How Could They Have Done It?

Did a bacillus descend from space and make Enron senior employees in equal parts evil and stupid?

Whatever else it was, the activities of Enron's finance department - people like Andrew Fastow and Michael Kopper, with the presumed if uncertain participation of CEO Jeff Skilling -- amounted to a colossal misjudgment. Their company is bankrupt instead of thriving. Its senior employees are jobless, their wealth is under attack and they face criminal prosecution and jail.

Presumably these are not the results Enron executives intended.

Laboring in the business schools have been a breed of researcher known as "behavior decision theorists," who would be inclined to see in Enron a saga of incompetence as much as cupidity. A widely-noted contribution to the field was "Ethical leadership and the psychology of decision making," which appeared in the January 1996 edition of Sloan Management Review, by Harvard's Max Bazerman and Northwestern's David Messick.

Their clinical point of view, on first glance, will infuriate those who believe moral condemnation is the end of analysis: "Unethical business decisions may stem not from the traditionally assumed trade-off between ethics and profits . . . but from psychological tendencies that foster poor decision making."

Let's say right off that not everybody buys this stuff. It's based on psychological studies of decision making in controlled games, often involving the handy fodder of the grad student population. These experiments are said to reveal systematic deviations from rationality when people evaluate courses of action.

"There is a tendency to reduce the set of possible consequences or outcomes to make the decision manageable. In extreme cases, all..."
but one aspect of a decision will be suppressed, and the choice will be made solely on the basis of the one privileged feature."

As CEO, Jeff Skilling had set a goal of ridding Enron's balance sheet of poorly-performing or volatile assets. Did he decide at some point (well before his Congressional testimony) that it would be better not to know exactly how Mr. Fastow, his protege, was achieving his desired goal?

Did Mr. Fastow become preoccupied with designing structures that he could personally benefit from to the exclusion of other considerations? Chewco and RADR, two of the partnerships formed in 1997, arguably produced real benefits for Enron. By the time we get to Southampton, initiated in 2000, raking off fees for Mr. Fastow and selected others seems to have become the sole purpose. How could he imagine that somebody would not blow the whistle, if only out of resentment at not being given a cut?

"One reason we think we are relatively immune to common risks is that we exaggerate the extent to which we can control random events."

Enron's stock price was the helium that kept the partnerships airworthy. If the stock price remained high, Enron's hidden debt exposure would not have to be realized. But anybody in business knows that 99% of the factors influencing a company's stock prices are out of management's control.

People overestimate the likelihood that they will experience "good" future events and underestimate the likelihood of "bad" future events.

Mr. Fastow had done brilliantly in school, married an heiress, and attached himself to Mr. Skilling, the rising star at Enron, who put Mr. Fastow in the CFO's seat at age 36. He was obviously somebody who could take risks without really taking risks. Everything would always come up roses for him.

People believe their wants and demands are "fair" and "deserved."

A Journal article earlier this year quoted unnamed Enron "insiders" as suggesting that any monies Mr. Fastow steered into his own pockets were a "pittance" compared to the benefits he created for Enron.

People are "erroneously confident" in their knowledge and underestimate the odds that their information or beliefs will be proved wrong. They tend to seek additional information in ways that confirm what they already believe.

Mr. Skilling's surprise resignation a year ago came not long after he dismissed an analyst's question on a conference call by referring to a body part. Even allowing for the disgruntlement of ex-colleagues, the overwhelming picture painted of the Skilling-Fastow-Kopper circle's operating style is arrogant, secretive and exclusive. Anyone who questioned their methods was dismissed as not "getting it."

We're used to people making disastrous decisions in their personal lives, where they have complete sovereignty. We're used to people exhibiting obnoxious qualities to their own detriment. But business executives make decisions as a group and need the support of their colleagues: they create paper trails and have to explain themselves.
Maybe it's too much to ask them to be invariably honest but we would expect them not to be self-defeatingly stupid. In most cases thieves either plan to get away with it or think they aren't stealing. Enron executives seem to have believed they weren't stealing.

The purpose here is not to make psychological excuses but to get at the element of extraordinary miscalculation. On a final note, Prof. Bazerman (who bears no responsibility for the use I've made of his 1996 article) takes issue with those who, in the wake of Enron, have been clamoring for business schools somehow to teach remedial ethics to their grown-up students. Surely that's a job for parents and churches when children are still children.

What business schools can do, he says, is teach students to be aware of the systematic errors in people's thinking that can start a basically normal person "down the slippery slope to unethical decisions."

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