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Every company needs the big producers among its staff. But sometimes they can make you vulnerable

AUSTRALIAN EXECUTIVES may be resting on their laurels too early. The consensus is that Australia has escaped US-style accounting and financial scandals by having better corporate governance practices. But by defining the pathology narrowly, the experts may be overlooking incipient ailments.

In the 1990s, share prices became the most important measure of corporate performance. Senior managements therefore feel pressured to deliver consistent – better yet, improving – financial returns.

This focus on narrowly defined results distorts behaviour. We'll look at one manifestation, which we'll call the big producer syndrome: when an individual or unit that performs impressively is not monitored as closely as it should be.

Ironically, pathological big producers tend to surface in organisations that have admirable qualities: they're results-oriented, entrepreneurial, flexible. But these attributes, taken to excess, do great harm.

Financial services, which gives generous rewards and considerable latitude to capable employees, provides many examples of this phenomenon. They include Credit Suisse First Boston's Frank Quattrone, recently suspended for allegedly ordering the destruction of documents in an SEC investigation, and whose technology group was virtually a firm within a firm.

Barings' Nick Leeson and Kidder Peabody's Joseph Jett were both traders who exploited accounting weaknesses and whose actions led to the demise of their firms.

And the list of internet analysts who touted dubious businesses is long. In all of these cases management was well aware of the outsize profits generated and decided not to probe.

Any business that offers freedom to deliver results and rewards production is at risk. Many professional services firms, for example, have a partner or two whose work product or professional conduct is not up to scratch, but who is nevertheless considered valuable because he controls a large book of business.

Or consider the Swedish pharmaceutical company Astra, whose US CEO Lars Bildman regularly preyed upon young female staffers, a habit that ultimately led to a $US9.85 million settlement, the largest at the time for sexual harassment. Although Bildman's behaviour was in open view, executives from head office chose to look the other way.

Channel stuffing – using promotions to get distributors to take more product than they normally would and thus steal sales from future quarters – is another instance of the phenomenon. In 2001,

Bristol-Myers Squibb pushed hard to sell drugs about to go off patent on the assumption that new drugs would hide the bubble.

Things did not work as planned, and Bristol told analysts to expect earnings per share to fall by nearly a third in the next year as distributors worked off their inventories.

What is a vigilant executive to do?
There is no one-size-fits-all approach, but the following are some places to start:

- **Recognise your vulnerability.** Some situations increase the risk of key producers overreaching. They include rapid growth, significant use of equity-based compensation, high financial leverage, and adverse industry developments.

  OneTel is a classic illustration: a rapidly growing company with inadequate controls, pursuing the wrong objectives (signing up new customers irrespective of whether they could pay) because it generated short term cash and made the company more saleable to investors.

- **Walk your talk.** Forget codes of conduct. The only message that carries any weight is how you pay and promote people. And if you can't recall someone's career suffering from an ethical or business breach, be worried. It is unlikely that your company is such a paragon of virtue that there isn't someone who needs to be reined in.

  Even high-testosterone organisations define where the limits lie. General Electric is noted for dramatic firings. Goldman Sachs promotes team play through many means, the most powerful being bonuses. The steady, rock solid professionals reap greater rewards relative to the profits they generate than their flashier, more aggressive but potentially less judicious colleagues.

- **Make sure your controls have teeth.** Whether controls reside in particular departments, such as compliance and internal audit, or in certain processes, they need to have authority relative to line managers, even highly profitable ones.

- **Devise back channels for whistleblowers.** Informing the higher-ups of apparent corporate misdeeds is a career-limiting move. Yet in the great majority of corporate scandals, attempts to alert senior management were quashed or discredited.

- **Simple mechanisms can be effective.** For example, Bain polls members of each engagement team monthly on whether the project is adding value. If the majority votes no, the assignment is terminated.

- **Consider rethinking who you hire.** Harvard Business School has concluded that ethics can't be taught and has revamped its admissions policies to try to steer clear of those willing to do anything to get ahead. Organisations are what they recruit. Question whether yours needs to tweak its mix of personalities. It might be time to increase the proportion of people who are effective but who also have a solid moral code.

Australian executives would do well to use thisperiod of introspection to examine the way they balance financial results against other, less easily measured but no less important outcomes, such as reputation and quality of relationships. A minor course correction can yield disproportionate rewards.

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