Alsop, 2004; Behr, 2004a, 2004b).

ENRON: A MODEL OF CORPORATE ETHICS AND SOCIAL RESPONSIBILITY?

The collapse of Enron and the ethical vacuum that seemed to have precipitated it was all the more jarring and unexpected because Enron had long projected the appearance of an ethical, socially responsible corporation. As Sims and Brinkmann (2003) observed, Enron "...had been heralded as a paragon of corporate responsibility and ethics – successful, driven, focused, philanthropic and environmentally responsible. Enron appeared to represent the best a 21st century organization had to offer, economically and ethically" (p. 243). In 1996, Enron's boast of a strong environmental record was validated when it received the Corporate Conscience Award from the Council of Economic Priorities (Seeger, 2003). Enron was known as a leader in corporate giving for charitable causes and disaster relief (Prentice, 2003; Seeger, 2003; Sridharan, Dickes, & Caines, 2002). Enron's various international ventures, especially those in developing countries, were typically dressed in the trappings of corporate social responsibility such as protection of the environment, cultural sensitivity, and socio-economic conscientiousness (McLean & Elkind, 2003; Seeger, 2003).

Ken Lay, Enron's founder and long-time CEO and Chairman, was widely known as Houston's leading philanthropist (Behr, 2004a, 2004b; Prentice, 2003; Seeger, 2003). Lay not only gave millions of his own (or Enron's) money to various charitable causes, he also developed, on the international level, his reputation as the "go-to guy" to help raise money for any charitable cause. In addition to his philanthropic activities, Lay conscientiously projected the image of a moral man and a moral leader. His mild Midwestern manner, his background as the son of a minister, his regular church attendance, and his repeated exhortations that he lived by a strict code of personal conduct based on Christian values were often sufficient to overwhelm even some of the more glaring moral contradictions in his personal life.

Ken Lay was also the enthusiastic promoter of Enron's formal code of ethics, first articulated as a statement of human rights principles in 1996 (Seeger, 2003). These principles included a statement of Enron's core values of respect, integrity, communication, and excellence. Known throughout the firm as RICE, these core values were summarized as (Seeger, 2003, p. 65):

> ***Respect:*** We treat others as we would like to be treated ourselves. We do not tolerate abusive or disrespectful treatment. Ruthlessness, callousness and arrogance don't belong here.
> ***Integrity:*** We work with customers and prospects openly, honestly and sincerely. When we say we will do something, we will do it; when we say we cannot or will not do something, then we won't do it.
> ***Communication:*** We have an obligation to communicate. Here, we take the time to talk with one another ... and to listen. We believe that information is meant to move and that information moves people.
> ***Excellence:*** We are satisfied with nothing less than the very best in everything we do. We will continue to raise the bar for everyone. The great fun here will be for all of us to discover just how good we can really be.

On July 1, 2000, Enron published a comprehensive code of ethics. The foreword, signed by Ken Lay, advises employees, "Enron's reputation finally depends on its people, on you and me. Let's keep that reputation high" (Barth, 2003, p. 120). The Code reprints the Principles of Human Rights, including Enron's Vision and Values statement that encompasses the RICE values and a vision statement ("Enron's vision is to become the world's leading energy company ..."). The Code outlines policies on securities trades by company personnel, confidential information and trade secrets, compliance with environment laws, compliance with anti-bribery laws, compliance with antitrust laws, policies on political contributions and government relations, policies on conflicts of interest and investments, and other matters including employee privacy. A section on "Business Ethics" opens with the following,

> Employees of Enron Corp., its subsidiaries, and its affiliated companies are charged with conducting their business affairs in accordance with the highest ethical standards. An employee shall not conduct himself or herself in a manner which directly or indirectly would be detrimental to the best interests of the Company or in a manner which would bring to the employee financial gain separately derived as a direct consequence of his or her employment ... Moral as well as legal obligations will be fulfilled openly, promptly, and in a manner which will reflect pride on the Company's name ... (Barth, 2003, p. 125)

ENRON'S ROTTEN CORE

An analysis of the events and behavior surrounding the Enron scandal forces the conclusion that Enron's vaunted code of ethics was observed, at least by executives, mainly in the breach (Prentice, 2003). The RICE values, as Seeger (2003) notes, "appeared to function largely as platitudes, discussed yet dismissed in favor of more pragmatic issues of profit" (p. 63). Enron provides a good illustration of "window dressing ethics, with talking instead of walking, ethics as rhetoric" (Sims & Brinkmann, 2003, p. 253). Enron's accounting problems and subsequent bankruptcy did not emerge out of the blue, nor was there any single identifiable moment when Enron crossed the line between what was ethically acceptable and what was not. Instead, the "Enron scandal grew out of a steady accumulation of habits and values and actions that began years before and finally spiraled out of control" (McLean & Elkind, 2003, p. 132). Sims and Brinkmann (2003) likewise agree, writing, "It was the sum of incremental ethical transgressions that produced the business catastrophe" (p. 247).

A number of analysts suggested that Enron's basic business model contributed to its ethical and financial collapse. The company's reliance on mark-to-market accounting may have fostered a basic disconnect with actual earnings and costs, while the focus on doing business through affiliated special purpose entities undoubtedly increased the range and scope of conflicts of interest (Callahan, 2004; Jennings, 2004; McLean & Elkind, 2003; Prentice, 2003; Seeger, 2003). Enron's leaders' belief in the power of free markets and the need for complete deregulation also influenced the character of Enron's business model and its ethical parameters. As Callahan (2004) noted, "Enron's leaders believed they were reinventing the corporation by creating a company that wouldn't actually make anything – except profits, because it took advantage of the ebb and flow of fast-changing markets in which everything under the sun was bought and sold" (p. 127). Sridharan, Dickes, & Caines, (2002) argued that Enron's business model played a significant role in its eventual demise:

> Enron transformed itself from an energy company to a risk management firm that traded everything from commodities to derivatives. Enron's

> consultants may have advised Enron to pursue a strategy of building a large firm with very few real assets on its balance sheet. The use of special purpose entities (SPEs) allowed Enron to operate extensive undercover and risky trading operations in a manner that did not properly reflect their debt on its balance sheets. The 'asset-light' strategy, the SPEs, and the off-balance-sheet financing they provided to Enron appear to be the root cause of Enron's eventual failure. (p. 14)

ENRON'S FLAWED ORGANIZATIONAL CULTURE

Edward Schein (1996) defined organizational culture as the "shaped norms, values and assumptions" of how organizations function (p. 229). According to him, Enron's organizational culture was a breeding ground for ethical misbehavior among its employees, particularly its top executives. An organization's leaders, especially its CEO and other top leaders, play a vital role in shaping the organization's culture (Argyris, 1973; Schein, 1996; Sims & Brinkmann, 2003). On the basis of Schein's work on organizational culture – in particular, his model of the five primary mechanisms (attention, reaction to crisis, role modeling, allocation of rewards, and criteria for selection and dismissal) that a leader can use to influence an organization's culture – Sims and Brinkman (2003) showed how Enron's organizational culture, as influenced by its leaders, led to the crisis. Specifically, they argued that Enron's executives used Schein's five mechanisms "to reinforce a culture that was morally flexible, opening the door to ethics degeneration, lying, cheating, and stealing" (Sims & Brinkman, 2003, p. 247).

Two executives at Enron were especially important in shaping the organization's culture. Ken Lay, both as one of the company's founders and in his role as CEO and Chairman, was a key influence on Enron's culture. The other executive who most shaped Enron's organizational culture was Jeff Skilling, who served briefly as CEO and for years as Chief Operating Officer (COO) and President. Lay made the belief in free markets and the power of deregulation a central value at Enron. He was also responsible for promoting the image of Enron as an ethical corporation. Lay's deeds frequently failed to meet up to the promise of his words, however. Of all Enron's executives, none were guiltier than Lay of treating Enron assets like personal property (e.g., he and his family members used corporate jets for personal transportation needs), and none took as much advantage of executive privileges related to stock sales and insider loans as he did (Behr, 2004a, 2004b; McLean & Elkind, 2003; Raghavan, Kranhold, & Barrionuevo, 2002). While many Enron executives accumulated ostentatious trappings of wealth (i.e., sports cars, big houses, other real estate holdings, etc.), Lay did so with a vengeance. McLean and Elkind (2003) note that Lay grew up dirt poor and his early poverty may have influenced his seemingly ravenous hunger for the finer things in life, including his requirement that his lunch be served on a silver platter.

Lay's personal actions often contradicted the values model he touted. More importantly, Lay's questionable ethics served as a role model to employees. Lay helped foster a sense of entitlement among the other executives and even among line employees. McLean and Elkind (2003) observed:

> The sense of entitlement, bankrolled with corporate cash, was shared by many at Enron, from Ken Lay to the secretarial staff, most of whom carried Enron-purchased cell phones. There was no requirement to use a particular vendor; if you didn't want to wait for something, you could just pick up the phone. (p. 119)

Further:

> The perks the company handed out, which were excessive even by the standards of an excessive era, also reinforced the feeling of heady success. There was the elaborate health club in the basement of the headquarters, the free computers provided at home for every Enron employee, the subsidized concierge service... (McLean & Elkind, 2003, p. 240)

Sims and Brinkmann (2003) noted, "Employees observe the behavior of leaders to find out what is valued in the organization" (p. 250). Lay spoke about the importance of values, but in fact he was a horrible role model for employees. He condoned the unethical behavior of other executives and refused to communicate honestly to investors and employees about the financial status of the company, even as he was busy selling off his own stock.

Lay's direct influence on Enron's organizational culture was limited by the extent of his direct involvement in managing and leading Enron. He is often described as being "disconnected from the day-to-day operations of the company" and *never* described as a hands-on leader (Behr, 2004a, 2004b; McLean & Elkind, 2003; Seeger, 2003). Leadership theory argues that leaders, in contrast to managers, are usually visionaries, who have the capacity to project a vision for their company's future (Bennis, 2004; Goleman, 2004; Maccoby, 2004). Lay was a visionary in some ways: he founded Enron, he had a concept of an energy company operating in a deregulated environment, and he spent a considerable amount of his time as CEO imagining a future for his company. However, he lacked a talented leader's capacity to translate that vision into a reality. He had the social skills to help smooth over differences but not to motivate followers. Indeed, according to most reports, Lay was often at the mercy of his followers, particularly those at the executive level, who found him to be easily manipulated (McLean & Elkind, 2003; Offermann, 2004). In addition, Lay did not fit the model of an effective manager. The day-to-day aspects of leading and managing were left to other executives.

Before Jeff Skilling joined Enron in 1990, day-to-day leadership was under the control of Rich Kinder. Originally serving as Enron's General Counsel, the abrasive Kinder was given the title of Chief of Staff in 1987 and later became COO in 1989 (McLean & Elkind, 2003). By all accounts, Kinder was an effective manager, albeit a manager with a reputation for meanness. He was less effective, however, as a leader and lacked the leader's capacity to be a visionary. Enron found its *de facto* hands-on leader in 1990 when Ken Lay persuaded former McKinsey consultant Jeff Skilling to join the firm. Skilling was the architect of Enron's business model. When Kinder left Enron in 1996, Skilling took his job as president and COO. Whereas Kinder was more a manager than a leader, Skilling a pure leader with few management skills, fit most of the characteristics of a narcissistic leader (Maccoby, 2004). He was known as being incredibly smart, ruthless, and arrogant. He had admirers at Enron but few real allies. Skilling brought in CFO Andy Fastow, who was later named as one of the main architects behind Enron's various accounting frauds. Fastow worshiped his mentor. He even named (to the ridicule of other Enron managers) his first-born son after Skilling and worked hard to emulate the values that Skilling espoused (Raghavan, Kranhold, & Barrionuevo, 2002).

Skilling, more than any other Enron executive, shaped the organization's ultimately toxic culture. According to McLean & Elkind (2003), Skilling cultivated a macho, risk-taking culture at Enron that Raghavan, Kranhold, and Barrionuevo (2002) called "cowboy culture". Callahan (2004) observed:

> Skilling sought to shape Enron into something akin to a pure state of nature where individuals could advance themselves – and the company stock – unencumbered by the typical restraints found in corporate civilization ... Vicious competition among employees was a natural outgrowth of the Skilling approach ... Skilling encouraged the dog-eat-dog culture, and it reflected his own survival-of-the-fittest mentality. (p. 129)

The epitome of this dog-eat-dog culture was the "rank and yank" system of annual employee performance reviews used at Enron. Pioneered at General Electric in the early 1990s, the rank and yank system was honed to new levels of cruelty and competitiveness at Enron. With input from rival employees in the same unit, managers rated all of their subordinates on a scale of 1 (best) to 5 (worst) every six months and then fired 15% of the employees at the bottom rankings (Callahan, 2004; Sims & Brinkmann, 2003). The performance review system fostered a "win-at-all-costs mentality, and a willingness to cross the ethical line" (Sims & Brinkmann, 2003, p. 250).

Like Milton Friedman (1979), Skilling believed with his whole heart that the social responsibility of business was to earn a profit. Contrary to contemporary motivation theories that stress the importance of intrinsic rewards, Skilling was a firm believer that *money* was the primary and most important motivator in the business world. These beliefs were clearly reflected in Enron's organizational culture. Potential bonuses were virtually unlimited for top performers. Strong performers quickly developed a strong sense of entitlement. In his analysis of unethical behavior at Enron, *Wall Street Journal* columnist Holman Jenkins (2002) observed that thieves can be divided into two categories: those who think that they can get away with stealing and those who don't believe that what they are doing is stealing. Jenkins (2002) opined, "Enron executives seem to have believed they weren't stealing" (p. A15).

Skilling created an organizational structure and operational system that was particularly suited to the macho, dog-eat-dog culture at Enron. As Seeger (2003) explained:

> Highly skilled and ambitious 'individual operators' worked in a decentralized structure with little or no oversight. The company encouraged experimentation and innovation but discouraged anything less than stunning success measured in profits. These operators were encouraged to be 'creative' in finding new opportunities for profits in a wide variety of markets ... these schemes were often very complex and defied conventional business and accounting wisdom ... (p. 65)

In interviews with the business press, Skilling asserted that Enron featured a highly decentralized organizational structure. This decentralized structure, argued Skilling, complemented what he termed – borrowing a phrase from *In Search of*

Excellence – a "loose-tight" culture that permitted loose management through tight internal control mechanisms (McLean & Elkind, 2003, p. 120). On the contrary, Stanford (2004) argued that Enron's ethical problems were partly a result of the company's *highly centralized* organizational structure. He suggested that some firms might appear to be less centralized than they actually are, even appearing to be completely decentralized. Ultimately, the degree of centralization is "contingent solely upon the actions of upper administration in making crucial organization-wide decisions" (Stanford, 2004, p. 18). He further argued that Enron, in fact, fit a pattern of a highly centralized organization:

> In extreme instances of high centralization, top executives may vie for power among themselves and seek to make decisions they believe will best support their individual interests. According to reports, including court testimony, Enron was an example of this type of situation. Former CFO Fastow made critical financial decisions that, at the time they were initiated, were supposedly unknown to members of the board or to Lay, then CEO. From these decisions, Fastow was able to greatly enrich himself ... (Stanford, 2004, p. 19)

Overall, Enron was a company that presented an image of itself that was almost completely contrary to its internal reality. Ken Lay successfully presented the ethical face of Enron even as he himself was contradicting the ethical principles he espoused. While Lay advertised Enron's values as those laid by the RICE model, Skilling transformed Enron into a company that adhered to values focused on success, profits, and personal financial gain. Seeger (2003) reported that while the company's Code of Ethics touted the RICE values, the employee parking garage at corporate headquarters touted the business values. Large signs on each level extolled a business virtue such as "bold, innovative, smart, ambitious, accomplished, undaunted, adventurous" (Seeger, 2003, p. 65). This duality – or hypocrisy – was also reflected in a Lucite paperweight cube on CFO Fastow's desk. The cube supposedly set forth Enron's RICE values of respect, integrity, communication, and excellence. However, on Fastow's cube, the values were given different definitions than those found in Enron's published code of ethics. For example, the cube's inscription explained the real meaning of the value of "communication": "When Enron says it's going to 'rip your face off' it will 'rip your face off'" (Raghavan, Kranhold, & Barrionuevo, 2002, p. A1).

CASE STUDY 2: WORLDCOM

> *"The only experience Bernie had before operating a long-distance company was he used the phone."*
>
> – Carl J. Aycock, an original LDDS investor and WorldCom board member, reflecting on Bernie Ebbers qualifications to lead a telecom giant (Romero & Schiesel, 2004, p. C1)

> *"Bernie was a paradox. He wore the clothes of a good old boy. And he kind of wanted to be one of the good old boys. But ... he was always somewhat confrontational, and in-your-face, compared to most of us in the Deep South ... and that created some problems ... Conversely, he could be extremely*

compassionate ... I've seen him in church ... just weep ... on the other hand, if he ... smelled competition, he became another person ... he'll cut your heart out."

– David Singleton, original LDDS investor and WorldCom board member, on Bernie Ebbers' mood swings (Jeter, 2003, p. 60)

"He has no peer in his ability to earn the trust and confidence of the investment community."

– WorldCom CEO Bernie Ebbers, praising Scott Sullivan in 1998 (Feder & Leonhardt, 2002, p. C1)

"Scott was well regarded as a straight shooter who had his arms around a lot of the details."

– Blake Bath, Lehman Brothers analyst, reflecting on Scott Sullivan, former WorldCom CFO, shortly after he was indicted on charges of securities fraud (Young & Perez, 2002, p. B1)

"We recognize that we, as a company, have let you down. I have let myself down ... [the attempt to acquire Sprint] ended up a mistake – and I am certainly accountable...people have a legitimate right to ask if I have a right to lead this company."

– Bernie Ebbers, CEO of WorldCom, speaking to investors in July 2000 after calling off WorldCom's proposed acquisition of rival Sprint (Jeter, 2003, p. 120)

"I'd always wanted to work for WorldCom and was finally hired in 2001. But the entire time I was there – all nine months – I stayed confused. I thought telecom was telecom, but it wasn't. That's why I returned to BellSouth. How would I describe work life at WorldCom? Kinda like Dilbert."

– A former WorldCom sales representative (Jeter, 2003, p. 151)

"I just want you to know that you aren't going to church with a crook. No one will find me to have knowingly committed fraud."

– Bernie Ebbers, CEO of WorldCom, addressing the congregants at his church in Brookhaven, Mississippi after WorldCom disclosed the fraud (Pulliam, Lafour, & Brown, 2004, p. A1)

"There are a zillion documents in this case and there ain't one smoking gun."

-- Reid H. Weingarten, defense attorney for former WorldCom CEO Bernie Ebbers, in his opening statement at Ebbers' trial on securities fraud charges (Washington Post, 2005, p. F3)

I knew it was wrong, and I know it was against the law, but I thought we were going to get through it in a short period of time."

-- Scott D. Sullivan, former CFO of WorldCom, testifying about why he had made accounting adjustments to improve the firm's bottom line (Washington Post, 2005, p. F3)

BACKGROUND

On July 21, 2002, while the Enron scandal was still unfolding and just a week before President Bush signed the Sarbanes-Oxley corporate reform bill into law, telecommunications giant WorldCom filed for bankruptcy, usurping Enron's title for the world's largest bankruptcy (Jeter, 2003); the ensuing corporate scandal soon to robbed Enron of that title. Investigations indicated that former WorldCom CEO Bernard "Bernie" J. Ebbers and his top managers, especially WorldCom CFO Scott Sullivan, had carried out a massive and systematic fraud, totaling more than $11 billion – the largest accounting fraud in corporate history (Blumenstein & Pulliam, 2003). As New York state comptroller, Alan G. Hevesi lead plaintiff in a lawsuit against former WorldCom directors, auditors, and Wall Street underwriters, quipped, "WorldCom is the granddaddy of the frauds" (Young, 2005, p. C3).

WorldCom was founded in 1983 (operations started in May 1984) in Clinton, Mississippi, as a discount long-distance service called LDDS (Long Distance Discount Services, Inc.) that aimed to take advantage of the impending AT&T breakup. One of the initial founders was Bernard J. Ebbers. A 6' 4" tall, self-described devout Christian from Edmonton, Alberta who grew up poor and relocated permanently in Mississippi. After attending and graduating from Mississippi College with a bachelor's degree in physical education, Ebbers worked for a while as a high school basketball coach and then owned and operated a small chain of motels (Jeter, 2003). A year after its founding, Ebbers took over as CEO of the by then heavily leveraged LDDS. Under Ebbers' direction, LDDS (Ebbers changed the name to WorldCom in 1995) began to grow and prosper. Among business analysts, the company "was known for its aggressive salesmanship, its ruthless cost-cutting and its passion for corporate takeovers" (Schiesel & Romero, 2002, p. C1).

Thanks mainly to an extremely aggressive acquisition strategy, by 1992 LDDS had grown into the fourth largest long-distance carrier in the nation, behind AT&T, MCI, and Sprint (Romero & Schiesel, 2004). The company was much admired on Wall Street and its charismatic CEO had become almost a corporate cult hero. In 1992, WorldCom acquired Advanced Telecommunications of Boca Raton, Florida, and with it came a young and brilliant accounting manager by the name of Scott Sullivan (Young & Perez, 2002). Although they reportedly were not personally close, Sullivan and Ebbers formed what many observers described as a symbiotic business relationship. Working together they accelerated the company's acquisition strategy (Callahan, 2004; Young & Perez, 2002). Their acquisition binge culminated in 1997 with the $37 billion takeover of MCI, a deal engineered by Scott Sullivan. The two companies began operating as WorldCom in 1998. WorldCom had a close relationship with investment banker Solomon Smith Barney, which handled the MCI acquisition. Ebbers also had a close personal and fruitful relationship with Solomon's lead telecom analyst, Jack Grubman, who was extremely bullish on WorldCom (Pullman, Solomon, & Mollenkamp, 2002).

WORLDCOM'S ROTTEN CORE

Ebbers built a personal fortune based on WorldCom's success. He used his stock holdings as collateral to get loans to purchase yachts, a shipyard and yacht builder, farms, a hockey team, and a 500,000-acre ranch in Canada. When WorldCom's stock price began to fall in 1999 – 2000, Ebbers convinced the Compensation Committee to give him loans ($50 million at a crack) to cover the margin calls on his loans so he wouldn't have to sell his stock. Eventually, he owed WorldCom more than $400 million (Pullman, Solomon, & Mollenkamp, 2002).

WorldCom's accounting problems came to light in the aftermath of an aborted effort to purchase Sprint in 2000. Subsequent investigations revealed that WorldCom's fraudulent understating of expenses and overstating of revenues was systematized in 1999, in a process that became known inside the company as "close the gap" (Blumenstein & Pulliam, 2003; Pulliam, Latour, & Brown, 2004). It was the news of WorldCom's personal loans to Ebbers that eventually forced his resignation on April 29, 2002 (Romero & Schiesel, 2004). Sullivan hung on for another month until he was fired and implicated as the chief architect of the accounting fraud (Young & Perz, 2002). WorldCom filed for bankruptcy protection on July 21, 2002. On August 28, 2002, Sullivan was indicted on securities fraud charges and charges of conspiracy to commit securities fraud. He maintained his innocence and vowed to fight the charges (Young & Perez, 2002).

As investigations continued, it became apparent that the fraud at WorldCom went deeper than just Sullivan and his immediate staff. Many people seemed to have been involved in systematically engineering the $11 billion fraud and investigators charged that "the company had a culture that lent itself to the fraud" (Blumenstein & Pulliam, 2003, p. A3). Ebbers denied any knowledge of the fraud. Because he did not use email, rarely engaged in written correspondence (except the occasional hand-written fax), and had banned any written records of substantive meetings, investigators did not have a paper trail to follow (Blumenstein & Pulliam, 2003). However, in the spring of 2003, investigators uncovered a memo that Ebbers had written to Ron Baumont, WorldCom's COO, on July 10, 2001 that strongly suggested that Ebbers had knowledge of the close the gap process at WorldCom (Blumenstein & Pulliam, 2003).

Still, there was not sufficient evidence to pursue a separate case against Ebbers until the spring of 2004 when Scott Sullivan reversed his stand and agreed to testify against his former boss. Facing a maximum of 165 years in prison under the indictment filed against him in August 2002, Sullivan decided to plead guilty and testify against Ebbers in exchange for a reduction in sentence to a term of 25 years (Pulliam, Latour, & Brown, 2004). On March 2, 2004, Ebbers was charged with securities fraud, conspiracy to commit securities fraud, and making false filings to regulators (Pulliam, Latour, & Brown).

WORLDCOM: A LEADER IN SOCIAL RESPONSIBILITY AND VALUES?

Like Enron, WorldCom before its fall had a reputation of a socially responsible company. As Jennings (2004) observed, "WorldCom and Bernie Ebbers were revered for their generosity to colleges and charities in Mississippi and visible presence in the community" (p. 14). In fact, WorldCom was so highly regarded in its home state that, even as the stock was collapsing and it was apparent to nearly everyone that the company was about to collapse, the locals who owned WorldCom stock held onto it (Blumenstein & Pulliam, 2003; Jeter, 2003). Just as Ken Lay's devout Christianity added to the impression of Enron as an ethically run company, Bernie Ebbers' devout Christianity (which he highlighted by starting board meetings with prayers and by attending church and bible classes with the locals in Brookhaven, Mississippi) was arguably critical to securing WorldCom's reputation in Mississippi (Jeter, 2003). Also, like Ken Lay, Ebbers was a well-known philanthropist, especially in Mississippi, where he donated millions to colleges, community centers, and churches. His right-hand man Sullivan was also highly respected and widely viewed as an ethical leader. Like Ebbers, Sullivan was also involved in various philanthropic causes.

WORLDCOM'S FLAWED ORGANIZATIONAL CULTURE

Investigators into the WorldCom accounting fraud charged that WorldCom's organizational culture made it easier to commit fraud. As at Enron, WorldCom's culture was shaped by its top executives – in this case Ebbers and Sullivan. Ebbers had the qualities of a highly effective leader, while Sullivan had those of an effective manager (Bennis, 2004; Goleman, 2004; Maccoby, 2004). While Ebbers was clearly the man in charge at WorldCom, CFO Scott Sullivan also helped set the tone. Sullivan was a workaholic who routinely put in 20-hour days and expected his staff to work equally hard (Jeter, 2003). Unlike Ebbers, Sullivan was reliably even-tempered and known for taking care of his staff (Callahan, 2004; Jeter, 2003). Whereas Enron's Chairman and founder Ken Lay was reportedly disengaged from the day-to-day operations at his firm, Bernie Ebbers kept a close watch on everything that went on at WorldCom. He managed to inspire both fear and loyalty in his employees. Many people worked extraordinarily long hours for relatively little pay, especially in the early days of WorldCom (Jeter, 2003). It was not uncommon for paychecks to be delivered late, except for the sales staff who were always paid on time, and paid relatively generously. However, employees, especially in the early days, didn't seem to mind the long hours and modest pay all that much. According to one former manager, "Bernie made us all feel that we would definitely be compensated one day. No one even thought about abusing sick days" (Jeter, 2003, p. 41). Although internal auditors eventually blew the whistle on WorldCom's accounting fraud, for years internal auditors and other management-level employees took enormous personal risks with little guarantee of significant personal gain (Blumenstein & Pulliam, 2003). Although top executives were paid handsomely, there was no culture of extravagance at WorldCom. Wages were modest, bonuses were non-existent, and perks were limited to simple privileges like free coffee in the office and discounts on phone cards (versus free computers at Enron). Even these modest privileges were cut when WorldCom's stock began to tank (Jeter, 2003). Ebbers did not win the obedience and loyalty of employees through charm alone. As one former WorldCom top manager told Jeter (2003), "Bernie was a John Wayne type character. He always seemed to be the nice guy, but people were scared and intimidated by him" (p. 61). Investigations into the WorldCom fraud uncovered a culture of fear at WorldCom. Employees were under intense pressure to follow management orders, with many reporting that they feared that they would lose their jobs, a reasonable fear since they had seen others lose their jobs if they didn't follow orders (Blumenstein & Pulliam, 2003; Jeter, 2003).

Ebbers used a combination of intimidation and charm to control WorldCom's board. Jennings (2004) noted that the business press referred to the WorldCom board as Bernie's board "because there were so few outsiders and those who were outsiders were personally and financially obligated to Ebbers" (p. 15). Ebbers started each board meeting with a prayer, "a tradition that especially endeared older Mississippians, many of whom had invested their life savings in WorldCom stock ... they didn't realize that Ebbers was known to stay up drinking half the night with colleagues" (Jeter, 2003, p. 91). Investigations of the fraud at WorldCom revealed that Ebbers often kept the board in the dark about some of the acquisitions. One report found that "several multibillion dollar acquisitions were approved by the board of directors following discussions that lasted for 30 minutes or less and without the directors receiving a single piece of paper regarding the terms or implications of the transactions" (Blumenstein & Pulliam, 2003, p. A3). Ebbers also quickly dissuaded the board from considering an offer made by Verizon to purchase the troubled WorldCom in November 2001 when WorldCom's stock was trading at $15 per share. Verizon was offering $21 per share; Ebbers wanted to hold out for nothing less than $30 per share (Blumenstein & Pulliam, 2003).

Ebbers was reportedly especially mercurial with his top managers. As was the case with board meetings, staff meetings started with a prayer. The next item on the agenda was usually the stock price, or rather, how to boost the price of the stock. The *Wall Street Journal* reported that "at a 1998 meeting, when WorldCom shares were hovering around $65, Mr. Ebbers told about 20 senior WorldCom and MCI managers that they had to figure out a way to push the stock up to $100 a share" (Pullman, Solomon, & Mollenkamp, 2002, p. A1). Ebbers had a firm rule prohibiting his executives from selling their WorldCom stock. Those who defied this order often found themselves summarily escorted out the door (Jeter, 2003; Pullman, Solomon, & Mollenkamp, 2002).

CASE STUDY 3: TYCO INTERNATIONAL LTD.

> *"The culture is very tough but very businesslike. A few of these guys are ex-military men. And Kozlowski, whose father was a cop or a fireman, personifies that. I think it's important to distinguish between the stock price and sales and profits. Last year, Tyco had almost $37 million in revenues, and so this is not some kind of scam. This is not Enron. There is no comparison to Enron except for the fact that both companies are on the front page of the business section."*
>
> – Harvard Business School Professor Robert Kennedy, responding to questions about rumors of an accounting scandal at Tyco in May of 2002 (Sweeney, 2002, p. 20)

> *"...an honest man, who understands numbers and is not going to cheat."*
>
> – Robert A.G. Monks, a former Tyco board member and Chairman of Ram Trust Services, describing Dennis Kozlowski, Tyco's CEO in the spring of 2002 (Sweeney, 2002, p. 20)

"Mark knows the numbers in a way that makes you comfortable; he isn't flashy, he comes across as a straight shooter. Mark has always been a bit more polished than Dennis, who is rough around the edges."

– John Waterman, chief investment officer at Rittenhouse Financial Services, characterizing Mark Swartz, Tyco's CFO in the spring of 2002 (Hechinger & Zuckerman, 2002, p. A6)

"We discussed Sardinia, but only as comic relief. The jury focus wasn't on how they spent their money, but on how they got the money they spent."

– Mr. Donovan, a management consultant and a juror on the Kozlowski/Swartz trial, discussing how most of the jurors were ready to convict (Maremont, Scannell, & Forelle, 2004, p. A1)

"I choose managers from the same model as myself. Smart, poor, and wants to be rich."

– Dennis Kozlowski, Tyco CEO, explaining to *Business Week* how he chooses managers (Jennings, 2004, p. 15)

BACKGROUND

In September 2002, former Tyco CEO Dennis Kozlowski and former Tyco CFO Mark Swartz were indicted on criminal charges (24 counts each) including grand larceny, securities fraud, and enterprise corruption charges (Maremont, Scannell, & Forelle, 2004). The former Tyco executives were accused of stealing $170 million in unauthorized compensation and pilfering an additional $430 million by illegally selling stock while misleading shareholders (Maremont & DeBaise, 2004). Both men pleaded not guilty. Kozlowski also faced charges of tax evasion in New York where he was accused of evading sales tax on purchases of artwork. During the course of an internal investigation led by superstar attorney David Boies, the lawyer who argued Al Gore's case before the U.S. Supreme Court in the disputed 2000 Presidential election, and during a subsequent trial in the New York Supreme Court, the sordid details of the Tyco scandal unfolded. Most attention focused on Kozlowski's extravagant and many argued, poor, tastes. Kozlowski used stolen Tyco money to purchase a range of items including a $6,000 shower curtain, a $38,000 backgammon table, a $4,995 bed skirt, a $103,000 mirror, a $500,000 hand-painted bird mural, and a $2.1 million birthday party in Sardinia thrown by Kozlowski for his wife (Maremont, 2003, 2004). Kozlowski and Swartz's trial opened in September 2003 in New York's state Supreme Court. Six months into the trial, the judge threw out the enterprise corruption charges against the two, but kept the larceny and securities fraud charges. On April 2, 2004, the judge declared a mistrial in the case, citing intense outside pressure on Juror No. 4, who, as she entered the courtroom on March 26, had reportedly flashed an OK sign to the defense (Maremont, Scannell, & Forelle, 2004). Subsequent interviews with jurors indicated that Kozlowski and Swartz would likely have been convicted on all counts.

In 1992, Kozlowski became CEO of Tyco, a company founded in 1960. Swartz, at the age of 30, became Tyco's CEO the same year. Under the Kozlowski – Swartz team, Tyco grew from a $3 billion company focused mainly on fire safety to a $37 billion conglomerate with businesses ranging from fire extinguishers to health products (Maremont, Scannell, & Forelle, 2004). Like WorldCom, the main vehicle of Tyco's growth was acquisitions – some 200 of them during the ten years that Kozlowski served as CEO – a feat that earned Kozlowski the nickname of "deal a month Dennis" (Management Mayhem, 2003, p. 5). Like Bernie Ebbers of WorldCom, Kozlowski was much admired on Wall Street and in the business press. Writing in early June 2002, just before Kozlowski resigned in disgrace, Sweeney (2002) observed,

> As recently as six months ago, L. Dennis Kozlowski, the company's hard-charging CEO, was still inviting favorable comparisons to Jack Welch, the former General Electric Co. CEO and business icon. Despite Tyco's involvement in the unglamourous – and often unrelated – businesses of cranking out fire hydrants, sprinkler heads, medical syringes and burglar alarm systems, Kozlowski was emerging as a business celebrity. There was the coveted cover story in *Business Week* last year, for example, billing him as Corporate America's "most aggressive CEO". Kozlowski's Midas touch was even the subject of a laudatory case study by the Harvard Business School, which asked, "What was so special about Tyco?" (p. 22)

In the wake of the Tyco scandal, *Strategic Direction* opined, "Now disgraced, instead of Jack Welch he can only draw unfavorable comparison with Enron's Kenneth Lay" (Management Mayhem, 2003, p. 5). While not nearly as flamboyant as his boss, Kozlowski, Tyco CFO Mark Swartz was every bit as much admired. Like WorldCom's Scott Sullivan, Swartz was admired not only for his bean-counting skills but also for his brilliance as a mergers expert (Hechinger & Zuckerman, 2002).

The Tyco case is clearly different from the other cases considered here in a number of respects. First, the scope of the scandal was smaller and seemed more confined to key executives (Kozlowski and Swartz). Although Tyco was faulted for its aggressive accounting tactics, the fraud in which Kozlowski and Swartz allegedly engaged focused more narrowly on their personal interests. The Tyco case also differs from the other cases in that this scandal did not involve company founders and the damage done to the company overall was arguably less devastating than in the case of Enron, WorldCom, or HealthSouth (Pillmore, 2003). Tyco did not have to declare bankruptcy and many of its business units were unaffected by the scandal.

However, there are important parallels between the Tyco case and the other cases that must be noted. As in the WorldCom case, Tyco executives, Kozlowski and others, maintained close and ethically questionable relationships with security analysts. Specifically, SEC regulators have accused Phua Young, a former Merrill Lynch analyst, of showing bias in favor of Tyco in his research reports. Perhaps in return for these favors or in anticipation of future favors, Kozlowski provided Young with free investigative services, valued at $20,000, to check out his fiancée. Kozlowski and Young also exchanged expensive cases of wine valued at more than $5,000 (Maremont & Bray, 2004). The sheer greed and extravagance of the Tyco executives is a clear reminder of the Enron executives. Kozlowski's brusque manner and his relentless focus on acquisitions remind one of Ebbers and WorldCom. Another factor linking the Enron, Tyco, and WorldCom scandals concerns the young age of the respective CFOs – Scott Sullivan (WorldCom), Andrew Fastow (Enron), and Mark Swartz (Tyco). In each case, the young finance wizards were paired with an older CEO. Jennings (2004) argued that this situation invites unethical behavior:

> Discernment, experience and priorities are different before and after age 40 ... These young executives, promoted rapidly despite their lack of experience, are often used by CEOs who are a full generation older because they are vulnerable and overly willing to earn the acceptance of their charismatic and powerful leader ... (Jennings, 2004, p. 16)

TYCO'S FLAWED ORGANIZATIONAL CULTURE

To what extent did Tyco's corporate culture contribute to the scandal? At first blush, it might seem that the Tyco scandal is confined to just a couple of bad executive apples, notably Kozlowski and Swartz. However, it can be argued that the fact that Kozlowski and Swartz were able to get away with their misdeeds indicates a corrupt culture, at least at the executive level. Verschoor (2003) argued that:

> Extensive corporate funds were used for the personal benefit of its CEO. Tyco also announced that a five-month internal investigation had uncovered a corporate culture that openly encouraged managers to push the rules of accounting to mislead investors about the company's results. This benefited the senior level to the long-run detriment of shareholders. A memorandum to employees at one division directed them to find cost savings by 'financial engineering'. At another unit, employees were told to 'create stories' to justify an accounting change that would improve Tyco's earnings. (p. 19)

Tyco's executive compensation and reward system also shows evidence of a corrupt culture, or at least an executive culture that fostered a strong sense of executive entitlement. For example, consider the extraordinary golden parachute deal that Mark Swartz enjoyed. Tyco's directors had considered the CFO so valuable that in 2001 they offered Swartz a retention agreement that would provide him with a windfall if they terminated him for any reason other than a felony. Under the terms of the contract, Swartz would receive a $63 million severance payment plus a payment of $8.5 million in previously restricted stock, *plus* $1.75 million annually for three years in a consulting contract for which he must work 30 days a year (Hechinger & Zuckerman, 2002). The Tyco directors reportedly signed a similar deal with Kozlowski in 2001. He was to get a $135 million severance payment in addition to a lifetime consulting contract for $3.4 million annually, extending his contract to 2008 and stipulating that he could only be fired if he was charged with a felony (Management Mayhem, 2003). Fortunately, for Tyco, it didn't need to pay up: Kozlowski resigned, thereby voiding the contract, and Swartz was fired in relation to the felony charges.

The efforts taken by the new Tyco management team under CEO Ed Breen in the aftermath of the scandal suggest that Tyco management believed that the company might be laboring under a corrupt culture. Breen replaced the entire top management team. Most of the board was also replaced. An office of corporate governance was established and a comprehensive *Guide to Ethical Conduct* for employees was developed and distributed to Tyco's 260,000 employees (Pillmore, 2003). Tyco restructured and separated finance from operations. In a step directly relevant to the Kozlowski/Swartz scandal, Tyco revamped its compensation structure, placing a cap on severance payments, bonuses, and stock option equity awards (Pillmore, 2003). Much to the consternation of line employees who felt that they were being punished by the crimes committed by executives, Tyco also mandated ethics training for all employees (Reigber, 2003).

CASE STUDY 4: HEALTHSOUTH CORPORATION

> *"I've been so mistreated, so lied to, it's just massive."*
>
> – Deposed HealthSouth CEO Richard Scrushy, in a phone call with *Fortune* magazine (Helyar, 2003, p. 76)

> *"We just need to get those numbers where we want them to be. You're my guy. You've got the technology and the know-how."*
>
> – HealthSouth CEO Richard Scrushy, encouraging his CFO William T. Owens (who was wearing a wire at the time) (Freudenheim, 2003, p. C2)

> *"I am innocent of the accusations against me and have been blessed by the Lord in having the resources to confront my accusers."*
>
> – Former HealthSouth CEO Richard Scrushy, in a statement made through a spokesman to *Business Week* magazine (Grow, 2004, p. 86)

> *"The trial will be a fascinating soap opera."*
>
> -- John C. Coffee Jr., a Columbia University professor who specializes in securities law, offering his prediction about the upcoming Scrushy trial (Abelson & Freudenheim, 2004, p. C1)

> *"You're not going to find on single memo, document, note, e-mail – nothing – with Richard Scrushy's fingerprint on it."*
>
> -- James W. Parkman III, defense attorney for former HealthSouth CEO Richard Scrushy, in his opening statement at Scrushy's trial on 58 criminal charges including conspiracy, perjury, obstruction of justice, and money laundering (The Washington Post, 2005, p. F3)

> *"Could I get this past the auditors?"*
>
> -- William T. Owens, former CFO of HealthSouth, quoting his ex-boss, Richard Scrushy, during Scrushy's securities fraud trial (The Washington Post, 2005, p. F3)

BACKGROUND

HealthSouth Corporation, a national chain of rehabilitation hospitals based in Birmingham, Alabama, was formed in 1984 by respiratory therapist Richard Scrushy and a few of his friends. He took the company public in 1986, and through an aggressive acquisition strategy, soon built HealthSouth into the nation's largest for-profit chain of rehabilitation hospitals (Hoover's, 2004). For the next ten years, HealthSouth posted double-digit profit growth each year, mainly based on Medicare revenues (Haddad, Weintraub, & Grow, 2003). In late 1997, Scrushy sold four million of his HealthSouth shares at $27 each, raising $108 million. A month later, the company cut its earnings forecast, citing a change in Medicare payment rules. A similar chain of events occurred in early 2002. A few months later in September, HealthSouth became the subject of an SEC investigation. The SEC was examining the possibility that HealthSouth had been fraudulently overstating earnings to boost artificially its stock price. It was also looking into charges that Scrushy had engaged in insider trading (Grow, 2004). Initially, charges were filed against HealthSouth's financial officers, but based on information gathered from them, the SEC focused on Scrushy. On March 19, 2003, Weston L. Smith, former CFO for HealthSouth, pled guilty to fraud charges. That same day, the SEC accused CEO Scrushy of a $1.4 billion accounting fraud. A week later, then current CFO William T. Owens pled guilty to fraud. On March 31, 2003, HealthSouth's board voted unanimously to fire Scrushy from his positions as Chairman and CEO (Abelson & Freudenheim, 2003a).

Scrushy was eventually indicted on 58 counts of conspiracy, fraud, perjury, obstruction of justice, and money laundering. Prosecutors claim that Scrushy illegally enriched himself through the systematic filing of false financial reports (Reeves, 2005) as part of a scheme to boost the company's stock by inflating HealthSouth's financial results by $2.6 billion between 1996 and 2002 (Abelson & Freudheim, 2004).

Additionally, Scrushy was charged with "false certification of corporate finances" in the first test of the Sarbanes-Oxley Act (Jury selection begins in trial of former HealthSouth Chief, 2005, p. C5). Sixteen other HealthSouth officials, including eight former CFOs, have all pled guilty to fraud (Abelson & Freudenheim, 2004).

HEALTHSOUTH'S FLAWED ORGANIZATIONAL CULTURE

Scrushy fomented a culture of fear and loathing at HealthSouth. Before the meltdown at HealthSouth, Scrushy was often described as a charismatic leader. Analysis of his leadership style in the work setting suggests that his charisma was more of a diabolical variety. According to *New York Times* analysts:

> Interviews with associates of Mr. Scrushy, government officials and former employees, as well as a review of the litigation history of HealthSouth, paint a picture of an executive who ruled by top down fear, threatened critics with reprisals and paid his loyal subordinates well. (Abelson & Freudenheim, 2003b, p. 3)

On Monday mornings, Scrushy conducted staff meetings, which his employees came to call "Monday morning beatings" because the main purpose of the meeting was for Scrushy to call attention to some failure and then publicly berate the person(s) he deemed to be responsible for the failure (Abelson & Freudenhim, 2003b, p. 3). In his profile of "The Insatiable King Richard", *Fortune* magazine writer John Helyar (2003) paints a similar portrait of the Monday morning meetings:

> At HealthSouth's Monday management meetings, discussion wasn't part of the drill. Officers made two-minute, numbers-packed reports, then braced for Scrushy's decrees and judgments. They might not get that far if he interrupted with his dreaded catch phrase, 'That was the stupidest thing I ever heard'. (p. 78)

By all indications, Scrushy cultivated a talent of ruling through intimidation. Abelson & Freudenheim (2003b) wrote that Scrushy prided himself "on calling any manager who was not performing," quoting him as often saying, "Shine a light on someone – it's funny how numbers improve" (p. 3). Scrushy did not appreciate hearing contrary opinions. Haddad, Weintraub, and Grow (2003) reported that he "publicly berated financial analysts who dared to challenge his forecasts of continued growth" (p. 70).

While focused on the numbers, Scrushy did not ignore any aspect of HealthSouth's operation; he was the antithesis of the Ken Lay's disengaged style of management. Scrushy was reportedly obsessed with dirt and dust. Helyar (2003) reported that, "Every HealthSouth facility was subject to a 'pristine audit', a white-glove test conducted by Ernst & Young staffers with 50-point checklists. They may have missed billions in financial fraud, but they were great at finding dust bunnies" (p. 79). Scrushy also carried out these inspections on his own:

> Scrushy would pop up unannounced at his rehab centers for surprise inspects. Like a drill sergeant, he would run a finger along the tops of a picture frame, then wipe it on the blazer of the center's administrator. Any visible mark meant points deducted – and possible dismissal. (Haddad, Weintraub, & Grow, 2003, p. 70)

Almost single-handedly, Scrushy shaped HealthSouth's culture, hammering into shape a group of pliant, cowering employees. Kimberly Landry, a former HealthSouth employee who was sued for defamation by the corporation after she criticized its management on a Website, said that working at HealthSouth "was like being in a cult" (Abelson & Freudenheim, 2003a, p. 3). Other employees likened the corporate officers "as a species of Stepford Wives – excessively obedient and eager to please" (Abelson & Freudenheim, 2003a, p. 3). Scrushy did not limit his imperial management style to HealthSouth's sales and administrative employees. In 2000, when revenues were down, he decided it was time to lower the boom on doctors working in HealthSouth's hospitals. He decreed that every doctor would henceforth report at 8 a.m. sharp on Monday to see patients, that surgeries would begin on Tuesdays, followed by rehab on Wednesday, and patient discharge as soon as possible thereafter (Haddad, Weintraub, & Grow, 2003).

Scrushy had no tolerance for criticism or contrary opinions and was exquisitely sensitive to any hint of a personal slight. At the same time, he demanded constant approval and adulation from those around him. Helyar (2003) commented, "Scrushy needed applause the way he needed oxygen" (p. 79). Scrushy ordered employees to attend free concerts performed by his rock band, with the clear implication that applause was mandatory. His main motivation for donating large sums of money to Alabama schools and community centers seemed to be to get his name (not his company's) on local signs and to gain personal recognition from the local community (Haddad, Weintraub, & Grow, 2003). Scrushy even built a small museum as a tribute to himself. Located on the back of HealthSouth's headquarters campus in Birmingham, the museum exhibits depict "the story of how, as a former respiratory therapist, he started the company with $1 million in seed capital and turned it into a wildly successful $4 billion hospital empire" (Haddad, Weintraub, & Grow, 2003, p. 70). Scrushy liked to hang out with celebrities, even if he had to hire them to do so. He hired athletes Bo Jackson and Troy Aiken as well as TV actor Jason Henry. Scrushy continued to seek attention and applause even as he fought the charges against him. He launched his own Website defending himself and funded his own TV talk show in Birmingham (Grow, 2004). Like Enron's executives and Tyco's Kozlowski, Scrushy enjoyed the trappings of wealth. His personal net worth reached $300 million in the late 1990s (Haddad, Weintraub, & Grow, 2003). He owned four mansions, a $135,000 bulletproof BMW, a $7.5 million Sikorsky helicopter, a fleet of 11 corporate jets, and ten boats, including the 92-foot yacht, *Chez Soiree*, from which he liked to conduct business (Haddad, Weintraub, & Grow, 2003; Helyar, 2003).

As CEO of HealthSouth, Scrushy fit to a tee the prototype of the narcissistic leader. Indeed, Scrushy embodied both the best and the worst of the narcissistic leader as outlined by Maccoby (2004):

> Productive narcissists are not only risk takers willing to get the job done but also charmers who can convert the masses with their rhetoric. The danger is that narcissism can turn unproductive when, lacking restraining anchors and self-knowledge, narcissists become unrealistic dreamers. They nurture grand schemes and harbor the illusion that only circumstances or enemies block their success. This tendency toward grandiosity and distrust is their Achilles' heel. Because of it, even brilliant narcissists can come under suspicion for self-involvement, unpredictability, and – in extreme cases – paranoia. (p. 94)

Fortune magazine writer John Helyar (2003) went so far as to charge that Scrushy met the diagnostic criteria for "narcissistic personality disorder . . . a pattern of grandiosity, a need for admiration, and lack of empathy" (p. 76).

SUMMARY AND CONCLUSION

> *"Power tends to corrupt; absolute power corrupts absolutely."*
> – Lord Acton

> *"It's not hard to make decisions when you know what your values are."*
> – Roy Disney

The four cases of executive extravagance and corporate fraud portrayed in this analysis are all examples of organizational cultures that harbored and masked an underlying ethical vacuum that ultimately steered these organizations into bankruptcy, tarnishing the reputations of their top-level executives in the public eye, and substantially hindering the continued viability of each corporation. Because an organization's culture provides the "behavioral norms for getting things done" (Holt, 1987, p. 262), often employees confronted with behavior they know to be wrong will ignore or rationalize it.

Only Enron bothered with the façade of a formal code of ethics. In that case, the formal code was nothing more than hypocritical window dressing, constructed for the purpose of polishing Enron's external image and feeding its CEO, Kenneth Lay's, delusions about his own morality. While they pursued their objectives in different ways, the senior executives of the four companies operated under the assumption that the end justified the means – and the end was to amass as much personal wealth as possible. This scramble for wealth caused all four companies to appear to operate under the assumption that Friedman (1979) was right: that the only social responsibility of business is to make profits. In the case of Enron, WorldCom, and HealthSouth, these three organizations operated under the assumption that corporations filled their social responsibility so long as they provided the *appearance* of profits. In the case of Tyco, Kozlowski and Swartz were evidently not all that concerned about even preserving the *appearance* of profits so long as they covered their own interests. In all four cases, the executives involved in the scandals operated within what Mintzberg, Simon, and Basu (2002) termed an "ideology of selfishness," because their primary interest was in self-enrichment and self-aggrandizement. In their own ways, Richard Scrushy, Bernie Ebbers, Scott Sullivan, Dennis Kozlowski, Mark Swartz, Kenneth Lay, and the other executives provided proof for Jeff Skilling's assertion that, above all else, it is money that matters.

TOXIC ORGANIZATIONAL CULTURES BREED UNETHICAL BEHAVIOR

Although Friedman (1979) argued that the real and only social responsibility of business organizations was to increase profits and thereby serve their communities by providing employment, income, etc., he was not suggesting that ethics has no place in organizational culture. What he really seemed to be saying was that corporate responsibility and organizational ethics must be vested in the people, such as the leaders and employees within the organization. The also seems to be one of the clearest messages in the four cases analyzed in this paper.

Several other studies available in the literature (e.g., Rossow & van Vuuren, 2003; Sims & Brinkmann, 2003; and Stephenson, 2004) also point to the critical role people within the organization play in determining the organization's culture. This analysis also supports the argument advanced by Sims and Brinkmann (2003) that an organization's culture may encourage or allow unethical behaviors. Hill and Jones (1995) argued that the norms and values of the organization become part of the employees' own value system: "Control through culture is so powerful because, once these values are internalized, they become a part of the individual's values, and the individual follows organizational values without thinking about them" (p.365). Nevertheless, not all employees who work in a toxic environment will commit or condone unethical acts because not all employees in a toxic environment will stay in the organization long enough for the culture to erode their own value system.

The present analysis revealed a number of similarities between the four cases studied. In each case, the leaders of the organizations created pressure to maintain financial performance, sometimes at any cost. In each case, there was little in the way of external supervision from board members, regulators, or others of the behaviors of executives. Another commonality of all four firms, as noted by Jennings (2004), was the pairing of a young, relatively inexperienced CFO with an older CEO. With the exception of Tyco, another commonality was the facade of social responsibility and ethical behavior as evidenced through charitable contributions, philanthropic activities, and, in the case of Enron and WorldCom, Christian values. The primary difference among these cases is that Enron, WorldCom, and HealthSouth all involved entrepreneurial leaders and founders, while Tyco stood apart as a case involving executives within an established organization. The executives at Enron, WorldCom, and HealthSouth independently built their toxic organizational cultures, while the greed-crazed executives at Tyco were facilitated by an established board and management structure.

Nevertheless, the results were the same: toxic leaders created organizational cultures that, up until the end, effectively masked their personal and the organizations' unethical behavior, ultimately destroying the viability and reputation of their organizations and the public image of their employees (if only by association).

THE ROLE OF LEADERS IN SHAPING ORGANIZATIONAL CULTURE

There is strong agreement in literature that organizational leaders, especially the top executives, play the most important role in shaping the overall organizational culture through role modeling, establishing organizational strategies ("rules of the game"), and setting the tone for the overall ethical climate. Certainly, the examples from Enron, WorldCom, Tyco, and HealthSouth suggest that unethical organizational behavior is driven from the top down through the organization.

Although leaders are probably the single most important force in shaping and maintaining organizational culture, they are not the only factor. The organizational structures and systems (e.g., compensation systems, communication structures, and management hierarchies) also play an important, supportive role in shaping the culture of an organization. There is also the oft-forgotten role of the whistleblower in alerting the organization to covert mismanagement. Whistleblowers can play a significant role in uncovering corporate fraud and alerting outsiders to questionable activities. As examples, Cynthia Cooper, former WorldCom chief audit executive, and Sherron Watkins, former Enron Vice President of Corporate Development, are credited for detecting and reporting corporate fraud at WorldCom and Enron, respectively. Both were named two of Time Magazine's 2002 Persons of the Year (Pellegrini, 2002; St. Mary's University, 2005).

While top executives can lead their organizations and their employees down an ethical path, leaders on their own cannot foster genuine, organization-wide ethical behavior and attitudes. A culture of ethical behavior and attitudes requires not only the cooperation of employees and other stakeholders, but also that these stakeholders essentially "buy into" the complete ethical organizational culture.

CAN GOVERNMENT OVERSIGHT PREVENT TOXIC CULTURES?

As a direct result of the Enron scandal, the U.S. government passed the Sarbanes–Oxley Act in an attempt to make business leaders more responsible than they were before for the financial results released by their organizations. Passed in the summer of 2002, the legislation sets a series of deadlines for public companies to certify that their financial results are accurate, that all material information is reported in a timely fashion, and that they have strong business process controls to protect the integrity of their financial data. Failure to meet the deadlines places their CEOs at personal risk for any financial misstatements. In demanding these guarantees, the Act is arguably responsible for the most thorough reevaluation of financial processes among U.S. businesses since the founding of the Securities and Exchange Commission.

Despite government efforts to legislate processes, the literature supports and the Enron case illustrates the contention that an ethical organizational culture cannot be created through the imposition of a code of corporate ethics or through the establishment of an ethics program in response to legal or regulatory requirements, such as the Sarbanes–Oxley Act (Altham, 2001; Clark, 2003; Hatcher, 2003; Rossouw & van Vuuren, 2003; Sims & Brinkmann, 2003). Instead, an organizational culture of ethical behavior must be inculcated throughout the organization, with each individual in the organization adhering to a personal moral code. It can thus rightly be concluded that the starting point for fostering a healthy organizational culture should be with top corporate leaders – not legislation.

ENDNOTES

1. All quotes from McLean & Elkind, 2003 (*, p. xxv; ** p. 3, ***, p. 55).

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