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The cesspool syndrome: How dreck floats to the top of declining organizations

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Executive Overview

In contrast to successful organizations, in which cream rises to the top, organizations falling victim to decline often suffer from the "cesspool syndrome," wherein, figuratively speaking, dreck floats to the top. In declining organizations, the early departure of qualified employees will inhibit recovery and, if unchecked, can accelerate decline.

It has become abundantly clear over the last 15 years that organizations must continually renew themselves if they are to survive and prosper. Indeed, intricacies of the renewal process as experienced by myriad organizations over this period have been repeatedly catalogued and documented.[1] For many organizations, renewal has involved downsizing in an effort to forestall or reverse decline. Despite the glut of guides on how to or how not to downsize, untold organizations continue to make hasty decisions that haunt their bottom lines.[2] All too often, downsizing becomes dumbsizing, as uninformed organizations fail to understand the relationship between short-term cost-cutting and long-term prosperity.[3]

Based on over twelve-years' observation and involvement with a broad spectrum of distressed private- and public-sector organizations, we wish to suggest that a unique and unrecognized dynamic common to many organizations that have downsized may partially account for their difficulties. This cesspool syndrome is no less significant than the strategic concerns that have been widely addressed by others.[4]

We wish to stress that the following comments apply specifically to organizations that have downsized in response to decline and not to those that have used downsizing intentionally to enhance their efficiency or effectiveness. In this sense, our comments are primarily directed at organizations that have implemented downsizing as a defensive reaction to decline rather than as a voluntary strategy to bolster performance. This distinction recognizes that downsizing and decline are separate concepts. Organizations can downsize without declining and vice versa.[5] The percentage of companies that downsize to enhance competitiveness rather than to respond to deteriorating performance is unknown.[6]

Those Who Can Go, Go

When an organization downsizes, by definition, it reduces its number of employees. At the same time, it has been noted that both involuntary and voluntary turnover typically increase in declining organizations.[7] The current emphasis on downsizing has led some observers to describe such restructuring as "organizational anorexia."[8] Not only do fewer employees remain to perform the same functions, the most competent (hence, the most mobile) employees are often the first to leave.[9]

In a Louis Harris and Associates study of 406 restructured companies, one out of every five reported losing the "wrong people," that is, valuable contributors with critical skills or needed talents, following downsizing.[10] Rather than have their records marred by failure, many of those most qualified to turn around a declining organization choose instead to seek more attractive employment alternatives.[11] Especially in the case of employees with high-demand skills, those who can go, go; those who can't, stay. This appears to be particularly true for qualified managers unfettered by the golden handcuffs of pending retirement, family or social ties to a community, or an emotional investment in an organization's success. With the early departure of its most qualified managers, a declining organization can expect that its recovery will be inhibited, or its decline accelerated.[12]

Anxious Marplots and Meddlers

The all-too-likely consequences of this dynamic go far beyond the immediate effect of placing an organization at a serious competitive disadvantage. A potentially devastating secondary effect is on an organization's ability, over time, to successfully reverse its decline. As assuredly as Gresham's law specifies that bad money drives out good money, incompetent managers, wherever situated, inevitably drive away competent employees. This occurs both internally and externally. Internally, incompetent management is a further impetus for an organization's most mobile and competent employees to move on to more attractive career opportunities. Moreover, with their more qualified employees departing, many declining organizations may actually hasten their anorexic death spirals by reducing their training budgets at the very time when remaining employees are likely to need more training.[13]

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Viewed externally, incompetently managed organizations, by their nature, repel qualified job candidates for two reasons.[14] The cynical nature of such organizations makes them less attractive to all except those with few employment alternatives. Moreover, there is a common, although seldom acknowledged, perversion inherent in declining organizations. Fearing for their own place, those employees bound by their own inadequacies to a failing organization typically feel threatened by bright job candidates. Such new blood may not only further disrupt the status quo, but also speed up the competition for whatever limited resources remain. In such a work setting, it is not uncommon to find anxious marplots and other meddlers discouraging or even blackballing promising job applicants in favor of nonthreatening also-rans. This circumstance becomes especially malevolent when anxious strivers and invertebrate accomplices appear in an organization's hierarchy and, consequently, inhibit reform.[15] This scenario lends credence to the twin observations that turkeys will hire only more turkeys[16] and that successful turnarounds require either the replacement of top-level management or a substantial change in the learned behavior of an existing management team.[17]

Rainmakers and the Double Whammy

Self-serving defensive actions of some incumbent employees can lead to their own short-term benefit. But left unchecked, these actions ensure an organization's long-term failure and, in turn, that of its employees. This explains why one noted consequence of decline is its effect on the rate of organizational innovation.[18] Whereas some organizations appear able to generate significant innovations in the face of decline, others seem paralyzed by a fear of failure. Even more distressing, if an organization's most valuable employees—those rainmakers most likely to come up with innovations—are the first to leave, their new employers soon capture market opportunities that could have been realized by their old employers. In circumstances where the two employers are in the same marketplace, such a brain drain represents a double whammy. The declining organization loses its most valuable employees, and supplies value to its competitors.[19]

The Cesspool Syndrome

A properly maintained cesspool will cleanse itself as it digests waste materials and processes menthane gases. If compromised, however, dreck at the bottom of a cesspool will rise to the top and sludge will form below. In a similar manner, unless declining organizations are properly sustained and their most competent employees retained, those remaining will be among the least qualified to provide its future direction. The all-too-predictable outcome, in either a cesspool or declining organization, is a stinky and costly mess.

Organizations most likely to fall victim to the cesspool syndrome are those at least partially protected from immediate market conditions. These include public organizations, such as government agencies, universities with ensconced tenure systems, city schools, the armed services, and governments, as well as public- and private-sector organizations saddled with inactive oversight boards or commissions.[20]

Unlike private-sector organizations that receive income only when they provide a good or service that customers want or are willing to exchange for their purchasing power, public agencies are paid from budget allocations. As a result, there is only a loose relation between a public agency's performance and the costs of its operations. In such situations, the criteria for measuring effectiveness are generally either altruistically or politically based. Consequently, goals are not necessarily either stable or agreed on and administrators are free to bumble along without attempting to survey possible alternatives for achieving superior performance, let alone being held accountable for such performance. Indeed, for most public-sector organizations, performance means increasing next year's budget, which is a direct function of this year's expenditures. Whereas those who approve such budgets may hope for prudence in spending, such a system rewards not economy, but spending.[21] Thus, perversely, the behavior desired is not being rewarded, but discouraged.

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Restless Boards

The role of responsible oversight in remedying the cesspool syndrome is slowly becoming recognized as more and more CEOs have felt the sting of increasingly restless boards, disgruntled employees, and impatient stockholders. The departure of Trans World Airlines CEO Jeffrey Erickson, following serious losses and the exodus of senior management, seems a case in point.[22] Prompted by complaints from dissident executives concerning his refusal to replace certain managers and his relaxed management style, Erickson stepped down under board pressure. Elsewhere, however, given the presence of acquiescent private-sector boards, and the political composition of most public-sector commissions, one can easily understand how the cesspool syndrome persists, with only second-best big chunks floating to the top. During the downward spiral of the now defunct retailer the W. T. Grant Company, President Richard C. Mayer and Chairman Edward Staley (founder W. T. Grant's brother-in-law) centralized all decision making, actively discouraged differing opinions, and essentially controlled the Grant board.[23] In effect, no system existed for introducing changes to overcome what became a terminal disease.

This last example highlights the difference between idealized beliefs about corporate governance and what actually prevails in some cases. Retired Illinois Central Railroad chairman, president, and CEO Harry J. Bruce scoffs at the notion that boards of directors are the supreme power in the typical corporation.[24] He holds that most U.S. boards are subordinate to management, with directors owing their positions and compensation to the corporation's CEO. Bruce suggests that this is especially true in the 75 percent of U.S. corporations in which the CEO and the chairman are the same person. In many such corporations, as *Business Week* notes, boards are "little more than a claque of the CEO's cronies, [who] quietly nod and smile at their buddy's flip charts and rubber-stamp his agenda for the corporation."[25]

Avoiding the Cesspool Syndrome

Organizations in both the private and public sectors would be wise to develop downsizing strategies that identify those star performers they wish to retain.[26] An organization's ability to survive and prosper will depend on its ability to retain these most talented employees who have the greatest career mobility and, moreover, will likely be the hardest to replace.[27] Because a declining organization's employees can be expected to be concerned with their continuity of employment, deriving their explicit career paths would seem to be commonsensical.[28] Amazingly, however, according to a Right Associates study of over 900 downsized organizations, only 26 percent reported telling survivors the criteria used to determine who would go and who would stay. Equally dismaying, only half reported informing survivors of their current and future roles and responsibilities.[29]

The implications of a declining organization's loss of its most valuable employees must be incorporated into its strategic planning process.[30] The failure to account for this loss may well explain why some organizations suffer from lower productivity and further decline after downsizing. Although it is the responsibility of all managers, regardless of circumstance, to nurture those employees on whom an organization's future depends, during a period of decline is especially vital for avoiding the cesspool syndrome.

An Agenda for Future Research

At present, there are numerous unresolved controversies about how organizations adapt to decline.[31] Thus we are unable to offer either a theoretical system applicable to the cesspool syndrome or data-driven models from which statistical inferences can be drawn. Yet observations such as we have provided are an essential initial stage for defining the cesspool syndrome as a substantive construct. These initial observations are a necessary precursor to stating and testing hypotheses concerning conditions that foster its development.[32] Only after first getting a descriptive hold on the cesspool syndrome will researchers then be able to empirically explore what kinds of people it affects, under what circumstances, and with what consequences. To stimulate consideration of the dynamics underlying the cesspool syndrome, we pose some questions for future research:

- **How can declining organizations best renew themselves if they are to survive and prosper?** Recent figures suggest that downsizing is expected to be a substantial challenge far into the future. Organizations continue to cut jobs and employees remain concerned about their careers.[33] Research yielding a fuller understanding of the intricacies of the renewal process is needed so that hasty decisions giving rise to the cesspool syndrome can be avoided. More specifically, prospective studies are needed to follow individuals and organizations that fall victim to the cesspool syndrome so as to facilitate managerial understanding of the complex relationships that exist among the goals of reduced costs or improved profits and employee attachment and workplace commitment. Unlike retrospective studies based on historical data, longitudinal research could observe the processes that avoid the cesspool syndrome.
- **How best can organizations that have fallen victim to the cesspool syndrome reverse its underlying dynamic?** At the heart of reversing the cesspool syndrome is the need for an organization to retain its remaining qualified employees, and to attract new employees with the skills necessary for its survival and eventual turnaround. Keeping and attracting star performers is thus essential. To date, researchers, for instance, have focused little attention on understanding why the very people needed to rescue a declining organization are the first to circulate their resumes.[34] Keeping star performers obviously requires communication, but how to communicate effectively in an organization that is no longer functioning well is a topic likewise ripe for research.[35] Such communication must simultaneously strengthen trust and facilitate change without undermining credibility and fostering animosities between the departments, teams, and employees an organization is counting on for direction after a downsizing effort.

  Research is also needed to help managers avoid knee-jerk reactions incorporating the latest downsizing fads and quick-fix solutions. Such actions may be expeditious in the short term, but can be disastrous for maintaining long-term employee attachment and workplace commitment. Indeed, quick use of fads may communicate that an organization has turned on its own employees, falling victim to what may be a form of a yet undiagnosed autoimmune disease that further hastens the cesspool syndrome.
- **How can organizations best use training, performance appraisal, compensation, and other human resource programs to minimize the presence of employee dreck?** As noted, a perversion inherent in declining organizations is that employees bound by their own inadequacies to a failing organization typically feel threatened by bright job candidates. Unfortunately, there is little research on the effectiveness of alternative mechanisms for dealing with this perversion. Case studies, cross-sectional studies, and longitudinal studies are needed to answer fundamental questions about which human resource practices work and which don't work to best prevent dreck floating to the top of an organization and sludge forming below.

  The initial hiring and continued training of qualified employees, for example, should be one means for avoiding the later presence of anxious strivers. Similarly, a reliable and valid performance appraisal system should help guard against the retention of incompetent managers who, wherever situated, inevitably drive away competent employees. Likewise, a sound compensation program that clearly links pay and performance should be an important means for retaining star performers. To expand conceptual and empirical knowledge about the effects of the cesspool syndrome, management researchers are encouraged to explore the efficacy of alternative human resource practices in declining versus healthy organizations.
- **How can governance at the board level be improved to protect organizations from being victimized by the cesspool syndrome?** An effective response to the syndrome requires an understanding of boards of directors that fail to curtail governance practices that protect incompetent top managers and otherwise leave them unaccountable to shareholders. Research suggests that many organizations that have downsized did not anticipate the challenges that would follow. A 1990 AMA survey of 1,142 downsized companies found that more than half had begun downsizing without programs to minimize the

inevitable resulting disruptions.[36] Boards that allow such situations to develop and then permit underperformance and decline foster the conditions that create the cesspool syndrome. The whole question of board-level governance in declining organizations needs to be empirically investigated. Specifically, management researchers need to become more involved in the study of good governance and to focus their attention on relations among an organization's directors, its shareholders, and its management so as to gain a clearer understanding of the diligence required by each in assuring that the cesspool syndrome doesn't claim another victim. It would be particularly interesting to know why some boards have the cojones to cross swords with incompetent topsiders and others don't.

Conclusion

Downsizing, a worldwide phenomenon, is a challenge that is likely to continue for years and, indeed, may become a permanent feature of organizational life.[37] Management researchers and practitioners therefore need to apply their analytic skills to understanding the effects of downsizing on organizational practices. The cesspool syndrome is perhaps one of many unintended negative consequences that will be confronted by managers attempting to right floundering organizations. Its deleterious impact on organizations and their employees creates an important opportunity for management researchers to make a significant contribution to understanding the dynamics of sustained economic success.

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Endnotes

[1] For an analysis of why organizations downsize, see McKinley, W., Sanchez, C. M., & Schick, A. G. 1995. Organizational downsizing: Constraining, cloning, learning. *Academy of Management Executive*, 9(3):32–42. A summary of what is known of the economic and organizational consequences of downsizing is presented in Cascio, W. F. 1993. Downsizing: What do we know? What have we learned, *Academy of Management Executive*, 7(1):95–104. An analysis of alternatives to downsizing appears in Perry, L. T. 1986. Least-cost alternatives to layoffs in declining industries, *Organizational Dynamics*, 14(4): 48–61. Perry offers human resource guidance in making layoff decisions in his 1985 article, Cutbacks, layoffs, and other obscenities: Making human resource decisions, *Business Horizons*, 28(4): 68–75.

[2] The bottom-line, as well as the cultural downsides of downsizing, are analyzed in *Los Angeles Times*. 1995. Corporate anorexia may wind up being fatal. November 8:B11; and *Chicago Tribune Magazine*. 1996. Downsizing won't work. April 14:15–16.

[3] For a report on organizations whose downsizing decisions have been flawed, see *Wall Street Journal*. 1996. Call it dumbsizing: Why some companies regret cost-cutting. May 14:A1 and A6.

[4] See, for example, Bruton, G. D., Keels, J. K., & Shook, C. L. 1996. Downsizing the firm: Answering the strategic questions. *Academy of Management Executive*, 10(2):38–45 and the references therein.

[5] More on the distinction between downsize and decline can be found in Freeman, S. J., & Cameron, K. S. 1993. Organizational downsizing: A convergence and reorientation framework. *Organization Science*, 4:10–29.

[6] Information on the relationship between downsizing and productivity is contained in *Business Week*. 1997. Big payoffs from layoffs. February 24:30.

[7] Greenhalgh, L. 1983. Organizational decline. *Research in the Sociology of Organizations*, 2:243; and Greenhalgh, L., Lawrence, A. T., & Sutton, R. I. 1988. Determinants of work force reduction strategies in declining organizations. *Academy of Management Review*, 13:241.

[8] *Wall Street Journal*. 1995. Some companies cut costs too far, suffer "corporate anorexia." July 5:A1 and A5.

[9] For a discussion of specific organizations trying to rebuild employee loyalty after downsizing, see *Wall Street Journal*. 1996. Some companies try to rebuild loyalty. September 27:B1 and B7.

[10] This study is reported in Marks, M. L. 1993. Restructuring and downsizing. In P. H. Mirvis (Ed.), *Building the competitive workforce*: 76. New York: Wiley; and Mirvis, P. H. 1997. Human resource management: Leaders, laggards, and followers. *Academy of Management Executive*, 11(2):43–56. Evidence suggests that this phenomenon affects both private- and public-sector organizations. See, for example, *Business Week*. 1993. Take the money and run—or take your chances. August 16:28–29; *Wall Street Journal*. 1995., *op. cit.*, *Industry Week*. 1996. The bureaucracy: Downsizing effects. October 21:17.

[11] A conceptual framework for guiding career development in downsizing organizations is presented in Brockner, J., & Lee, R. J. 1995. Career development in downsizing organizations: A self-affirmation analysis. In M. London (Ed.), *Employees, careers, and job creation: Developing growth-oriented human resource strategies and programs*, 51. San Francisco: Jossey-Bass.

[12] See Greenhalgh, 1993, 243. For further affirmation of this result, see Whetten, D. 1980. Sources, responses, and effects of organizational decline. In J. R. Kimberly, R. H. Miles, and Associates, *The organizational life cycle*, 369–370. San Francisco, Jossey-Bass.

[13] This unintended consequence is discussed in the *Wall Street Journal*, 1996. *Op. cit.* and Cameron, K. S., Freeman, S. J., & Mishra, A. K. 1991. Best practices in white-collar downsizing: Managing contradictions. *Academy of Management Executive*, 5(3):57–73.

[14] This point is underscored by a study reported in Useem, M. 1993. Management commitment and company policies on education and training. *Human Resource Management*, 32:421–422.

[15] This observation was perhaps first noted in Parkinson, C. N. 1957. *Parkinson's law and other studies in administration*. Boston: Houghton Mifflin, 78–90.

[16] *Wall Street Journal*. 1995. Letters to the editor: Family name on door shaped firm's morality. June 27:A15.

[17] Bedeian, A. G. 1984. *Organizations: Theory and analysis*, 2nd. ed. Hinsdale, IL: Dryden, 342.

[18] This effect is treated in Whetten, op. cit., 370–371; and Greenhalgh, op. cit., 1993, 244.

[19] For confirmation of this occurrence, see *Wall Street Journal*. 1996. May 14:A1.

[20] Additional discussion of this point as it relates to different organizational contexts appears in Drucker, P. F. 1974. *Management: Tasks, responsibilities, and practices*. New York: Hayes & Row, 137–147; *Financial World*, The downsizing of academia. March 15:46; *Wall Street Journal*. 1996. Letters to the editor: The great migration of 'Einsteins'. September 24:A19; and *Wall Street Journal*. 1996. Still the noblest calling. May 24:A10.

[21] Steven Kerr's *AME* classic documents this folly, see Kerr, S. 1995. On the folly of rewarding A, while hoping for B. *Academy of Management Executive*, 19(1):7–14.

[22] This case is reported in *Wall Street Journal*. 1996. Lessons from CEOs no crisis can unseat. October 31:B2 and B9.

[23] The W. T. Grant Company saga is chronicled in Weitzel W., & Johnson, E. 1991. Reversing the downward spiral: Lessons from W. T. Grant and Sears Roebuck. *Academy of Management Executive*, 5(3):7–22.

[24] For further details of Bruce's argument in this regard and a corporate governance perception/reality checklist see *Directors & Boards*. 1997. Duty, honor, company. 21(2):12–19.

[25] *Business Week*, 1996. The best & worst boards. November 25:82.

[26] Guidance in this regard is provided in Brockner, J. 1992. Managing the effects of layoffs on survivors. *California Management Review*, 34(2):19.

[27] For an early statement on this point, see Levine, C. H. 1979. More on cutback management: Hard questions for hard times. *Public Administration Review*, 39:181.

[28] This notion is further developed in Greenhalgh, L., & Rosenblatt, Z. 1984. Job insecurity: Toward conceptual clarity. *Academy of Management Review*, 9:443, and Brockner, op. cit., 26.

[29] This study is reported in *Working Age*. 1995. Companies report decline in employee morale among survivors of downsized companies. 11(1):2–4.

[30] For strategic models that can be used to guide downsizing decisions, see Applebaum, S. H., Simpson, R., & Shapiro, B. T. 1987. The tough test of downsizing. *Organizational Dynamics*, 16(2):68–79; and Kozlowski, S. W. J., Chao, G. T., Smith, E. M., & Hedlund, J. 1993. Organizational downsizing: Strategies, interventions, and research implications. *International Review of Industrial and Organizational Psychology*, 8:264–332.

[31] McKinley, W. 1993. Organizational decline and adaptation: Theoretical controversies. *Organization Science*, 4:1–9.

[32] For more on the fundamental interdependence between description and explanation in the social sciences, see Bentler, P. M. 1978. The Interdependence of theory, methodology, and empirical data: Causal modeling as an approach to construct validation. In D. B. Kandel (Ed.), *Longitudinal research on drug use*: 267–302. Washington, DC: Hemisphere.

[33] For more on job anxiety resulting from widespread downsizing, see *Business Week*. 1997. Who says job anxiety is easing? April 7:38.

[34] For more on the needs of those who survive downsizing initiatives, see Caplan, G., & Teese, M. 1997. Survivors: How to keep your best people on board after downsizing. Palo Alto, CA: Davies-Black.

[35] Kozlowski, Chao, Smith, & Hedlund, op. cit., 291–293.

[36] For further details of this study, see Mroczkowski, T., & Hanaoka, M. 1997. Effective rightsizing strategies in Japan and America: Is there a convergence of employment practices. *Academy of Management Executive*, 11(2):8.

[37] *Ibid.*, 57.

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Executive Commentaries

Editor's note: AME invited commentary from business practitioners on *The cesspool syndrome: How dreck floats to the top of declining organizations.*

June Delano
Eastman Kodak Company

Authors Bedeian and Armenakis describe one of the conundrums of organizational life: good management is the key to successful downsizing, yet organizations in decline are rarely well-managed. When these organizations decide to reduce their employee population, they invariably do it in a way that creates more problems and contributes to their downward spiral.

The loss of the talent that is needed for turnaround is a devastating consequence of poorly executed downsizing, and yet it is avoidable by the kinds of measures the authors suggest. Unfortunately, companies in trouble have rarely laid the groundwork for successful downsizing and they do not usually have the management talent to downsize well.

The groundwork consists of two things: building employee loyalty and trust, and having clear performance measures in place. A loyal workforce gives management a safety margin of good will