

Scientific American Mind - January 31, 2008

Do All Companies Have to be Evil?

Enron, Google and the evolutionary psychology of corporate environments

By Michael Shermer

In the 1987 film *Wall Street*, Michael Douglas's character, the high-rolling corporate raider Gordon Gekko, explains why America has lost its standing atop the industrial world: "The new law of evolution in corporate America seems to be survival of the unfittest. Well, in my book you either do it right or you get eliminated." He elaborates:

The point is, ladies and gentlemen, that greed—for lack of a better word—is good. Greed is right. Greed works. Greed clarifies, cuts through, and captures the essence of the evolutionary spirit. Greed, in all of its forms—greed for life, for money, for love, knowledge—has marked the upward surge of mankind. And greed—you mark my words—will not only save Teldar Paper but that other malfunctioning corporation called the USA.

In the now famous "greed" speech, we find several myths that I hope to bust in this article: that capitalism is grounded in and depends on cutthroat competition; that businesspeople must be self-centered and egotistical to achieve success; that evolution is selfish and only winnows and never creates; and, of course, that greed is good.

Humans are by nature tribal and xenophobic, and thus evolution has enabled in all of us the capacity for evil. Fortunately, we are also by nature prosocial and cooperative. By studying how modern companies work, we can gain insights into the evolutionary underpinnings of our morality, including concepts such as reciprocity, altruism and fairness. When we apply these evolutionary findings to economic life, we learn that Enron and the Gordon Gekko "Greed Is Good" ethic are the exception and that Google's "Don't Be Evil" motto is the rule. Two conditions must be present to accentuate the latter: first, internal trust reinforced by personal relationships, and, second, external rules supported by social institutions. The contrast between Enron and Google here serves to demonstrate what in corporate environments creates trust or distrust.

The Evil of Enron

When President George W. Bush made a public statement about the Enron disaster, he attributed the company's downfall to a "few bad apples," as he would later also explain the Iraqi prisoner abuses at Abu Ghraib. The theory about a few bad apples, however, does not explain what happened at Enron, nor does it give us any deeper insight into the psychology of corporate malfeasance. In a comprehensive study of the evolution of Enron's corporate culture, management analysts Clinton Free and Norman Macintosh of the Queen's University School of Business in Ontario found that something happened between the time of Richard D. Kinder's term as president from 1986 to 1996, when Enron operated with a highly effective managerial system that included transparent governance practices, and Jeffrey Skilling's era, from 1996 to 2001, in which openness and the opportunity for checks and balances were neutralized. What was it?

Enron began in 1985, when Kenneth Lay orchestrated the merger of the Houston Gas Company with Internorth, Inc., becoming CEO of the new energy corporation. Lay then hired Kinder to run it for him while he brokered deals and curried political favors in Washington. During part of the Kinder era, from 1990 to 1996, Enron's reported earnings increased from \$202 million to \$584 million, while its revenues skyrocketed from \$5.3 billion to \$13.4 billion.

The keys to Kinder's management style were transparency, accountability and his own personal involvement at every level of the company. At regular meetings with managers and department

heads, Kinder expected everyone to come prepared to be grilled in great detail about every aspect of their job, and with a near photographic memory Kinder was not easily fooled. As one manager later remembered, “You could give him a budget number and explain where it came from and he’d say, ‘That’s not what you told me last year.’ And then he’d go to his desk and retrieve the year-earlier budget and prove you wrong. It was amazing.” Another unit leader said that Kinder “was impossible to bullshit,” and if managers “lied to him about their numbers, Rich would eat them for lunch.”

Evil often happens in hidden places, removed from social accountability, such as in the deep recesses of Abu Ghraib. The first line of defense against evil, then, is transparency, open communication and the constant surveillance of every aspect of a system. Kinder—known at Enron as “Doctor Discipline”—demanded up-to-the-minute reports such that he always knew who was doing what to whom and when. As one long-term Enron executive recollected, “Kinder would sit in that room with his yellow pad, and he knew every goddamned thing happening in that company.”

Kinder accentuated trust and accountability through a management style that included closely reading his managers’ reports, then challenging and debating them at regularly scheduled face-to-face meetings; in turn, he had these managers do the same thing with the employees under them, such that at every level Enron was transparent and thus less susceptible to mismanagement and corruption. Further, Kinder fostered a familylike atmosphere at Enron, for example, showing care and concern for the personal lives of his employees (for instance, paying the travel expenses for one of his managers to return home for a family funeral), which tends to engender respect and loyalty.

Social Shift

Everything changed in 1997, when Skilling replaced Kinder as president. A graduate of Harvard Business School and a fan of Richard Dawkins’s epochal book *The Selfish Gene* (Oxford University Press, 1976), Skilling misread the theory to mean that evolution is driven exclusively by cutthroat competition and self-centered egotism. Enamored of the notion of “survival of the fittest,” he implemented a policy at Enron called the Peer Review Committee (PRC) system, known among the workforce as “Rank and Yank.” PRC was based on the mistaken presumption that people are primarily motivated by greed and fear. Skilling ranked employees on a scale of 1 to 5, with 5s being given the boot. As a result of this strategy, 10 to 20 percent of his employees got axed every six months, leaving everyone on edge and in a state of anxiety over job security. The formal reviews were posted on a company Web page along with a photograph of the employee, increasing the potential for personal humiliation. Those who received a 5 in the relative ranking system—no matter how good their absolute performance may have been—were automatically sent to “Siberia.” From that purgatory the 5s had two weeks to find another position at Enron, after which they were “out the door.”

As Lay described it, “Our culture is a tough culture. It is a very aggressive culture.” Charles Wickman, one of Enron’s energy traders, described the corporate ethos under Skilling this way: “If I’m on my way to the boss’s office to argue about my compensation, and if I step on somebody’s throat on the way and that doubles it, well I’ll stomp on the guy’s throat. That’s how people were.”

Skilling’s evaluation and bonus system led to a lot of behind-the-scenes wheeling and dealing between department heads and managers, who swapped review evaluation points like so much horse trading. Here is one typical conversation recounted by an unnamed manager: “‘I was wondering if you had a few minutes to talk some PRC.’ She replied, ‘Why—you want to cut a deal?’ ‘Done,’ I said—and just like that we cut our deal.” Another manager described the PRC system as creating “an environment where employees were afraid to express their opinions or to question unethical and potentially illegal business practices. Because the Rank and Yank system was both arbitrary and subjective, it was easily used by managers to reward blind loyalty and

quash brewing dissent.” By pitting employees against one another, the PRC system established an environment that brought out the worst in Enron’s employees: selfishness, competitiveness and greed.

While he was producing his 2005 documentary film on Enron, director Alex Gibney presented a cache of audio tapes from a West Coast energy company, in which Enron traders can be heard requesting that power station engineers manufacture the shutdown of energy stations to decrease energy supplies along a particular grid, thereby boosting energy prices from which Enron directly benefited. In 2000 this decreased supply led to rolling blackouts in California, significant increases in energy bills and, of course, a huge spike in Enron’s stock price. When fire season exploded in California, further disrupting the energy grid and driving prices through the ceiling, one trader could be heard on tape excitedly saying, “Burn, baby, burn.”

In addition to his belief in the outdated and untenable doctrine of applying “survival of the fittest” to people, Skilling was a high risk taker, driving him to take ever greater chances with both his body and his company. Adventurous corporate trips, such as a motorcycle expedition down the ragged terrain of Baja California, only reinforced the macho competitive atmosphere of Enron’s corporate environment. Skilling’s bonus system, based on the PRC database rankings in which employees were arrayed on a bell curve, further eroded any sense of team spirit. Because bonuses ranged from 10 to 26 percent of an employee’s take-home pay, there was considerable motivation to manipulate the ratings to boost one’s rankings in the hierarchy, as well as backstabbing and sabotaging deals put together by other employees and departments. One executive said that the bonus system “had a hard Darwinian twist” that made “a humongous difference on Enron by instilling a competitive streak in every employee.” Ultimately, what causes corporate corruption is an environment of evil established by the founders, executives, directors and managers within a corporation—in short, its corporate social psychology—which then creates situations that encourage our hearts of darkness to beat faster.

The Good of Google

In contrast to the Gordon Gekko theory of economics that produces a bad-barrel corporate environment that can readily turn good apples into bad, the Google Guys’ theory of economics generates a good-barrel corporate environment that optimizes the “good apleness” of its employees and customers.

I first met Google co-founders Sergey Brin and Larry Page in 2003 at a weekend gathering in Seattle for gifted high school students called Adventures of the Mind and later at a function at the Googleplex headquarters in Mountain View, Calif., whose lobby features a giant whiteboard called Google OS (operating system), chockablock full of multicolored Expo marker–produced flowchart goals for the company, such as Develop AI, Orbital Mind Control, Google Football League, Buy New Zealand, Build Singularity, Crop Circles and, appropriately, Elimination of Evil. It is toward this last goal that the Google milieu is structured, starting with its corporate slogan, “Don’t Be Evil.”

Environments are both physical and psychological, and the Google lobby sets the tone for what awaits inside the glass doors. Speaking of which, glass doors and walls are transparent, and such openness is one of the foundations of trust. Hallways contain bicycles and large rubber exercise balls. Googlers—as employees are known—work in small group clusters, sharing space with couches and dogs. Googlers work hard because they play hard, and the Google campus is loaded with workout rooms, video games, foosball tables, pool tables, Ping-Pong tables, volleyball courts and assorted other recreational conveniences. And if all that were not enough to make employees think 27 times before pilfering pens and Post-it notes or embezzling checks and click-ad funds, free meals are available at assorted restaurants, and numerous snack bars offer a variety of goodies to munch on between meals. Professional chefs prepare healthy and delicious meals, which nine out of 10 employees cited as what they most liked about their job.

Of course, all economists know that there is no free lunch. The business model to justify feeding thousands of people a day is as obvious as it is logical: feeding your employees means that they will not leave the Googleplex grounds for meals and will thus spend more time in the office and less time driving, parking and eating somewhere off-property. And taking care of laundry, going for a haircut, getting a car wash or enjoying a massage—all can be done at the Googleplex. It is an environment that fosters both a sense of teamwork and of independence. “People talk over lunch about the things they are playing with,” one Google software engineer noted. “It is like they are the CEO of their own little company.”

There is another reason for offering employees free food and convenient amenities: reciprocity. The fundamental principle of reciprocity evolved in its most base form as food sharing among primates and has since developed into complex networks of exchange employed by everyone from mass-mailing merchants to Madison Avenue marketers—if I give you something for free, you will feel obligated to reciprocate.

Hunter-gatherer groups accumulate social credit with other groups by throwing a feast (for example, the Native American potlatch), which must be paid back in kind to maintain political capital, build economic trust and generate social goodwill. Consumer-traders accumulate psychic credit by throwing the equivalent of a potlatch, which must be reciprocated in kind to maintain political, economic and social equilibrium. Give a small gratis token to potential customers, and you increase your chances of turning them into actual customers. Readers my age and older will recall Hare Krsishnas in the 1970s handing out flowers at airports (no longer allowed) in hopes of guilting people into making a donation. More recently, one of the more blunt instruments of reciprocity I have seen is by pollsters who include a crisp new dollar bill with the survey they hope you will then complete.

The Google environment accentuates amity and attenuates enmity by minimizing corporate hierarchy and maximizing cross-pollination among people in different departments. “Because everyone realizes they are an equally important part of Google’s success, no one hesitates to skate over a corporate officer during roller hockey,” explains a statement on corporate culture employees are encouraged to read. Googlers are even expected to devote 20 percent of their time toward exploring new ideas and projects, without hierarchical supervision. A horizontal corporate structure generates an atmosphere of equalitarianism and nonelitism that taps into the environment of our Paleolithic ancestors, who evolved in what are believed to have been largely egalitarian bands and tribes.

That atmosphere expands beyond the Googleplex and throughout the world. Consider the implications of the Google Print Library Project, in which millions of books from the New York Public Library and the university libraries at Stanford, Harvard, Oxford and Michigan are being scanned and made available online, for free, and searchable by anyone from anywhere in the world. There are copyright issues with this project still to be resolved, of course, but such projects reinforce an environment of trust and are thus an important step in the millennia-long march toward greater freedom and prosperity for more people in more places. As Brin and Page wrote in their document released with the company’s Initial Public Offering: “We believe a well functioning society should have abundant, free and unbiased access to high quality information. Google therefore has a responsibility to the world.” Those who control information control the world, but if everyone has access to that information no one can control the world. Information transparency trumps political hegemony.

The central pillar of Google’s code of conduct is its now familiar slogan, “Don’t Be Evil.” But what does this phrase really mean? “It means making sure that our core values inform our conduct in all aspects of our lives as Google employees,” according to the code of conduct posted on Google’s Web site. And what are those core values? Brin and Page’s answer shows how markets can be moral when they are grounded in a foundation of trust. “Being a Googler means holding yourself to the highest possible standard of ethical business conduct. This is a matter as much

practical as ethical; we hire great people who work hard to build great products, but our most important asset by far is our reputation as a company that warrants our users' faith and trust. That trust is the foundation upon which our success and prosperity rests, and it must be re-earned every day, in every way, by every one of us."

The code of conduct goes on for pages detailing all manner of potential evils to avoid, for example, dealing with competitors' private information. Here we see a return to the most basic code of conduct—the golden rule: "The level of business ethics to which we aspire requires that we apply the same rules to our competitors' information as we do to our own, and that we treat our competitors as we hope they will treat us. We respect our competitors and, above all else, believe in fair play in all circumstances; we would no sooner use a competitor's confidential information to our advantage than we would wish them to use ours. So, although gathering publicly available information about competitors is certainly a legitimate part of business competition, you should not seek out our competitors' confidential information or seek to use it if it comes into your possession. If an opportunity arises to take advantage of competitors' confidential information, remember: don't be evil. We compete, but we don't cheat."

Of course, I am well aware of the controversies that have arisen with Google's growth, including click fraud, the use of competitors' trademarked keywords in Google's AdWords advertisements, the inclusion of morally questionable content in Google Groups (most notably pornographic content and racial hate speech), copyright issues associated with Google's purchase of YouTube, and the high-profile case of Google in China, in which the company was forced to make concessions for the censorship of politically sensitive material to gain access into the country. Controversies of this nature are inevitable for any company that grows as rapidly as Google has, and no matter how lofty a company philosophy may be, perfection will always be an unattainable goal.

"Don't Be Evil" is a moral standard toward which to aim, not a sinless existence whose unattainability means no such norm should be invoked. The point of having moral codes—whether you are a hunter-gatherer or a consumer-trader—is to construct an environment of trust that encourages the expression of moral behavior.