

A Crisis of Core Values

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As I dusted off my old notes and began to prepare these comments, the Chicago Tribune published the story of the rise and fall of Andersen (Tribune Special Report: A Final Accounting; September 2, 2002). The Tribune reported that the founder, Arthur Andersen, had established the firm on principles of integrity. If a client threatened to take his business elsewhere because the accounting firm would not sign off on a financial statement that contained deception, Andersen would fire the client. As the accounting business became more competitive and profits were squeezed, new management launched a drive for increased revenue and profits with the "hope" that the principles of integrity would not be compromised. After disasters with Waste Management, Enron, et. al., Andersen was found guilty of obstruction of justice in the Enron case because it destroyed tons of documents that pertained to the case. Andersen ceased all auditing of public companies on August 31, 2002. On September 17, 2002, the Chicago Tribune reports: "Andersen, once a revered member of the Big Five accounting firms, has just a few thousand of its 28,000 workers as it shuts its audit practice."

Andersen changed from core values based upon integrity of audit results to core values based upon revenue growth and profits. Those partners that produced profits in spite of legal sanctions and lawsuits were promoted.

Let's look at the example of one Andersen partner, Robert Kutsenda. He first came on the scene with his management of "Supercuts," a chain of barbershops. A new Chief Financial Officer was hired and was alarmed with the practice of "construction cuts." At an early point in the construction of a new shop, the hair of one of the construction people would be cut and the franchise fees would be posted to the company's Profit and Loss Statement. The new CFO discovered that elimination of all back "construction cuts" revenue would mean that the company had experienced zero growth in revenue. The public release of this information would jeopardize the company's public offering. The CFO was fired and the accountant was promoted to the Waste Management account where revenues were over-stated by \$1 billion from 1992 to 1996. After settlement of shareholder lawsuits and SEC sanctions in the Waste Management case, the accountant was promoted to Senior Partner in charge of worldwide record retentions policy. The new policies were used to destroy documents in the Enron case, which ultimately led to the obstruction of justice suite that brought Andersen down.

Andersen was not able to balance the need for profits with the "hope" that their principles would not be compromised. Running a successful business is more difficult than just achieving profits. Andersen became very profitable and the partners prospered. The average income of a partner in 1980 was \$130,000. In 1990 the average income was \$200,000 and in 2000, it was \$450,000. Jim Collins explains the problem well in his book, "From Good to Great." "Enduring great companies don't exist merely to deliver returns to shareholders. Indeed, in a truly great company, profits and cash flow become like the blood and water to a healthy body: They are absolutely essential for life, but they are not the very point of life." Collins goes on to say that he found no consistent set of core values in the "great" companies but many of the core values of the "great companies" will sound familiar to those who have studied Quality; a commitment to customer satisfac-

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tion, prevention of problems, intolerance of error, and management by fact.

A commitment to customer satisfaction begins with the understanding that the processes that deliver products, services and information to the customer must be well-defined and capable of delivering defect-free outputs to the customer. Well-defined processes are ones where there is a clear understanding of what the customer wants. These wants are defined by "requirements." Requirements are specific, measurable and define the output to customers. Let me provide an example. I moved to Florida in 1983 and learned that one of the joys of Florida living was that the grass surrounding my home grew year round and needed year-round maintenance. I decided to hire Pepe's Landscaping Service to maintain my lawn. Randy Pepe spent an hour with me surveying the lawn and asking questions to understand our needs. We agreed that the lawn would be cut to a height of 1 1/2 to 2 inches because it was St Augustine grass. The other common grass in Florida was Bermuda, which is cut much shorter. We agreed: the day of the week it would be cut; whether clippings would be collected or left on the lawn; trimming of the walks, drives and shrubs; fertilizing and insect treatments; and, finally price. We had met face-to-face to clearly understand what my needs were and agree on the requirements. We had defined customer satisfaction up front before the work began and Randy's commitment to meeting those requirements led to many years of outstanding service. One of Andersen's fundamental mistakes was losing sight of the core values. The purpose of an audit is to ensure and attest to the integrity of reported financial results. Once Andersen started treating audits as a "loss leader" for the more profitable business, it was only a matter of time before the integrity of the audit process came under severe pressure.

The second core value is "prevention of problems." Randy had several choices in his approach to my business. He could have negotiated the best price and promised the moon without taking the time to understand my needs. However, as each week rolled by with the grass being cut to the wrong height, the clippings not being collected and grass overgrowing the sidewalks, Randy would have made his money but our relationship would have been destroyed and his future employment in doubt. The first step in "prevention of problems" is to take the time to clearly understand the "requirements" of the customer. The next step is to assure that the work process is capable of consistently meeting the requirements. Randy must assure that: he has room on his production schedule to cut my lawn every Wednesday; the lawn mowers are maintained and the blades are sharp; other crews, who may cut my lawn have a clear understanding of my requirements; and, all new employees are trained before being put to work. Randy did these things and, therefore, had a happy customer who would pay his bills on time and refer new business to him. Andersen's flaw was elevating revenue generation above problem prevention. It's as if the healthcare profession had changed their core value from the Hippocratic "Above all, do no harm" to "Above all, hit your revenue target."

The third "core value" is the attitude that error is unacceptable. This does not mean that people will never make a mistake. It means that when error does occur it is unacceptable to all involved and efforts will be made to assure that that error never occurs again. Philip Crosby called this attitude "zero defects." W. Edwards Deming called it "continuous improvement." Motorola calls it "6 sigma." The Japanese call it "kaizen." Whatever the guru, the concept is simple, "Do It Right the First Time."

The last of the core values is "management by fact." I remember a Christmas party my first year out of college and the opportunity to speak to a company president. I was intrigued because I had never had the

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opportunity to speak to a company president before. I asked him what a president did. He said, "I make decisions. Right or wrong, I make decisions." Philip Crosby, the author of "Quality is Free" and founder of the Quality Management consulting practice, Philip Crosby Associates, did much to ignite the world's interest in Quality Management in the early 1980's. Phil explained the role of executives in decision making as follows: "Sometime, you will not have all the information you need to make a decision. When that happens, think hard and make the best decision that you can. By the way, Phil would say, that should happen to you once or twice in your career, not once or twice a day." Andersen made a decision to break from the past with a daring new strategy that for twenty years generated increases in revenue, profits and income for the partners. Unfortunately, the decision led to its down-fall. I wonder how that momentous decision was made.

As we face the rigors of the 21st century, I believe that the concepts and techniques of Quality Management have a new place. Management has struggled with a unifying theory of management. MBA programs present classes in marketing, finance, accounting, operations, human resources, etc., but what holds these functions together? One of my old business professors once maintained that managing a company was like driving a stagecoach in the old west. The president of the company is the driver and each set of reins in his hands goes to a bit in the mouth of one of the horses. Each horse represents a different functional department and by shear force the president drives the coach onward towards its goal. I think we can do better than that. The discipline of Quality Management presents us with a concise and actionable set of core principles: Commitment to customer satisfaction, prevention of problems, intolerance of error, and management by fact.

Andersen is just one example of so many of today's firms which have lost their bearings. I propose that a new unifying theory of management, using the principles I've just described, provides a vehicle to get business "back on track." It's up to us to make sure that the current crop of systemic business failures becomes the last.