Red Flags of an Ethical Collapse

Wilson Sonsini Goodrich Rosati
Silicon Valley NACD
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Jim Balassone, Markkula Center for Applied Ethics
Katie Martin, Member, Wilson Sonsini Goodrich & Rosati, Board of Nuance Communications, Inc.
Skip Battle, Boards of FICO, LinkedIn, Netflix, OpenTable, Expedia, Workday and Sungevity
Vince Vannelli, KPG Ventures, Boards of Clipsync, National Payment Card Association, Solariat, TuneUp Media, Jilidy
The Seven Signs of Ethical Collapse

How to Spot Moral Meltdowns in Companies...
Before It's Too Late

Marianne Jennings, J.D.
Seven Signs of Ethical Collapse

- Published in 2006 by Marianne Jennings, Arizona State
- Studied: Tyco, HealthSouth, WorldCom, Adelphia Enron, AIG, Rite Aid, Marsh & McLennan
- Identified Seven Signs:
  1. Pressure to maintain numbers
  2. Fear and silence
  3. Young’uns and a larger-than-life CEO
  4. Weak board
  5. Conflicts of interest (back-scratching dominates)
  6. Innovation like no other
  7. Goodness in some areas atones for evil in others
<table>
<thead>
<tr>
<th></th>
<th>MF Global</th>
<th>Olympus</th>
<th>Penn State</th>
<th>B of A</th>
<th>Galleon</th>
<th>UBS Rogue</th>
<th>Murdoch</th>
<th>APS</th>
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<tbody>
<tr>
<td><strong>Numbers Pressure</strong></td>
<td>bonuses/acct tricks</td>
<td>slower growth; shell companies</td>
<td>football’s largesse</td>
<td>economy; acquisitions</td>
<td>being &quot;ahead&quot; of the market</td>
<td>progress based on returns</td>
<td>story must be unique</td>
<td>&quot;no excuses&quot;</td>
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<td><strong>Fear &amp; Silence</strong></td>
<td>fired CRO for objecting</td>
<td>fired CEO for asking</td>
<td>Janitor; disciplinary</td>
<td>General counsel</td>
<td>traders required to perform</td>
<td>co-workers who expressed</td>
<td>terminated those who</td>
<td>table punishment</td>
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<td></td>
<td></td>
<td></td>
<td>officer</td>
<td>counsel terminated</td>
<td>at meetings</td>
<td>concerns</td>
<td>failed</td>
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<td><strong>Young ‘uns</strong></td>
<td>trading staff</td>
<td>selling assets</td>
<td>young coach; young boys</td>
<td>succession issues</td>
<td>recruited from Wharton</td>
<td>31 yrs old</td>
<td>murdoch’s children</td>
<td>Direct reports</td>
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<td><strong>Icon</strong></td>
<td>Corzine</td>
<td>Chairman; Yokoo Bros.</td>
<td>Paterno</td>
<td>Ken Lewis</td>
<td>Rajaratnam</td>
<td>Big spender</td>
<td>Murdoch</td>
<td>Beverly Hall</td>
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<tr>
<td><strong>Weak Board</strong></td>
<td>Corzine made all decisions</td>
<td>dysfunctional Chairman involved in deals</td>
<td>deferential</td>
<td>sent e-mails to each</td>
<td>non-existent</td>
<td>struggles with direction;</td>
<td>failure to take action</td>
<td>unengaged</td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td>other; no action</td>
<td></td>
<td>leaders</td>
<td></td>
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<td><strong>Conflicts</strong></td>
<td>Regulator</td>
<td>bonuses and executive roles; yakuza</td>
<td>PSU officials on coach’s</td>
<td>plan for fed to take</td>
<td>experts betraying</td>
<td>profits not questioned</td>
<td>Family ties</td>
<td>recognition</td>
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<td></td>
<td></td>
<td></td>
<td>board</td>
<td>losses; bonuses</td>
<td>companies</td>
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<td><strong>SR</strong></td>
<td>Suits donated</td>
<td>political controls (puppy pond)</td>
<td>Foundation Paterno gifts</td>
<td>diversity; community</td>
<td>Work overseas</td>
<td>Social involvement</td>
<td>generous donors</td>
<td>worthy goal</td>
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<td><strong>Belief that they are better</strong></td>
<td>we do not need regulation</td>
<td>disregard of laws and investigations</td>
<td>Winning record</td>
<td>we survived subprime</td>
<td>&quot;we’re smarter!&quot;</td>
<td>experience in internal</td>
<td>The stories we run</td>
<td>We outdid all of them</td>
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<td>controls</td>
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Signs of Ethical Failings

1. Bigger than life CEO; the rock star exec; “its only illegal if you get caught”
2. Conflicts of interest undermine integrity; lack of transparency; back scratching
3. Silo effect: Board members highly specialized in skill or experience; trees and forests
Signs of Ethical Failings

4. Excessive pressure/highly leveraged compensation leads to rule “bending” (sic!)

5. Intense loyalty distorts integrity and transparency; some real good atones for some bad

6. Conduct in personal life is excused or ignored, e.g. “men behaving badly”
Signs of Ethical Failings

7. Inability/unwillingness to speak truth to power (or hear); don’t ask, don’t tell; appearing stupid

8. Board members acting like caretakers or consultants and not owners; skin in the game