002Bat.Intro 2/10/03 1:37 PM Page 1

# Introduction

## Values Make the Company

A COMPANY'S VALUES—WHAT IT STANDS FOR, WHAT ITS PEOPLE BELIEVE IN—ARE CRUCIAL TO ITS COMPETITIVE SUCCESS.
—Robert Haas, Chairman, Levi Strauss & Co.[1]

"Think about how much of our lives we spend at work," the executive of a New York publishing house said wistfully to me. "Then consider how ambivalent—and perhaps a bit ashamed—most of us feel about the corporations who employ us. I know that I want my life to count for something more."

He is not alone. Corporate workers from the mailroom to the highest executive office express dissatisfaction with their work. They feel crushed by widespread greed, selfishness, and quest for profit at any cost. Apart from their homes, people spend more time on the job than anywhere else. With that kind of personal stake, they want to be part of something that matters and contribute to a greater good.

002Bat.Intro 2/10/03 1:37 PM Page 2



Sadly, those aspirations often go unmet. Trust in our financial and commercial institutions is eroding. Every day, the newspaper fills us in on the latest corporation to fall into financial misconduct and public deception. Insider trading on public markets, cooking the books, outlandish executive pay and perks, fraudulent research that covers up the harmful effects of products on people and the environment: a steady stream of scandals deeply scars the business landscape. "Business as usual," an expression that once implied steady confidence in the flow of financial exchanges, now sounds the alarm to watch your back—if not your wallet.

Truth be told, the corporate crisis is as much spiritual as it is financial. Yes, fortunes are won or lost on the ability to anticipate trends and create products that meet those demands. But capitalizing on innovation is not enough today. A company's success also hinges on whether in the eyes of its employees and the public it honors a common sense of justice.

"Whatever company I work for in the future, I'll never again trust at face value what top executives say." A deep sense of betrayal marks these words spoken by a Global Crossing vice president who was laid off just weeks before the broadband telecommunications company filed for federal bankruptcy protection amid questions about its accounting. Along with thousands of other Global Crossing employees, she did not receive severance pay. "When top executives laid us off they must have known they were going to file bankruptcy and that they'd never have to pay us severance," she says, adding that some senior officials left the company with generous exit packages. "Maybe what they did was legal, but it feels unethical, especially when you look at how they treat themselves."[2]

002Bat.Intro 2/10/03 1:37 PM Page 3



Workers are six times more likely to stay in their jobs when they believe their company acts with integrity, according to Walker Information, a research company that measures employee satisfaction and loyalty at the workplace. But when workers mistrust their bosses' decisions and feel ashamed of their firm's behavior, four out of five workers feel trapped at work and say they are likely to leave their jobs soon.[3]

To thrive, corporations need to take account of this crucial shift in social values. Dispirited workers do not perform well; low morale saps the passion and creativity that otherwise would be unleashed on behalf of a company's mission. Corporate workers are looking for a new vision, a path to save the corporate soul. And just maybe their own.

## Soul Searching

What is it about the corporation that makes joining it feel as if we're making a bargain with Mephisto for our soul?

Nearly fifty years ago, my father launched his professional career in the corporate world, joining General Electric in a management training program. He then made a horizontal move to Union Carbide and finally fled the corporate world altogether a few years later to start a family-owned retail business. My dad could not point to any specific conflict he had with the corporation, and, now in retirement, he wrestles with the what-ifs had he stayed and patiently climbed his way up the corporate ladder. At the time, however, my dad deplored the feeling that he was becoming just another number in an impersonal organization, a cog in the machine.

In his 1956 classic *The Organization Man*, William Whyte gave ample evidence that my father did not face his spiritual

002Bat.Intro 2/10/03 1:37 PM Page 4



struggle alone. Whyte showed that the growth of large organizations, while leading to vast economic and political changes, was having an equally dramatic impact on the individuals who worked inside them. Their collision with the corporate structure stripped workers of a sense of uniqueness and forced them to make decisions not of their own choosing. These observations led Whyte to a radical conclusion: "We do need to know how to co-operate with The Organization but, more than ever, so do we need to know how to resist it."[4]

That legacy is still deeply rooted in our popular consciousness. Recall the number of movies you have seen that feature heroic characters who fight against the greed of a corporate giant to save their community. Hollywood has made an icon of the underdog fighting incredible odds to do the Right Thing.

Is it really meaningful, then, to talk of a corporate soul? After all, the corporation was created in part to protect individuals from being held personally responsible for the actions of a public entity. It also offers a more efficient structure for aggregating capital that yields the potential for higher profits. None of these objectives depends on promoting the dignity and worth of individuals or their communities. The corporation's harshest critics in fact depict it as a cold, calculating machine.

In this book, I will show that a corporation has the potential to act with soul when it puts its resources at the service of the people it employs and the public it serves. That journey begins once a company seeks to align its mission with the values of its workers. It is unrealistic to expect that all of the workers' values will match those of the company, of course. But when that alignment moves closer together, the morale of the company is transformed.

002Bat.Intro 2/10/03 1:37 PM Page 5



Precisely for that reason, senior managers need to step back occasionally from the tyranny of the urgent and ask their own people, "Why is it that you want to work here?" If workers cannot get inspired about the company, they will not communicate a compelling message to customers. A vital corporation helps its people to think, plan, and express their dignity in the way they carry out their daily tasks on behalf of the enterprise. In other words, it tends to its soul.

Workers, in turn, need to evaluate honestly what their company stands for. If its core ethos violates their personal values and they are unable to change the environment to align who they are with the real company mission (rather than the published one), then it may be time to start looking for a new place to work.

The market alone cannot guide our decisions. Although the market is a dynamic platform for producing meaningful social goods, it is inherently bent toward impersonal ends. Read Tom Higa's story, which follows, and I think you will agree.

## How Much Is Enough?

Tom Higa operated his Chevron gas station on a corner block in San Francisco for over twenty-five years.[5] It was the old-fashioned kind of shop where the attendant would wash the windows and kick the tires. Tom began working at the gas station as an attendant in 1964. After eight years of hard work, he took over as owner and picked up the station lease with Chevron.

Tom is exceptionally popular in his community. He hired locally over the years and provided a high quality of service to his customers. In turn, Tom owes a great debt to his neighbors. They saved his business.

002Bat.Intro 2/10/03 1:37 PM Page 6



Back in 1989, Chevron gave Tom the shocking news that it would not renew his station lease. The underground storage tanks on the property were in need of replacement at a cost of about $150,000. Oil company officials told him that the station was outdated and no longer matched the image of what a Chevron station should look like.[6]

Tom didn't see it coming. He had consistently met or surpassed the gas sales Chevron had set for his station; in fact, his operation was returning a healthy 12 percent profit margin on average. "I wasn't going to become a millionaire, but I earned enough to keep my family secure and deliver a good return to the corporation. I don't know what profit level it would take to satisfy Chevron," wondered Tom.[7]

The financial analysts back at Chevron headquarters indeed had crunched the numbers and concluded they could do better. By closing Tom's business, demolishing the station, and building a commercial building on the site, the property could return at least a 15 percent profit margin. Chevron corporate saw it as a clear-cut business decision to maximize profits.

Tom went into a panic. What other livelihood could a man nearing fifty with two young children and a lifelong career at a gas station pursue? Chevron officials suggested he might enter a computer-training course. To Tom, the idea was absurd; such a career detour did not match his skill set or his interests. He knew what he had a passion for, and that was running a gas station.

The neighbors were upset as well. They wanted a service station in the community, not another commercial building. "The whole neighborhood loves this place," remarked one of Tom's long-time customers. "They're honest and friendly and trustworthy, and they give real good service. Isn't that the kind of image a company wants?"[8]

The neighbors leaped into action. They sent hundreds of letters and a long list of signatures on a petition to Chevron urging the corporation to reconsider. Copies also were sent to San Francisco's city hall, and they landed on the desk of Mayor Art Agnos.

Agnos backed a thriving private sector in his city, but he also took seriously his responsibility to protect the interests of citizens.[9] He placed a call to Chevron's corporate headquarters, and within days, one of its senior managers paid a visit to his office.

The mayor asked the Chevron manager whether the neighborhood had presented an accurate picture of Tom Higa's business. Did Tom really hit his numbers for gas sales quarter after quarter? Yes, the manager confirmed, but then went on to review the business case for Agnos, emphasizing how the corporation could raise its profit margin with the execution of its plan.

Agnos searched for a compromise. How about delaying the plan for another eight to ten years until Tom was closer to retirement age? No, the manager responded; the company was determined to move forward now.

His stubborn and callous attitude angered Agnos. The mayor informed him that Chevron's plans to develop the property might not go as smoothly as the company had projected. In fact, he threatened him on the spot with a stringent environmental impact procedure that in all likelihood would lead to delays and substantial unforeseen costs.

A pitched political struggle ensued in San Francisco. The details will not be fully recounted here, but suffice it to note that Agnos and the city council went ahead with the environmental impact legislation, Chevron's plans to repurpose the

002Bat.Intro 2/10/03 1:37 PM Page 8



property were thwarted, and Tom Higa's Chevron went on to operate at a healthy profit for another decade.

There's an added behind-the-scenes piece to this drama that underscores the values at stake. While he was mayor, Agnos held a quarterly luncheon with the chief executive officers (CEOs) of the major corporations with headquarters in San Francisco. The atmosphere turned chilly shortly after the mayor's showdown with Chevron. Agnos recalls entering the dining room to an awkward silence. Moments after all were seated to begin lunch, the CEO of one of California's major banks raised his voice so that all gathered could hear: "Arthur, you realize that we're pretty upset at you over this environmental legislation."

Agnos paused a second before replying, "Okay, I guess that's understandable, but let me give you my perspective. Here's a man with a family to support, owner of his own franchise for sixteen years, and the business is thriving. Then a wealthy corporation announces it's going to shut him down. He's always made money for the company, yet some green analyst in headquarters figures on paper the company can make a few percentage points more. So let me ask you something: How much is enough?"

All conversation and movement came to a stop. Agnos, it seems, had uttered an unpardonable blasphemy. The bank executive came back with emotion: "Arthur, the very fact that you can ask that question terrifies me."

Agnos let another agonizing half-minute pass, each player waiting for the next move in this awkward chess game. He then drove home his point: "So, guys, I ask you again: How much is enough? Since no one has responded, I guess the answer is that there's never enough, no matter what the cost."

002Bat.Intro 2/10/03 1:37 PM Page 9



Agnos had raised the relevant question: How does a business calculate the cost of personal livelihood and community vitality? For the financial analysts at Chevron, at least, the Right Thing to do lies plainly in front of us in the numbers.

But raw numbers can tell many tales. In this instance, the effort to close Tom's business may have ended up being more costly than Chevron had anticipated. It could not quantify the financial impact of a tarnished company reputation once the saga was dragged through the media. Nor could it calculate the strategic impact on other Chevron franchises once word spread that reaching, and even surpassing, targets for gas sales would not protect them from foreclosure. Finally, it could not put a financial figure on the low morale of Chevron employees at corporate headquarters, who surely felt something less than pride in their company's efforts. In short, a strong business case can be made that Chevron's decision to close down Tom Higa's service station was costly indeed.

## Finding Common Ground

The vast majority of corporate executives would say, at least in their more candid moments, that their firm's public responsibility begins and ends with their shareholders. "What is enough?" you ask. "More than last quarter" is what they answer. That is the measure by which they are hired, compensated, and fired. It is also the plumb line that the stock market uses to reward or punish their companies.

Over the past two decades, public markets have tended to be unrealistic about the growth curve of individual enterprises. Even the best-run companies are subject to the rise and fall of economic cycles, but one bad quarterly earnings report these

002Bat.Intro 2/10/03 1:37 PM Page 10



days and a company's stock gets hammered on the trading floor. This quarterly vision practically forces senior managers to look for short-cuts that will inflate short-term results at the expense of long-term sustainability.

For that reason, the burden for reinventing corporate behavior extends beyond the executive office. It is vital for other stakeholders who participate in the business web to reevaluate the ways they work, invest, partner, supply, and consume.

The problems at Enron, for instance, cannot be isolated to a small group of executives who looked to enrich themselves. When the going was good and Enron was reporting mind-blowing profits, few people cared that they could not make heads or tails of the company's financial statements. The desire to believe the illusion led lots of eyes to gloss over the obvious signs of chicanery. Once Enron started to stumble and report losses, the emperor's clothes fell off with startling quickness.

Given this landscape, I try to be very practical about what it takes to change corporate behavior. We are in dire need of senior managers who have the vision and courage to make good choices when the payoff may not be immediately apparent on the balance sheet. But in most cases, they will need to be convinced that doing the Right Thing will have a positive effect on their firms' bottom line, or at least will not add to the cost of doing business.

I realize that "doing the Right Thing" may seem quite subjective as a standard for corporate behavior. Business leaders rarely talk about the values that shape the character of a corporation and make an impact on its financial performance. But they do exist. In this book, I feature the following eight principles that I consider the most crucial for corporate performance:

002Bat.Intro 2/10/03 1:37 PM Page 11



Principle One: The directors and executives of a company will align their personal interests with the fate of stakeholders and act in a responsible way to ensure the viability of the enterprise.

Principle Two: A company's business operations will be transparent to shareholders, employees, and the public, and its executives will stand by the integrity of their decisions.

Principle Three: A company will think of itself as part of a community as well as a market.

Principle Four: A company will represent its products honestly to customers and honor their dignity up to and beyond a transaction.

Principle Five: The worker will be treated as a valuable team member, not just a hired hand.

Principle Six: The environment will be treated as a silent stakeholder, a party to which the company is wholly accountable.

Principle Seven: A company will strive for balance, diversity, and equality in its relationships with workers, customers, and suppliers.

Principle Eight: A company will pursue international trade and production based on respect for the rights of workers and citizens of trade partner nations.

Companies that incorporate these eight principles into their operations do not put themselves at a competitive disadvantage. In fact, substantial evidence indicates that principled companies excel financially over the long haul. Towers Perrin, the management consulting firm, took a close look at twenty-five companies that enjoy a strong reputation for public integrity and are rated year in and year out as desirable places to work. That model group includes well-known corporations like Southwest

002Bat.Intro 2/10/03 1:37 PM Page 12



Airlines, Johnson & Johnson, Applied Materials, and Procter & Gamble. Towers Perrin analyzed the market performance of these principled companies over a fifteen-year period and then compared their returns to those generated by public companies at large. The results: the principled companies delivered a total shareholder return of 43 percent, while the shareholder return of Standard & Poor's 500 performed at less than half that figure: 19 percent.[10]

A snapshot of Johnson & Johnson may offer a clue to why principled companies excel. In its corporate credo, Johnson & Johnson lists the stakeholders that its employees are asked to honor with their business decisions: first, customers; second, coworkers; third, management; fourth, the communities where the company operates; and fifth, shareholders. Lest we think that Johnson & Johnson is a philanthropic endeavor, the company credo also declares the obvious: "Business must make a sound profit." But the company does pledge that profit will not eclipse its other priorities.

In 1982, the Johnson & Johnson credo was put to the test when a major disaster hit. Eight people died from ingesting cyanide-laced Tylenol capsules. Johnson & Johnson executives made a decision immediately to recall 31 million bottles of Tylenol from store shelves even before the cause for the crisis could be determined. The company also promptly redesigned product containers and introduced tamper-proof packaging. Although Johnson & Johnson turned out to be blameless, the crisis ended up costing the company $240 million and cut its profits on $5 billion in revenues that year almost in half. But its decisive action ended up saving the Tylenol brand and generating a wave of goodwill from its customers.[11]

002Bat.Intro 2/10/03 1:37 PM Page 13



The Johnson & Johnson experience underscores why corporations would be foolish to sacrifice their credibility at the altar of earnings reports. Long-term market value does not rise or fall independent of a company's social impact. And like it or not, every action a corporation takes may be interpreted as a statement about what it stands for.

## Accounting for the Good

If we had to settle on one philosophy that rules business operations today, it could be captured by this mantra: If you can't measure it, you can't account for it. That's precisely the reason that efforts to translate principles into corporate practices so often languish at the point of execution. Most senior managers today do feel an escalating pressure to conform to higher standards of integrity. But if they cannot understand how to identify and measure their outcomes, they are likely to consider principles a matter of image, not substance.

I hope to make it clear that a company's capacity to integrate the eight principles detailed in this book will enhance or (alternatively) diminish its overall business performance. The Towers Perrin study cited above indicates the potential impact on shareholder return over an extended period. There are three other prime areas where principles and their business outcomes can be assessed:

- A principled company will fortify its reputation.
- A principled company will be more likely to avoid costly lawsuits.
- A principled company will manage its business network more effectively.

002Bat.Intro 2/10/03 1:37 PM Page 14



Let's turn our attention first to reputation. Although it may seem the most intangible area of the three, it is a crown jewel among a company's assets.

*Reputation: The Guardian of Your Brand*

A brand is the visual, emotional, and cultural image that we associate with a company or a product. While the daily grind of business is about sales, brand building looks to create a bond and loyalty that lasts. Over time, customers develop a personal affinity with a brand; once they feel betrayed, their fury lashes out as it would toward a fallen politician or a movie star.

Reputation is not the same thing as a brand. We attribute character to people, and we do the same thing to companies. Reputation is the perceived character a company holds in the public eye. A company's reputation in large part depends on its ability to meet the expectations of a broad range of stakeholders.

A lot of companies have a strong brand but lack a well-established reputation. Sony and Pepsi-Cola, for instance, can boast solid brands, but neither company really has much of a reputation. When we think of Volvo, on the other hand, we think safety,

**The Public's View**

The public's impression of a company is most influenced by . . .

Contributions to social good: 56 percent

Brand quality: 40 percent

Business fundamentals: 34 percent

*Source: Corporate Social Responsibility Monitor 2001* (Toronto: Environics International, 2001).

002Bat.Intro 2/10/03 1:37 PM Page 15



**What People Look for When Choosing an Employer**

| *Factor* | *Rating* |
|---|---|
| Career growth potential | 1 |
| Strong corporate reputation | 2 |
| Starting salary | 3 |
| Fringe benefits | 4 |
| Record of high yield for shareholders | 5 |
| Good sports and social facilities | 6 |

*Source:* Cone/Roper, *Cause-Related Trends Report: Evolution of Cause Branding* (Boston: Cone, 1999).

which is a reputation holding up a brand.

Reputation serves as the guardian of the company brand. A company can take years to build a brand yet destroy it overnight with a soiled reputation. Arthur Andersen is a prime example of a firm that took a shortcut marked by dollar signs and undercut a brand that had been carefully cultivated over nine decades.

In today's business climate, reputation has become as important as brand. For starters, it is a key asset for attracting employees. A Cone/Roper study finds that corporate reputation is the second most important factor for people choosing an employer. Remarkably, job candidates rate reputation more highly than starting salary or fringe benefits.[12] People put a high premium on working for a firm that can be trusted.

Customers and investors also are highly influenced by a firm's reputation. Nearly four out of five Americans say they at least consider reputation when buying a company's product, and 36 percent call it an "important" factor in their purchasing decision, according to a survey conducted by Hill and Knowlton. The same study shows that more than 70 percent of investors consider reputation in their decisions even if that choice means lowering their financial returns.[13]

002Bat.Intro 2/10/03 1:37 PM Page 16



Now here's the bad news: consumers give very few companies high marks for reputation. Less than 2 percent of Americans surveyed look at U.S. companies as "excellent corporate citizens," and more than half rate corporations as "below average" in social responsibility.[14]

### *Going After Carrots and Avoiding Sticks*

While some business leaders like to pin the spate of corporate scandals on a few rotten apples in the barrel, the American public believes they reflect more fundamental problems with the way corporations do business. In a Washington Post/ABC News poll, roughly three of four people viewed the malfeasance of WorldCom, Enron, and Global Crossing as "a sign of broader problems with the way many companies report their financial condition." Fewer than one in four believe that these scandals are "pretty much isolated incidents."[15]

The public thirsts for justice in the business world. If corporations are unwilling to take the steps necessary to amend their behavior, citizens will turn to the courts and legislators to set the standards. Historically, the levels of public trust in American business determine how much citizens look to their government to regulate business.

To date, the punitive stick has focused on a practice that the corporate world euphemistically calls aggressive accounting, and in many cases is nothing more than cooking the books. In April 2002, the Securities and Exchange Commission (SEC) levied a fine of $10 million on the Xerox Corporation, at the time the largest penalty ever given a public company in connection with financial reporting violations. As part of the set-

002Bat.Intro 2/10/03 1:37 PM Page 17



tlement with the SEC, Xerox was forced to restate its earnings for a five-year period.[16] In levying such a stiff penalty, the SEC was sending a clear message to corporate America: if we can go after an established, well-respected player like Xerox, any company can be exposed and punished.

A business professor at the University of Pittsburgh, Jeff Frooman, measured the stock market's reaction to incidences of corporate misconduct. He took a close look at twenty-seven separate incidents when a corporation was slapped with punitive measures, such as regulatory fines, environmental lawsuits, and product recalls. The pattern he found should be a strong caveat to all who are responsible for corporate governance: offending companies suffered significant losses in shareholder wealth that in most cases they never recovered.[17]

### *Delivering on Trust Across the Network*

The modern corporation does not live as an island unto itself. It swims within a sea of network-based enterprises that extend from manufacturing to distribution to marketing. As a result, many of a company's key relationship assets—the people whom it must trust to succeed—are located outside the corporate structure. Despite that fact, a firm is held accountable for every action that takes place in its name across the network enterprise. That fact alone should raise real concerns about the effectiveness of conventional structures of governance.

The operation of a business has a new level of transparency today. Because network-based enterprises are so heavily information driven, just about every policy, administrative action,

002Bat.Intro 2/10/03 1:37 PM Page 18



investment, or transaction eventually reaches the public domain. Over the Internet, hundreds of millions of people have at their fingertips an effective tool for getting access to and sharing information. The higher the profile of a brand, the greater is the scrutiny of its activities.

Executives at Boise, the giant timber company, can attest to the daunting challenge this level of transparency creates. Over the past decade, Boise has faced intense pressure from consumers and distributors to end the harvesting of old-growth trees. At the prompting of environmentalists, a diverse group of customers including Kinko's, L. L. Bean, Patagonia, and the University of Notre Dame started boycotting the company's paper products. Explaining his company's decision to cancel its contract with Boise, John Sterling of the clothing company Patagonia, said, "There will always be companies that don't care where their lumber and paper come from, but as their customers become more sophisticated about environmental issues, they're going to have to pay closer attention to the practices of suppliers that sell them wood products."[18]

The consumer boycott and erosion to its brand forced Boise to reevaluate all its supplier relationships, and in March 2002, it announced that it would drastically reduce old-growth logging. An official for the timber industry, disappointed that Boise caved in to public pressure, complained, "It's blackmail any way you slice it. As more and more retailers fall victim to this extortion campaign, it could definitely have an impact on the industry."[19]

What this timber industry official fails to understand is that we have entered a new era. Network enterprises cannot ignore the values of their customers and partners. The savvy corpora-

002Bat.Intro 2/10/03 1:37 PM Page 19



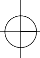
tion will not treat public scrutiny as blackmail, but instead will see it as an opportunity to strengthen its reputation with customers.

Because environmentalists are holding the business enterprise accountable for its impact on the earth, most large corporations are putting protocols and standards in place to address their concerns. This book offers a blueprint to take action as well on other areas of public trust that are rising to prominence. Absent standards of accountability, a firm risks a reputation breakdown anywhere in its network.

Corporate workers often have to make decisions that will affect the lives of their fellow employees, customers, and the broader community. Yet most feel as if they are navigating through these prickly dilemmas without a compass. For them, my book will be a welcome guide. In each chapter, I feature real-life predicaments that confront the business enterprise and demonstrate how a principled company can meet the challenge. As useful as it is to identify the failings of business, it's more inspiring to show how companies can do it right. Hence, the lion's share of each of the following chapters will hold up best practices among corporations that are doing well by doing good. Along the way, I offer "vital signs" and practical tools that will help to monitor the application of my principle within any enterprise size.

Change can begin anywhere in the corporation. This book backs up that claim with solid evidence; a good number of the corporate innovators I feature do not hold an executive title. To make a major impact on the organization, however, an initiative eventually will need to gain the enthusiastic backing of leaders at the executive and board levels. They have the means

002Bat.Intro 2/10/03 1:37 PM Page 20





to introduce new practices across the company and the responsibility to govern their execution. The importance of leading and governing with integrity is therefore where we will begin.