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What People Are Writing About

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what people are writing about

BOOKS

The Great Wall Street Scandal by RAYMOND L. DIRKS and LEONARD GROSS, McGraw-Hill Book Company, New York, 1974, 295 pages, $8.95.

Chutzpah—that Yiddish word meaning unprecedented gall—is what this book is all about. For the Equity Funding case, unlike many other scandals that have rocked the financial world, was primarily a triumph of deliberate deception by the company—deception on so vast and deliberate a scale that the SEC, state insurance commissions, other insurance companies, even honest individuals involved in the machinations, literally wouldn't believe what was going on.

Yet the deception took everyone in, wary and sophisticated underwriters as well as gullible individuals. Everyone relied on everyone else: the state insurance commissions, or the SEC, or honest and reputable auditing firms. The insurance protective agencies of the various states did not check to see that the policies really existed and covered actual people. Nor did the New York Stock Exchange. It was the Captain from Kopenick story all over again, the tale of the retiring German tailor who got an Army captain's uniform, assumed it and the manner of a pre-World War I Prussian officer, and very nearly took complete charge of a small German village. The facade of Equity Funding was so impressive that no one checked to see if there were adequate foundations or anything behind the facade.

If any of the supervisory agencies, private or public, had even checked the origins of Equity Funding anywhere along the line, the career of the company and the catastrophic losses it caused, might not have occurred. The company evolved from the schemes of a motley group of five promoters: Mike

REVIEW EDITORS

In order to assure comprehensive coverage of magazine articles dealing with management subjects, MANAGEMENT ADVISER has arranged with seventeen universities offering the Ph.D. degree in accounting to have leading magazines in the field reviewed on a continuing basis by Ph.D. candidates under the guidance of the educators listed, who serve as the review board for this department of MANAGEMENT ADVISER. Unsigned book reviews have been written by members of the magazine's staff.

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Platt, Eugene Cuthbertson, Stanley Goldblum, Mike Riordan, and Gordon McCormick. McCormick, a Barnum and Bailey character more notable for high living than for any solid financial accomplishments, is generally acknowledged as the author of the idea that was to be the genesis of Equity Funding.

"Every dollar works twice"

Life insurance is good. Everyone needs it because of the certainty of death. Yet in a time of continued inflation, every dollar sunk in life insurance premiums is a dollar lost to diminishing purchasing power in the future. Why not buy a mutual fund in large quantities, then borrow against the value of the fund to invest in insurance? When the next fund policy payment fell due, pay it from the profits on the mutual funds. That way, every investor's dollar would work twice.

The holes in such a scheme should have been self-evident. The fact that they were not, to the thousands who invested in the scheme, speaks volumes about American naivete and greed. It speaks even more eloquently about the diligence of the regulating agencies that were supposed to be overseeing both the insurance and the mutual fund industries.

Finally, the conspirators who hatched the scheme fell out. Platt died of a heart attack in a New York bar. Riordan was buried in a California mudslide. Eventually, only Goldblum was left.

Goldblum was a cut above the others. Shrewd and intelligent, he could be impressive when the circumstances demanded it. He knew insurance and he also knew mutual fund sales.

And it was Goldblum who capped the first concept: every investor's money working twice; first to purchase mutual funds, then through loans on the funds to buy life insurance, with the final gimmick. That was to run up the profits of the conglomerate selling both funds and insurance to the point where it could afford to "purchase" other companies, and to add their profits to Equity Funding's, thus driving up the parent company's stock higher still.

But in 1969, with a general downturn in the stock market, Equity Funding's stock fell too. It no longer attracted enough eager individual buyers to run its stock to the point where it could be traded advantageously for another company's shares. Trouble was brewing in Paradise.

Strangely, the origin of this book was a visit paid to the author by a disgruntled employee of Equity Funding who had just been fired. The author, Ray Dirks, was a fairly well known insurance analyst on Wall Street. The ex-employee was Ron Secrist, a vice president for administration for Equity who had been working at an Equity subsidiary in New Jersey. He was suddenly summoned to Equity headquarters in Los Angeles to be informed that he was being fired as part of a general economy move.

What the company didn't realize was that Secrist had been suspicious of its way of doing business for a long time, had exchanged confidences with other employees who also thought something was very much amiss, and, at the very end, had actually been involved in some of the Equity machinations.

Together these scattered bits of knowledge amounted to a whole that was almost incredible. It looked very much as though the company were writing false insurance policies on non-existent people, recording them as legitimate sales, thus inflating their stock further, using the inflated stock to purchase legitimate companies, and then looting them.

To do this executives of the company would actually create false insurance papers by simply copying existing health records for one legitimate customer, combining them with financial information from another and, in effect creating an entirely new character. The work was done by a crew of not-very-bright clerks hired for this particular purpose who were told they were copying portions of existing records. Then company executives meeting secretly would use this cannibalized information to support new accounts on the company's computer records.

Equity's proudest boast

The proudest boast of the company was that its computer did not leave an audit trail—which it emphatically did not. The system had been deliberately designed so that it did not. The original records were there—assiduously assembled by the group of high school clerks. Entries had been made on the computer. These fake policies along with some real ones had been sold to reinsurers who, in most cases, didn't check on their authenticity any more than anyone else had.

Why hadn't Secrist, the ex-employee who finally went to Dirks, blown the whistle a long time earlier? He didn't think the insurance commissions of the various states would do anything. He didn't know too much about the SEC but he didn't put much faith in it either. When he finally went to Dirks it was in the thought of getting maximum publicity, since that would drive down the price of Equity stock, the surest way to destroy the company. Publicity also, he reasoned would force the state insurance commissions to investigate, which he wasn't at all sure would be the case if he went to see them privately.

Even Dirks was skeptical at first. It all seemed too impossible. But he talked to the head of one of the largest of Equity's five sales regions to find out how much business his salesmen had written during the year. He got an answer. Significantly it was far less than one fifth of Equity's reported earnings for the year.

Something was obviously wrong—in spite of the other insurance companies, the insurance commissions, and the SEC—with the financial reporting of the West Coast giant.

From that point on, it all unraveled—but not before Dirks was forced to change hotel rooms in Los Angeles three times on warnings that "the company" was out to get him. Perhaps the bitterest, most poignant note of all was struck by some unknown Equity Funding employee who penciled an anonymous note in a company facility:

"Thank God for Watergate!"

The Washington expose was breaking at the same time, and at least drew some attention away from the Equity Funding troubles.

In general, the atmosphere that produced both Watergate and Equity Funding seems to be the overwhelming note of this book. The sheer intricacy of the maneuverings in each case, the deviousness of many of the characters, the number of actors (this book has a cast of characters at the beginning reminiscent of a Russian novel)—all have more than a striking similarity to each other. The distrust of public institutions, the feeling that those charged with public responsibilities "wouldn't do anything about it," also characterizes both cases.

Product of its times

Dirks traces this to the atmosphere of the financial world at the time: an era of "go-go" funds, when a company's stock price was its most important asset, when corners could be cut and most often were, when "will it play in Peoria?" had become a national watchword denoting whether such and such an act could be gotten away with or not. Dirks himself was sued by various interested parties for divulging insider information because he had warned some friends and accounts to take it easy in investments in Equity Funding until his investigations—at that point purely informal — showed anything one way or the other.

This is a complicated but therapeutic book. Complicated because it is difficult to follow the involved machinations that Goldblum, McCormick, Platt, et al, devised to fleece their company's investors, therapeutic in the cathartic, Freudian sense. It shows us where we were just a short time ago—when whatever would sell was good, and honor, or honesty, was the last possible consideration.

Computer Crimes by GERALD MCKNIGHT, Walker and Company, New York, 1974, 221 pages, $6.95.

The growing relegation of power to the computer has made major crimes by the knowledgeable easier, this British reporter warns. He states the cases of some who have slipped and been caught and ponders how many crooks have gotten away leaving no traces.

If you are an expert in computer security, don't read this book because it adds much heat but little light. On the other hand, if you believe your installation can't possibly be the target of any evil force, this book may be for you. Its style is highly readable, if a bit sensational.

"The stakes, in the game of computer crime, are rising to a dangerous level. Anyone who now stands in the way of those determined to operate against the electronic world of data-processing is facing possible reprisals from criminal and hostile 'investors.' How easy it is to overstate this threat. Equally, it would be folly to ignore it," Mr. McKnight states.

He cites Alfonse Confessore as the "first electronic criminal to be murdered for his activities." Mr. Confessore was not a sinister systems analyst looking to rule the world, but a mechanic who managed to get hold of duplicate Diners Club cards and pass them on to gangsters.

But the author does tell some interesting stories without as much ballyhoo. The managing director of a big and successful British drug firm was one day approached by a representative of his EDP department and told, "I happen to know, sir, that if some of the men in the computer room don't see rises—double what we're getting now—right across the board, in the near future, then your invoices are going to suffer."

If the raises were not forthcoming, the men proposed to reduce all the invoices about 5 per cent. The manager called in a computer security expert. It would be cheaper to double the men's salaries than to suffer the markdown, and to bring the matter to the authorities would risk public confidence in the firm's computer-based operations. To do the invoices manually would also cost more than the raises and since the accounts would have to come out of the computer, they could be tampered with at that stage too.

The security expert advised that the raises be given, the invoices be sent out, and then the whole group fired. That was done. But Mr. McKnight questions what would happen if a similar sort of action took place once computer personnel are unionized.

"There will not, one imagines, be the need then for vulgar blackmail. For what corporation executive would be able to resist the demands of a deputation from his computer room if it not only possessed all power over the heartbeats of the business, but also was backed by closed-shop solidarity? It would be like a strike of iron-lung operators against polio victims."

No charges

Mr. McKnight tells of some hardware manufacturer's maintenance people who, allegedly, to twist management's arm in local union negotiations, tampered with a client's (a life insurance company) automated weather service. No charges were preferred against the suspects.

"From all of this, it may seem that if one is going to sabotage a computer for any reason, it is as well to be a paid-up member of a powerful union before attempting

to do it," the author wryly observes.

Just as charges were not pressed by either of these two harmed companies, other large corporations have kept silent about crimes committed against their computer operations.

"Because of what competitors, shareholders and loan-providers such as banks, might do if they found out that the company's costly computer had been broached, those in-the-know hush up scandal after scandal. How large a slice of the whole it represents one can only sense, but security experts with sealed lips and long memories talk of 'many more than get to be known about,'" Mr. McKnight states.

Rewards for corruption

An EDP-knowledgeable executive defrauded one company and, to prevent a scandal, left only after receiving additional compensation and a letter of recommendation. With that letter he went on to a second company and defrauded it too via its computer. His trail would have continued to a third company had he not broken the camel's back by asking for too much as a going away present, the journalist reports.

Mr. McKnight does offer some comfort to his readers, "In order to carry on a lasting, productive and systematic robbery of credit cards, or any other computerized sphere, criminals would need a well-run, well-managed operation, and this rarely exists in their society. It would have to be built on efficient, corporate lines. The likelihood of lesser, essentially hit-and-run, attacks is therefore very much greater."

Which group will win?

The author believes while some are busily employed in making systems more secure, the more greedy individuals in our society are looking for ways of getting to the computerized information. It is a question of which group will reach its goal first.

Security Procedures for Computer Systems by CHARLES F. HEMPHILL, JR., and JOHN M. HEMPHILL, Dow Jones-Irwin, Inc., Homewood, Ill., 1973, 251 pages.

If an institution is unable to afford an adequate computer security system, it is unable to afford a computer operation, these authors state. However, before making an investment in such a system, management should first avail itself of those basic deterrents and procedures that have proved effective in actual practice, the Hemphills say and give examples.

The Hemphills are an interesting team. Charles F. Hemphill, Jr., has been an FBI agent, worked on the investigative staff of the Attorney General of Utah, and is presently senior consultant in the Loss Prevention Division, the Wackenhut Corporation, Los Angeles. John M. Hemphill holds a Ph.D. in electrical engineering and has been involved in the management and operations of several large remote access computing systems. They seem to be the perfect pair for writing a book on computer security.

The book they have produced is far from technical. It provides many examples of what not to do and several common sense activities that can keep your installation from making the same mistakes. A few of the sensational newspaper stories about the destruction of data centers by students are repeated here. Checklists are included at the end of each chapter that can help management rate its own security program. The book may not give you startling new insights into data security, but perhaps a few of the hints will be useful.

For instance, don't plan your computer facility to be located near the firm's safe.

"There is frequently an unusual potential for explosion or fire in the area of business safes. This is because professional burglars sometimes utilize nitroglycerine or dynamite to blow open the safe, or cut into it with an acetylene-burning torch. Since these burglary techniques increase the possibilities of computer damage by explosion or fire, it is recommended that the computer be located at some distance from a company money safe. Since the acetylene torch is an unusual fire hazard under any circumstances, it is considered dangerous to allow welding in the vicinity of the computer."

The great magnet hoax

What about magnets? Remember the *Wall Street Journal* story that told of a group of boy scouts touring a computer center and unintentionally erasing company data because they were carrying magnets in their pockets? The authors point to the Stanford Research Institute study made in 1972 that found tape libraries are not as vulnerable to magnetic damage as some had claimed. Almost any magnet can be dangerous to computer data if brought into direct contact with magnetized data, but waving a magnet in the air in the direction of the tape library is not harmful. However, they point out that a tape does not have to be completely erased to be useless, just the destruction of a number of spots can cause it to have a "read error."

"In spite of the known dangers of all magnetic materials, recent business periodicals and computer magazines still contain advertisements of bulletin boards and wall charts with magnetic attachments, for use in computer areas. These devices utilize colorful markings and indicators, held in place on wallboards by magnetism. They are described as 'being helpful in flowcharting, book diagramming, Pert networks, and in charting business procedures and sales programs.' While these devices are undoubtedly of business value, if properly controlled, they should be looked on with skepticism in the computer center," the authors advise.

As an appendix, sample insurance policy forms are reproduced.

"In the final analysis, management has little choice but to utilize

whatever security seems reasonable, limited only by practical application and cost. To do otherwise is to jeopardize the very existence of the business or institution that relies on the computer," the authors conclude.

The Conscious Communicator by JOHN BRENNAN, Addison-Wesley Publishing Co., Reading, Mass., 1974, 191 pages, $7.50.

The author's basic idea—very sensible—is that good communications are based on good personal relationships, and that working relationships should in most respects, therefore, resemble personal relationships. Unfortunately, the author has drowned this good idea in a welter of overly discursive and unorganized thoughts on communicating and on supervising.

Books on communicating of late years have become progressively concerned with the human aspect of communicating as a reaction against the overconcern with technique, and this has been all to the good. After all, all of us spend most of our lives "communicating" and the kinds of communicating called for in the business or professional worlds are only one and not always the most complex of the aspects of communicating we human beings must master to get through life.

So these books suggesting a solution to our business communicating problems through a series of techniques are often quite misleading. Mr. Brennan's book is generally sensible about the issues and problems of communicating and supervising in a business environment, and his chapter heads and units are intriguing. He also has some amusing analogies and turns of thought as when he considers Adam's fall from the Garden of Eden as described in Genesis as an example of lack of communication between Adam and the Boss and the result: a typical Manager over-reaction. Part One of the book is entitled "Anyone Can Communicate Because Everyone is a Communicator." Part Two is entitled "Organization Climate: Mysteries, Myths and Models." Under Part One, we have some intriguing titles: "In the beginning was The Word . . . but no communication," "Retreat from Reality," "The Truth About Harry," and "A Personal Approach to Personnel Relations" and under Part Two: "Mysteries" and "Myths." But, alas, the intriguing titles and the sound idea are not borne out in the discursive and rather commonplace thoughts which follow, and it is not clear most of the time exactly to whom the author is speaking, though it appears that he is addressing middle management mostly.

Mr. Brennan is a consultant in communication and formerly manager-communication and public affairs at General Electric's Reentry and Environmental Systems Division in Philadelphia.

GEORGE DEMARE
Communications Adviser
AICPA

Measuring Corporate Strategy by CHARLES R. FERGUSON, Dow Jones-Irwin, Inc., Homewood, Ill., 1974, 120 pages, $9.95.

This book by a consultant hammers home the consultant's eternal theme: Problems involving techniques develop at a technological level and can best be solved there. Many serious problems, though, lie in the basic conceptual design of the company and are the fundamental responsibility of top management and its advisers. The basic problem is not how to improve a process but whether or not the process should be performed at all, what its true purpose is, what are its relationships to other areas of the corporation.

The author states his underlying theme on the second page of his book:

"A well-designed corporate conceptual framework provides the basis around which detailed and technical systems may be built. This framework must be very sound if the systems are to be sound. The framework also produces designs of organization structure, systems, facilities, and management which are complementary to each other in carrying out the work of the corporation. Because the conceptual framework is so basic to an effectively operating corporation, it seems obvious that managers should give careful attention to reexamining their company's conceptual design *before* shifting personnel and *before* installing advanced technology. That they do not is evident from the frequent instances of efforts to increase the efficiency of functions that should never have existed in the first place: programs to train managers in skills they will never need and compensation plans paying for executive qualities that have no value to the corporation."

The book, which is addressed to managers within the company rather than consultants, suggests that every manager consider conceptual design as a means of carrying out corporate strategy. "Strategy" Mr. Ferguson defines as the scheme or plan for achieving critical goals. For example, cost reduction might be a critical goal for a company. Strategies capable of achieving this might be building an automated plant, redesigning the product, reorganizing the plant management structure, or any combination of these. The point is that the critical goal must be established first, then the overall strategy for achieving that goal. Then the systems designer can come in to flesh out the concept, to work out the detailed plan by which it can be made real.

Review for consultant

The author, although addressing a hypothetical member of the management team, in effect gives a very brief overview of what every management consultant should ask himself when called on to do a corporate concept audit of his client.

Such a project may prove valu-

able even though the first approach to implementing a strategy may not work out. Mr. Ferguson gives as an example:

"A manufacturer of refinery equipment felt that in order to reach its goals for its share of a market it had to deal more with the design engineers and less with purchasing agents of its major oil company customers. The method used in carrying out this strategy was quite simply: to be more aggressive in making direct contact with the engineers and to get to know them better. Instead of improving the company's position, it worsened it by alienating both the purchasing agents and the engineers. The strategy was made to work by creating a highly specialized engineering and research group inside the company which could aid the customer design engineers in refinery design. The customer engineers recognized the value of the specialized design assistance they were able to get and requested assistance from the company's personnel, providing the contact needed at a critical stage in the competition for individual jobs."

Good strategy, poor tactics

Here the critical goal, gaining a larger share of the market, and the strategy for achieving it, getting a closer working relationship with customer engineers, proved valid. Only the first system developed, direct contact with company engineers, was at fault. The creation of an engineering and research group inside the manufacturing company which could aid customer engineers, and the overall strategy worked out well.

After defining his interpretation of a concept audit, Mr. Ferguson shows how such an audit might be conducted in five major areas of concern to management: the organization structure, management itself, management compensation, resource allocation and management, and, finally, the total corporation.

This book will reveal nothing new to experienced management consultants, but it may give them a few good ideas and it certainly gives them some convenient check lists. Perhaps its greatest value may lie in its potential as a gift to reluctant clients who are quite sure they don't have any problems a computer installation can't solve.

Affirmative Action for Women: A Practical Guide by Dorothy Jongeward, Dru Scott, and Contributors, Addison-Wesley Publishing Co., Reading, Mass., 1973, 334 pages, $8.95.

A practical "how to" guide, this book is on target in showing how managers and employees, of both sexes, can better utilize the talents of the 51 per cent of our population who are women.

Women are beginning to take new roles in many organizations—including stepping into jobs traditionally labeled "men's work." It is no longer a question of should women work or will women work but what can organizations do to provide equal opportunities for women. More and more women are entering the labor market and, in light of recently passed Federal and state laws dealing with discrimination in employment, most larger organizations are faced with the problem of establishing affirmative action programs to provide equal employment opportunities for women.

The book is a well-written, practical, and to-the-point collection of facts, workable concepts, comments, programs, and articles giving some insight and guidelines as to what useful courses of action organizations can take in implementing affirmative action plans. Practical steps for positive change are stressed. Specifically, it outlines what organizations need to do and are able to do in their Equal Employment Opportunity programs and also tells what they can do to assure corporate rights according to the new legislation. It is also a book for individual women now working or planning to work in organizations and offers original contributions from people actively involved in successful affirmative action programs.

In addition to describing how to organize and present affirmative action seminars for managers and supervisors and counseling seminars for career women, included is: (1) a clear interpretation of the laws affecting organizations and women, (2) the current place of women in government service and in organized religion, and (3) the unique problems of black women in organizations.

The seminar program developed and implemented by the Bank of America is described in detail.

The book, as was the intent in its design, should be a helpful reference source rather than a cover-to-cover reader.

Give & Take: The Complete Guide to Negotiating Strategies and Tactics by Chester L. Karrass, Thomas Y. Crowell Company, New York, 1974, 280 pages, $8.95.

This is a handbook, a set of rules to follow when in the process of negotiating an agreement, whether it be for the sale of a used car or a delicate diplomatic agreement between Israelis and Arabs.

According to the author, whose book jacket proclaims that he has "more than twenty years of major company buying and selling experience," the same techniques of playing from strength apply in each negotiating situation. There is always something someone wants and someone else wants—or at least is willing—to sell. How to find the common meeting ground?

This book considers almost every possible combination of circumstances that might arise in bargaining sessions and gives advice on how to deal with each. Some of the possible circumstances that

might arise are so simplistic they sound ludicrous; anyone with ordinary common sense should be able to foresee them and cope with them on his own. Others are more subtle and the advice given, though rudimentary in nature, is sensible.

The great advantage of the book is precisely its nature as a handbook. Each possible situation is encompassed in one brief example, usually no more than a page in length. Look up the situation you anticipate facing before your meeting and you go prepared for whatever the opposition may face you with.

Except, perhaps, the most intangible of all: Knowledge of the subject and all its nuances. The author pays lip service to this idea and in no case discounts knowing everything possible about the subject. But the idea of anyone entering diplomatic negotiations armed with only the advice rendered by this book is a little chilling. Better try it out on selling your car first.

Briefly listed

Guide to Corporations: A Social Perspective by the COUNCIL ON ECONOMIC PRIORITIES, The Swallow Press Incorporated, Chicago, 1974, 395 pages, $4.95.

How 43 corporations (in the chemical, automobile, steel, oil, paper, and airline industries) deal with the environment, equal opportunity, military contracting, and investment in Southern Africa.

MAGAZINES

Computer Models for Investment Analysis by HOWARD F. BLASCH, DONALD L. STRUVE, and NARAIN D. BHATIA, *Management Controls*, December, 1973.

As companies become more involved in investment activities, there is an increasing need for analysts to be able to make rapid and accurate comparisons and evaluations as a basis for management de-

Yes... you're a candidate for heart attack & stroke.

You can reduce your risk.
Don't smoke cigarettes.
Eat foods low in saturated fats and cholesterol.
Reduce if overweight.
Exercise regularly, moderately.
Control high blood pressure.
See your doctor regularly.
And support your Heart Association's programs of research, education and community service.

Contributed by the Publisher

cisions. This article describes how this need can be met by the use of a time-shared computer model known as PACE—Project Analysis by Computer Evaluation. The model substantially overcomes many of the limitations of traditional methods of analyzing the financial aspects of investment proposals.

A typical analysis of an investment or project involves simultaneous consideration of several sets of factors such as financing alternatives, tax implications, cash flows, and measures of project performance. All of these items are incorporated within the PACE model.

General steps

The usual steps to be taken when the PACE model is adopted include the following:

1. A description of the project is put together. The uncertain revenues, expenses, interest rates, salvage values, etc., are identified and a range of values established where possible.
2. The project is discussed with a PACE model specialist to determine the most effective way of formulating the problem to minimize the cost of collecting raw data and conducting the analysis.
3. The data are collected and critical assumptions are reviewed.
4. The data are entered and set up on the project file. Initial reports are then produced on-line and tested for reasonableness.
5. A sensitivity analysis is conducted wherein "what if" questions are asked. At this stage, the thrust of analysis moves away from computation to generation and evaluation of new alternatives as well as quantification exposure under different assumptions.

Time-phased cash flows

The investment project itself is completely specified by time-phased cash flows into and out of the project, taking into account various financial, accounting, and tax parameters. PACE model inputs include operating cash flows (revenues, expenses, and working capital), asset purchase cash flows, depreciation policies, types of financing, and tax information. These project data are entered into the model by responding at the time-sharing terminal to a sequence of requests from the program.

Model outputs

The outputs of the model include cash flow statements, income statements, depreciation schedules, financial repayments, and project evaluators such as net present value, yield, cumulative cash flow, and return on investment.

The flexibility of the PACE model makes it applicable to a wide variety of situations such as the evaluation of venture capital and loans, real estate promotion, syndication alternatives, financing alternatives, and lease vs. buy decisions. It allows for sound business judgment backed by speed and accuracy in quantitative analysis.

RICHARD BOES
Michigan State University

In Praise of Those Who Leave

by SAUL W. GELLERMAN, *The Conference Board Record*, March, 1974.

Personnel turnover is usually considered a headache to most organizations, but is it the monster it appears?

A number of distinct advantages accrue to the business with high turnover rates, the author points out. When a vacancy arises, management may fill it with a better trained, better qualified person while offering an opportunity for dissatisfied, and often under-productive, employees to find work elsewhere.

Turnover also offers financial advantages. Ordinarily, the longer an employee remains with the organization, the smaller his increases in productivity. Thus, management may be paying more and more for less and less. A high turnover rate alleviates this problem by encouraging employees to leave before their salary begins to rise faster than their productivity. High turnover also reduces pension fund costs when the benefits do not vest in the employee. The additional funds created when an employee leaves could be used to increase benefits for the more productive employees, or effect a cost savings to the company.

Turnover benefits

High turnover may enhance a company's "employment image." To increase their marketability, graduates often seek the employer who offers the best training program. After they have gained the necessary expertise, these employees may look for employment elsewhere at a higher salary. But both parties will have benefited—management gets to examine the new talent while the employee receives his desired training.

Finally, high turnover is economically beneficial since it promotes a more efficient allocation of labor resources. In a labor market with fewer obstacles, men can more easily shift to positions where their productivity is greatest.

Groups with greatest turnover

Employee turnover is concentrated in two groups: young people (under age 30) and middle-aged people (age 35-45). High voluntary turnover among youths is primarily attributed to the qualities of youth itself—the wanderlust, no permanent commitments, and the fact that youths usually get the least desired assignments. Turnover in this group can be expected to remain relatively stable since these conditions will most likely remain unchanged.

But higher turnover among the middle-aged is a different matter.

As the average age of the population increases, more employees will enter this age group causing even higher turnover.

Three "stable" groups

Who, then, are the employees who remain? Generally, they can be divided into three groups: (1) the "umbilical" types who will never leave before retirement; (2) the contented person who could become discontented; and (3) the reluctant type who really would like to leave, but hasn't a better offer. Of these three, the "reluctants" are the most important to management since they could most easily become defectors.

Identifying "reluctants"

Management should attempt to identify reluctants and classify them into one of the following three categories: replaceable, unclear, or irreplaceable. Most personnel are "replaceables" and should be allowed to leave. Only when the company is failing to recover training costs should it attempt to reduce turnover of "replaceables." The second category, the "unclear" group, should include those with conflicting evidence in their performance report. But the third group, the "irreplaceables," is the one where management should concentrate its efforts. "Irreplaceables" should be actively recruited. After an "irreplaceable" defects, informal ties should be maintained to determine his progress in his new position, and if he becomes dissatisfied with his new job, the company may wish to reacquire his talents.

A high turnover rate is here to stay: for this reason, companies should manage it as effectively as possible. The system in use today discourages turnover. Instead of enticing many lackadaisical, "replaceables" to stay, management should encourage employees to examine their future with the organization. When the employment arrangement becomes unsatisfactory to either party, the employee should be encouraged to look for work elsewhere.

Management should actively promote policies which support this point of view. Fully-vested, portable pensions should be considered. Salaries should be tied to productivity with only the "irreplaceable" receiving more than the going pay rate. Voluntary turnover should be carefully managed, departures timed to coincide with the termination dates of large contracts and replacements recruited to fill the vacancy. Perhaps even a placement service could be maintained to relocate dissatisfied personnel.

All of these policies help create a healthy attitude toward turnover. Employees dissatisfied with their work should not be enticed to remain. Why burden the organization with disgruntled, underproductive workers when talented, enthusiastic workers may be recruited to fill their places? Turnover can be managed effectively, Mr. Gellerman concludes.

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Foreign Markets—Another and Closer Look by J. RUSSELL DOWNEY, *Management Controls*, June, 1973.

Many companies are capable of exploiting the opportunities available in foreign markets, but hold back in the mistaken belief that such operations are beyond their capabilities. This article notes specific credit services available through the Export-Import Bank of the United States (Eximbank) and outlines other considerations relevant to entering foreign markets.

Eximbank has a broad range of programs designed to promote foreign operations. It operates a direct lending program in cooperation with private financial institutions whereby the buyer may finance up to 90 per cent of the purchase through Eximbank and a commercial bank. Eximbank will usually take the later maturities, thus enabling the commercial bank to be repaid first; because Eximbank's interest rates are generally lower, the overall cost to the borrower is reduced. This direct lending program is intended mainly for financing large capital equipment sales with long-term repayment schedules.

Guarantees foreign notes

Under the Exporter Guarantee Program, Eximbank will guarantee the repayment of foreign purchasers' notes to commercial banks which have financed foreign sales of U.S. suppliers. The Eximbank guarantee covers both commercial and political risks, thereby enabling the American supplier to enjoy the benefit of cash sales. The Exporter Insurance Program provides similar protection against nonpayment for the exporter who wishes to supply his own credit.

Financing exports is facilitated by the Discount Loan Program under which Eximbank lends commercial banks up to 100 per cent of the value of their export paper. This program assures commercial banks that export financing will not adversely affect their liquidity even during periods of high interest rates and liquidity shortages.

The Cooperative Financing Facility Program provides credit financing primarily for small- and medium-size firms which may lack experience in foreign credit financing. Through this program, Eximbank will arrange with private foreign financial institutions to jointly finance purchases from U.S. firms.

For the firm contemplating its financing needs pursuant to making foreign sales, Eximbank will at no cost specify the nature, the amount, the terms, and the conditions of support it will provide. To add flexibility this service is offered with no binding commitment on the part of the firm; Eximbank's commitment can be used in total, in part, or not at all.

In addition to credit serviced

through Eximbank, the Department of Commerce provides information on exports by commodity and product lines through its Bureau of International Commerce. Similar statistics on population, industry growth rates, and exports and imports are available through government ministries of most foreign countries seeking American technology and other products.

Prerequisite for investments

Mr. Downey notes that foreign operations should be undertaken only after comprehensive market studies by analysts familiar with the environment. For those firms contemplating direct foreign investment, familiarity with labor and other laws and U.S. and foreign taxes is particularly important. The Foreign Trade and Investment Act, the Office of Foreign Direct Investments of the Commerce Department, and the Sherman Anti-Trust Act also apply to U.S. companies operating abroad. And because foreign financing markets vary considerably, knowledge of relevant practices is needed with regard to interest rates, utilization of overdrafts, and other financial practices.

Although the considerations are many and complex, the opportunities seem to outweigh the obstacles as evidenced by the continued growth of foreign operations.

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Accounting and Behavioral Science: Some Interrelationships by CLARK E. CHASTAIN, *Michigan CPA*, November-December, 1972.

In recent years, interest has grown in the implications of the behavioral sciences for accounting. This article provides a survey of the area, including definitions of terms and topics of current interest.

Clark Chastain has provided us with a very intelligible and provocative discussion of the relationship between accounting and the behavioral sciences. He has examined some of the key issues involving accounting and the behavioral sciences, and has concluded that accounting researchers and practitioners must be acquainted with, use, and incorporate findings from the behavioral sciences.

The remarkable correspondence between the history of accounting and the behavioral sciences is brought out in the first section of the article. The initial writings on human behavior and the initial practice of accounting concurrently occurred around 5,000 B.C. Both accounting and the behavioral sciences became formal disciplines in the nineteenth century. But despite their parallel development, accounting benefited little from the behavioral sciences until the twentieth century.

Following the lead of the management profession, in the 1950's the accounting profession began to recognize the impact of human and social factors on accounting. Interest accelerated throughout the 1950's and 1960's and included research on the behavioral consequences of accounting actions (such as budgets and audits) and calls for the training of accountants in the behavioral disciplines.

Natures of various sciences

The natures and interrelationships of science in general, the social sciences, the behavioral sciences, and accounting are discussed in the next section. Science is defined as a body of systematic knowledge while the social sciences are sciences concerned with the activities of man. The behavioral sciences are those social sciences concerned with the behavior of man and are usually limited to the core disciplines of anthropology, psychology, and sociology. Whether management is a behavioral science and whether accounting is a social science are issues in much dispute, but the need for the application of the core behavioral sciences to both management and accounting is unquestionable.

The behavioral sciences are relevant to accounting on both the input and output sides. On the input side, accountants measure aspects of human behavior. Individual transactions are the result of human actions, and overall performance measures, such as income, are the measures of the cumulative behavior of individuals or groups. On the output side, accounting measures, such as those found in financial statements, influence behavior in both anticipated and unanticipated ways. Thus far, the major implications of the behavioral sciences for accounting have been to discover these unanticipated consequences and modify accounting measures to better achieve organization goals.

Clinging to obsolete

Chastain discusses many of the implications of the behavioral sciences for accounting. Because of the behavioral impact of accounting, he argues that accounting should extend its scope to the communication of nonfinancial as well as financial information. Much of the literature on behavioral science applications to accounting concerns the failure of accounting controls to effectively motivate employees to accomplish organization goals. Accountants and designers of accounting control systems are accused of making obsolete assumptions about the behavioral consequences of accounting measures or even failing to consider these consequences. Such failures have resulted in much hostility directed towards accountants. In addition, the failure to produce accounting measures which facilitate adjustment of organizations to changing environmental conditions results from accountants' clinging to the obsolete closed-system concept of organizations.

All of the above lead to Chastain's conclusion that accountants must be knowledgeable in and utilize behavioral science findings.

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